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CORRECTION APPENDED

**YOUR MONEY**; Today's Lesson: Rethink College Funds  
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It seems miserly, immoral and guaranteed to make your children more resentful than they normally would be, but saving for their college education is the last thing you should be doing.

Save for your own retirement and, then, if there is anything left, put something aside for them.

It may sound like crazy advice, tossed off just to get your attention, but the recommendation is well within the mainstream of counsel given out by many planners. "With most people, I'd recommend they save for retirement first," said Janine Stubbs, manager of college savings plans at Raymond James Financial. Parents who are writing the checks may sense the wisdom. They have seen the cost of an education at a top four-year private college rise to more than \$160,000. State universities, where tuition has been rising at a faster pace than for private schools, can cost \$110,000 to \$140,000 for out-of-state tuition.

"The numbers are really staggering," said Rich Calvario, national finance tuition consultant at TIAA-CREF, one of the nation's largest money management firms.

Parents can count on the costs growing. In 18 years, the bill for a private college could easily hit \$500,000, according to online financial calculators created by Raymond James planners. To get there, you would have to save \$1,000 a month and have it earn 7 percent a month from the day Junior was born. Tuition, which has been rising faster than inflation for two decades, is now also rising faster than the median family income of \$44,389. The factors that have pushed it to rise annually more than three percentage points above inflation -- demographics, reductions in state aid to higher education, the demand for college education -- are not changing, says Ronald Ehrenberg, a Cornell University economics professor.

Financial planners offer pretty frank advice. If you don't have enough money to put your children through college, they can always -- gasp -- finance it themselves with part-time jobs and loans.

You, on the other hand, cannot obtain a loan to pay for retirement. If you don't have enough saved for retirement, you'll either be eating cat food or depending on the kindness of your well-educated and pampered children. Friskies Ocean Whitefish and Rice, anyone?

There is another reason it makes little sense to sock away all that money for college. When you do, you usually end up paying full price for a college education. As a practical matter, you shouldn't pay full price for anything. "People should not be scared off by the posted price at most colleges," Mr. Ehrenberg said. "Tuition discounts are very, very large in most places."

Paying for college is a little like buying an airline ticket. Some people are given a discount for paying way in advance, for instance. They are subsidized by the last-minute buyers who pay full price. Economists call this price discrimination.

There is nothing wrong with it. Many a vendor has dreamed of trying it: a vending machine that charges more for cold drinks as the temperature rises or an online service that monitors online behavior to charge a higher price to the buyer least sensitive to price increases. Price discrimination works best if the vendor learns as much about a buyer's willingness and ability to pay as it can. If you had to tell an auto dealer exactly how much you make and what your liquid assets are before he tells you the price, you'd find yourself paying a lot more for cars.

That's what colleges do. They get that perfect information in the form of Free Application for Federal Student Aid. Under threat of a \$20,000 fine and prison, the family discloses income, cash and investments to the college aid officer. The more the parent and student save, the more they are penalized.

For example, take the popular prepaid-tuition 529 plans. They allow you to pay tuition at today's prices for a student of tomorrow. About 15 states offer such plans for financing an education at their state colleges and a consortium of about 250 private colleges have set up a similar plan.

Great idea? "They are the most damaging to financial aid," says Michael Kitces, director for financial planning for the private wealth management firm of the Pinnacle Advisory Group in Columbia, Md. "For every dollar saved you lose a dollar of financial aid."

Mr. Kitces instead steers clients to the less damaging 529 savings plans. These work like tax-sheltered individual retirement account or 401(k) retirement funds. The money, as long as it is kept in an adult's name with a child named as beneficiary, is assessed at a maximum rate of 5.64 percent.

Economists call this a disincentive to savings. "I'm not advocating not saving," says Richard Vedder, an Ohio University professor of economics and author of "Going Broke by Degree: Why College Costs Too Much" (AEI Press, 2004). He saved for his own children's educations, after all. But he notes that because financial aid reduces the incentives to save, it is like a 25 percent to 30 percent tax on a family's savings. "It might even be more than that."

It boils down to this: If you expect that you will qualify for financial aid either because your income will be modest or because you will have several children in college at the same time, save as much as you can for yourself in a 401(k) and I.R.A. Money saved in retirement accounts is invisible to the college financial aid officer.

If, however, you are wealthy or you anticipate being wealthy enough that your family will never qualify for financial aid, take advantage of the 529 tax shelters. Prepay the tuition and stash money for room and board in a 529 savings account.

Never feel guilty for exploiting a savings plan set up to aid the poor and middle class. After all, you will be paying for the children sitting in the discounted seats.

### **Several Ways to Prepare for the Halls of Ivy**

Trying to plan for an event 10 to 20 years off, an event subject to legislative whims, demographic change and the wiles of university bureaucrats, is going to be difficult. Here are a few things to consider when saving for college:

Do not put savings in your child's name. There is the fear, of course, that he will run off and buy a Porsche with it. But the real danger is that college aid officials can assess 35 percent of a student's assets versus only 5.64 percent of a parent's holdings.

Don't spend the money in a 529 prepaid tuition plan until after the Free Application for Federal Student Aid has been filed for the student's senior year. That way it won't count against financial aid.

Be careful about withdrawing the money in the tax year that the student will go off to his first job. If it is a high-paying job, the extra income could knock your child into a higher tax bracket.

Have grandparents contribute to a 529 savings plan. It is not counted as a family asset. In fact, the plans provide one of the best ways for grandparents to reduce their estates. Consult a lawyer or financial planner so you do this right, but a couple can contribute \$110,000 into one of these funds in a single year and not face any gift tax penalties. They can take it back out if they later need to, with penalty and some tax.

### **Correction: October 5, 2005, Wednesday**

The Your Money column in Business Day on Sept. 24, about ways to save for a college education, misstated the rate of return and the amount of investment needed, as an example, to earn about \$500,000 in 18 years. The investment would be about \$1,200 a month, not \$1,000, at a rate of 7 percent a year, not a month.

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