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POLICY BRIEF

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Toward More Inclusive College Savings Plans: Sample State Legislation

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Participation in state college savings (529) plans[1] has increased rapidly. Despite this rapid growth, low- and moderate-income families are much less likely to own 529 plan accounts than high-income families.[2] Savings play a key role in college financing in most families. To make higher education more accessible for all children in America, it is important to offer a savings plan that benefits families at all income levels.

For financial reasons, saving for post-secondary education is more important than ever. Aid for college has declined. In addition, a pattern of evidence suggests that saving for college may affect student performance. Controlling for income and many other variables, greater parental savings and assets are associated with an increase in children completing college.[3] Moreover, recent research finds a particularly strong association between a child having his or her own savings and later college access and completion.[4]

To promote greater 529 plan participation for all residents, some states use the following policy strategies: *1) facilitate enrollment and contributions*, *2) remove saving disincentives*, *3) increase saving incentives*, and *4) strengthen tax benefits*. In this brief, we identify inclusive state 529 policies achieved through legislative and administrative means, and point to existing examples.[5]

Facilitate Enrollment and Contributions

An effective and budget-neutral strategy is to simplify investment choices and automate contributions to make it easier for people of all incomes to save.

Allow state income tax refunds to be deposited directly into the 529 plan

Direct deposit of state income tax refunds into the 529 college savings plan facilitates saving for post-secondary education and increases awareness about the state's 529 plan. Taxpayers can elect to have either their entire or partial refund deposited directly into their 529. The second option gives taxpayers greater flexibility and may be

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especially attractive to households who need part of the refund for essential expenses.[6]

Legislative approach[7]
The [state agency] shall include on the [state] individual income tax forms, including those forms on which a husband and wife file separately on the same form, a designation as follows:
"If you are entitled to a refund, check if you wish to designate [ ] [$ x], [ ] [$ y], [ ] [$ z], [ ] _______ (write in amount) or [ ] all of your tax refund to a [state 529 plan] account. Your refund will be reduced by this amount."

Administrative approach[8]

STEP 6 ...late Your Refund or Amount Due

29 ***REFUND.*** (Line 25 minus lines 27, 27a and 28) - NOTE: If total of lines 27, 27a and 28 is greater than line 25, subtract line 25 from the total of lines 27, 27a and 28 and enter the amount on line 31 below....29 ____ , ____ . ____

IF YOU WOULD LIKE YOUR REFUND DEPOSITED DIRECTLY TO YOUR BANK ACCOUNT *($10,000 or less)* OR TO A NEXTGEN COLLEGE INVESTING PLAN® ACCOUNT, read the instructions on page 7 and fill out the information below.

Direct Deposit

30a Routing Number* ____________
*For NextGen Accounts, enter 043000261

30b Account Number* ____________
*For NextGen Accounts, enter the account owner's 9-digit social security number (do not enter hyphens).

30c Type of Account: [ ] Checking [ ] Savings [ ] NextGen®

Identify a default investment to simplify choices

A default investment in the direct-sold 529 plan[9] simplifies the enrollment process and benefits individuals who are uncertain about which investment option to select on the 529 plan application form. People are less likely to save when confronted with multiple investment options, especially when they lack the necessary financial skills to make prudent choices.

Administrative approach[10]

STEP 6 **Choose Your Portfolio(s)**

[**The Plan offers three different investment approaches. Select from Portfolio options A, B, or C, or select a combination. If you do not select a Portfolio, an Enrollment-Based Portfolio will be chosen for you based on the Beneficiary's age and expected college entry date.**]

▶ The minimum initial contribution is $250 per Portfolio/Account unless you invest at least $50 per Portfolio through regular monthly payments (Automatic Asset Builder or payroll deductions), the Alaska PFD program, or a Direct Rollover.

A Enrollment-Based Portfolios

Assets are invested in a mix of stocks, bonds, and money market funds allocated according to when the Beneficiary is expected to enter college. As the Beneficiary approaches college enrollment, the investment will move to an increasingly conservative allocation.

