

Balancing College and Retirement Savings

Hypothetical parents Jim Lawson and his wife Megan are in their early 30s. They want to start saving for when Billy, seven, and Jenny, five, start college—with a 529 plan for each child. But Jim already contributes \$10,000 a year to his workplace retirement plan and the couple doesn't want to short-change their retirement by diverting all their savings to the 529 plans. So how do they save for both retirement and college?

What to consider

- Although there's no up-front federal tax deduction for 529 plans, savings will grow tax-free. Withdrawals are also tax-free if the money goes toward education.
- Retirement savings should have top priority, since no one will make a loan to pay for retirement. (Part of the cost of college can be covered by financial aid and education loans.) Furthermore, Jim's workplace retirement plan contributions reduce their annual income tax bill, and grow tax-free too. Megan's parents want to help, too.

What they decided

- Jim will continue to contribute 10% of his salary to his workplace retirement plan. His plan offers an automatic savings increase feature, so he can boost his contribution each year when he gets a raise.
- Now that the children are in school, Megan will begin a part-time job. She'll contribute most of her earnings to an IRA.
- The couple agrees to contribute \$1,500 a year to each child's 529 plan. Future bonuses and tax refunds will go to the 529 plans as well. Their contributions may also save them money on their state income taxes.
- Megan's parents contribute \$1,000 a year to each child's plan. When Billy and Jenny reach college age, they can begin taking tax-free withdrawals of their 529 plan assets to cover expenses like tuition, room and board and books, while their parents continue to save toward retirement.

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