# Defaulted on your federal student loan? You can fix that.

There are a lot of available resources to help parents prepare and financially plan for their kids to go to college. But what if you're a recent student or graduate who needs some guidance on your federal student loan(s)? This article discusses some options on how to handle defaulted federal student loans and some possible next steps.

# How to Balance the Three-Legged Stool of 529 Plans, Financial Aid and Retirement Savings

Preparing for the future is always a smart financial move. But, are you placing too much emphasis on saving for your child's future college education at the expense of your retirement savings? Understanding how 529 Plans and your student's financial aid award package impacts your retirement savings is key to making contributions that reduce dependence on student loans while ensuring a financially sound retirement. This article discusses what you should know to avoid allocating too much to a 529 Plan.

# Saving for College: College Savings Plans

We all know the importance of saving for college. Without a college education, our kids could be at a great disadvantage later in life. But the skyrocketing costs of a college education are enough to make anyone feel a little faint. With a little planning and foresight, a great college education is actually within reach.

**Yes, those costs keep going up**
So how much are college costs increasing? On average, tuition at 4-year public colleges has increased by 37%, and net costs (including factors like scholarships and grants) have increased by 24%, according to a 2019 report from the Center on Budget and Policy Priorities.[1]

**That's just the tip of the iceberg**
But that's not all! Tuition, fees, room and board are just part of the costs that will be incurred. As you begin looking for schools and weighing costs, you'll need to think about computers, books, dorm furnishings, travel, entertainment and laundry. And that's not counting the million other ways your college-aged kids will find to spend your cash. So, if sending your child or children to college is in your plans, you need to begin setting aside money immediately.

**Get the government on your side**
The government has a number of programs and tax laws to make saving for college easier. These are only a few examples. You should make every effort to learn as much as possible before making any decisions. A few popular options include:

- **529 Plans** – These state-sponsored investment plans provide tax deferred earnings and income tax-free withdrawals (for qualified expenses). In addition to tuition, room and board, the money can be used for other expenses, such as books and supplies. Some state plans even allow you to deduct contributions from state income taxes. If the account's beneficiary (your child) decides not to attend college, you may be able to put the money towards another family member's education; otherwise, it could be taxed at your normal rate.
    - Before investing in a Section 529 plan, you should consider whether the state you or your designated beneficiary reside in or have taxable income in has a Section 529 plan that offers favorable state income tax or other benefits that are only available if you invest in that state's Section 529 plan.

- **Coverdell Education Savings Account** – This account provides tax-deferred earnings and income tax-free withdrawals (for qualified expenses); but participants must meet specific income requirements and you can only contribute up to $2,000 annually. The fund is transferable to another child if a first child does not go to college; however, taxes and penalties may apply if it's not used for college.
- **Uniform Gifts (or Transfers) to Minors Act** – These allow you to transfer up to $14,000 a year (tax limit for 2015), without triggering the gift tax, to an account held in a child's name; although you are the custodian. The money is no longer part of your taxable holding; so, technically, it can reduce your income tax bill. Realistically, though, the gift must be sizeable for any real tax benefit. It should also be noted that in some instances the child may have to file tax returns for taxes due (the kiddie tax). Also, it can't be taken back; so the child can use the money for anything – not necessarily college – once he or she reaches adulthood. Rules vary by state and are dependent on state law.

**Other federal government tax credits, such as the Hope Scholarship Credit and the Lifetime Learning Tax Credit, may be available subject to certain income requirements.**

**Invest wisely**

However you choose to save for your children's education, your may want to choose an investment strategy consistent with their age and number of years until college -- more aggressive during their early years, when you have more time for money to compound and grow, and more conservative as the child approaches college age. You may wish to consult with your financial professional to develop a strategy that best meets your family's needs.

**Consider a helping hand**

Financial aid, loans, and athletic & academic scholarships can help lighten the load. Other sources of aid include work-study programs, merit awards for academic achievement, awards for involvement in various student activities and assistance for disabled students. Contact each school for its specific programs and policies.

**Think about life insurance**

The death of a parent sometimes cuts off money that was to be used to put children through college. Life insurance death benefits can be used to help pay children's education expenses if a parent dies early. Loans and withdrawals from cash value policies can also help with tuition needs. College aid forms generally do not include the value of a life insurance policy when calculating financial aid. Policy loans and partial withdrawals may vary by state, generate an income tax liability, reduce available surrender value and death benefit or cause the policy to lapse.

**Secure their future without risking your own**

If possible, you may be able to develop a strategy that avoids paying for college by withdrawing from your retirement savings or taking out a home equity loan. Both of these could land you in hot financial water as retirement approaches. So remember that there are other approaches. With a little preparation, you may be able to have a broader range of schools from which to choose to send your kids. Maybe that can even include the school of their dreams.

[1]*The cost of college increased by more than 25% in the last 10 years—here's why, Hess, A; Dec. 13, 2019*

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