Remove Saving Disincentives

Regardless of political perspective, an appealing policy direction for encouraging college savings is to remove saving disincentives posed by state public assistance and state financial aid programs.

Eliminate asset tests for public assistance programs

Asset tests in public assistance programs such as Temporary Assistance for Needy Families (TANF) and Medicaid, which require households to "spend down" or keep assets to a minimum, create a disincentive for low-income families to save. States can encourage lower-income households to save for post-secondary education by eliminating asset limits entirely or exempting 529s from eligibility calculations.[11]

Legislative approach[12]
A [state 529 plan] account shall be exempt for purposes of determining eligibility for public assistance [define "public assistance" with list or cross-reference], provided that the federal rules for these programs permit such an exemption.

Administrative rule approach
Some states exempt assets from eligibility calculations in public assistance programs through administrative rule.[13]

Remove 529 plan balances from state student financial aid calculations

Although the amount of federal financial aid[14] vastly exceeds the amounts awarded at the state level, specific reforms to state financial aid programs can help remove barriers to saving. Approximately 17 states exempt assets in 529 plans from financial aid calculations.[15]

Legislative approach[16]
Notwithstanding any other provision of [the state tax code], no moneys invested in [a state 529 plan account] shall be considered to be an asset for purposes of determining an individual's eligibility for a need based grant, need based scholarship or need based work opportunity offered by the state under [state financial aid provision(s)].

Increase Saving Incentives

Use 529 savings matches and offer employer tax credits to encourage saving for future post-secondary educational expenses.

Match 529 plan deposits for low- and moderate-income accountholders

Some states offer 529 matching deposits for low- and moderate-income state residents to encourage saving for future higher educational expenses. State match programs vary in terms of funding, eligibility, and application.

Legislative approach[17]
The provisions of this subsection shall be subject to the limitations of appropriations. The amount of contributions made to an account by a participant who establishes a [state 529 plan] pursuant to [state code section(s)] shall be matched by the state on a dollar-for-dollar basis if the participant contributes at least [$ x] in each calendar year in which the account is open during the calendar year for which the application has been approved. The aggregate of all matching amounts for any participant shall not exceed [$ y] in any calendar year.

Provide tax incentives to employers for contributions to the state 529 plan

Many states partner with employers to facilitate payroll deductions for 529s. Saving in the workplace—via payroll deduction and employer matching—has significantly increased enrollment in 401(k) retirement savings plans. Likewise, employer matches for college savings plans could also encourage employees to save for their children's college education or their own retraining.

Legislative approach[18]
For taxable years ending on or after [starting date] and on or before [ending date], each taxpayer who, during the taxable year, makes a contribution (i) to a specified [state 529 plan account] under [state code provision] or (ii) to the [state tuition trust fund, if one exists] in an amount matching a contribution made in the same taxable year by an employee of the taxpayer to that account or fund is entitled to a [deduction or credit] against the tax imposed under [the state corporate tax provision] in an amount equal to [percentage] of that matching contribution, but not to exceed [$ x] per contributing employee per taxable year.

Strengthen Existing Tax Benefits

Extend tax benefits to all state 529 contributors, instead of limiting to accountholders, to make it easier and more financially attractive to participate in 529 plans.

Extend 529 tax benefits to persons other than accountholders

Expanding tax benefits to include individuals other than accountholders for 529 contributions allows state residents to receive tax deductions or credits for deposits to existing accounts benefiting relatives or friends. With this strategy in place, savings might be encouraged without the taxpayer having to complete 529 enrollment materials, thus making it easier to contribute.

> ***Legislative approach***[19]
> A taxpayer may deduct, to the extent not deducted in determining adjusted gross income, both of the following: Contributions made by the taxpayer in the tax year less qualified withdrawals made in the tax year from education savings accounts, calculated on a per education savings account basis, pursuant to the [state 529 plan enacting legislation], not to exceed a total deduction of [$ x] for a single return or [$ 2x] for a joint return per tax year. The amount calculated under this subparagraph for each education savings account shall not be less than zero.

Conclusions

These illustrative policy approaches are intended to inform more inclusive state policy for college savings plans. States are learning from each other to create sensible approaches that enable more families to save for college in 529 plans. At the end of the day, facilitating more inclusive college saving may be among the most efficient state policy strategies for increasing educational success.

Endnotes

1. 26 U.S.C. § 529 defines qualified tuition programs, both prepaid or savings plans, for post-secondary education. This brief focuses entirely on college savings plans.
2. Sallie Mae & Gallup (2009). *How America saves for college 2009*. Retrieved from http://www.salliemae.com/about/news_info/research/how_America_saves/
3. Zhan, M., & Sherraden, M. (2009). *Assets and liabilities, educational expectations, and children's college degree attainment* (CSD Research Brief 09-63). St. Louis, MO: Washington University, Center for Social Development.
4. Elliott, W., & Beverly, S. (2010). *The role of savings and wealth in reducing "wilt" between expectations and college attendance* (CSD Working Paper 10-01). St. Louis, MO: Washington University, Center for Social Development.
5. These examples highlight different state approaches and do not represent a comprehensive list of all state legislation on each 529 policy. States can draft specific legislation to meet their individual objectives, as well as comply with technical drafting requirements. This document does not constitute legal advice or a legal opinion.
6. The IRS allows taxpayers to split their refund and direct part of it to savings (such as accounts earmarked for retirement, health, and education) and the rest to a checking account, for example, to meet immediate needs.
7. Arkansas Act 211 (2009), codified at: Arkansas Code § 26-51-456 (2009); Utah Code § 59-10-1313 (2009)
8. 2008 Maine individual income tax 1040S
9. Direct-sold 529 plans, which state residents purchase directly from the state, have lower annual expenses than broker-sold plans that are accessed through financial advisors and charge additional fees.
10. University of Alaska College Savings Plan

11. Several states have eliminated asset tests for public assistance programs. States currently have authority to eliminate or modify asset tests when determining TANF, Medicaid, and SCHIP eligibility. There is no federal requirement for states to obtain a waiver to implement such changes. Recent federal legislation excludes 529s from asset tests in SNAP, formerly known as Food Stamps.
12. Arkansas Act 597 (2007), codified at: Arkansas Code § 6-84-114 (2009); and Oklahoma Senate Bill 1390 (2008), codified at: Oklahoma Statutes Title 56 § 4000 (2009)
13. For additional discussion of this topic, see Rand, D. (2007). Reforming state rules on asset limits: How to remove barriers to saving and asset accumulation in public benefit programs. *Clearinghouse Review Journal of Poverty Law and Policy*, March–April, 625-635.
14. Congress is considering legislation that would simplify the financial aid application process, including the elimination of most questions about savings and the addition of a net asset dollar cap for need-based aid eligibility (H.R. 3221).
15. Depending on the state, removing 529 savings from financial aid consideration could potentially increase the total number of students eligible for aid and thus diminish the amount of funds that would be available to the neediest students. Each state should consider whether the gains from exempting state 529 assets from state financial aid calculations outweigh the potential costs.
16. Georgia House Bill 417 (2001), codified at: Georgia Code § 20-3-641 (2009); Indiana Code § 21-9-7-2 (2009); and General Laws of Rhode Island § 16-57-6.6 (2009)
17. Arkansas Act 597 (2007), codified at: Arkansas Code § 6-84-114 (2009); Kansas Senate Bill 225 (2009); Minnesota House Bill 1385 (2005), codified at: Minnesota Statutes § 136G.11 (2009)
18. Illinois Act 096-0198 (2009), codified at: 35 Illinois Compiled Statutes § 5/218 (2009); Utah Code § 59-7-106 (2009), Utah Code § 53B-8a-106 (2009)
19. Georgia House Bill 1014 (2008), codified at: Georgia Code § 48-7-27 (2009); Michigan Act 134 (2009), codified at: Michigan Compiled Laws § 206.30 (2009)

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