# The 529 College Savings Plan: Bringing Higher Education into Focus for N.C. Children

## An Emerging Issues Report

May 2010

Action for Children
Celebrating 25 Years
North Carolina

# The 529 College Savings Plan: Bringing Higher Education into Focus for N.C. Children

## An Emerging Issues Report

**May 2010**

## Executive Summary

Every child should have the opportunity to pursue higher education. However, rising costs and increased student debt burdens have put higher education out of reach for many children--especially those from low- and moderate-income households. While reform of the student financial aid system is long overdue, there is additional evidence that policies that promote savings can support young people's pursuit of learning. Saving for educational opportunities has been found to mitigate the financial burden of higher education. Most importantly, however, emerging evidence suggests that savings provide an orientation to educational goals, thereby improving educational achievement and college preparation. Savings can improve educational outcomes in the short-term and, in the long-term, bring the promise of higher education to more students, resulting in lifetime returns in earnings and greater financial stability.

## Recommendations:

- Target outreach and education concerning the N.C. 529 College Savings Plan to communities with low levels of college attainment.
- Make the 529 College Savings Plan work for all children by: 1)providing an initial deposit to a 529 account for every low-income child born, and 2) matching contributions by low-income households through a state tax credit.
- Exempt 529 contributions from public benefit asset limits and state need-based financial aid calculations.
- At the federal level, make permanent the American Opportunity Tax Credit and expand the Saver's Credit to include 529 plans as qualified savings vehicles.

Action for Children
Celebrating 25 Years
North Carolina

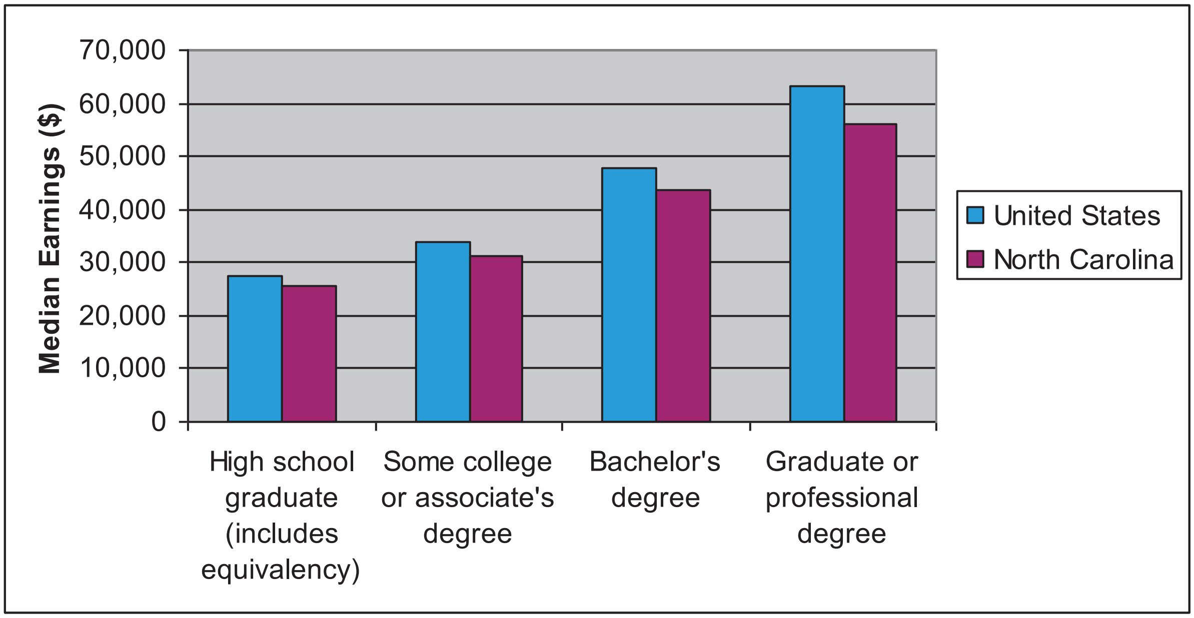
## North Carolina's Investment in Higher Education

North Carolina established the first public university in the United States in 1789, recognizing the important role that higher education plays in promoting a vibrant economy and civic life. Ongoing public investments in higher education have built nationally-recognized public university and community college systems that have provided North Carolinians with the training to compete for jobs in a global marketplace. Despite the N.C. Constitution's aim to provide higher education to all North Carolinians "free of expense, as far as practicable," these public investments have not resulted in affordable higher education for all North Carolinians.

In recent years, investments to improve the affordability of higher education for North Carolina's working families have declined. For every dollar in Pell Grants provided by the federal government, the state invests only 70 cents.[1] Recently, the EARN Scholarship program, which provided need-based financial aid through grants to low-income families, was eliminated. The divestment in the student financial aid system at the state level has been compounded by similar declines in federal financial aid. The result is that North Carolina's families today must pay nearly a quarter of their income for college expenses, even after financial aid.[2] It is clear that an improved system for need-based financial aid at both the state and federal levels is necessary to ensure that public investments in the infrastructure of higher education may be enjoyed by all North Carolinians. Evidence suggests that supporting participation in college savings plans is an important complement to an effective need-based financial aid system.[3]

Public investment in higher education must ensure that students, regardless of family income, can continue to learn after high school. Such investments can generate significant economic returns for young people, their families and their communities.

**Higher education delivers economic returns to students in the form of higher earnings.**




**Source:** American Community Survey, 2006-2008 Three-Year Estimates. U.S. Census Bureau.

**Higher education provides the best opportunity for children to move up the economic ladder, which benefits society's bottom line.** A study by the Pew Charitable Trust found that adult children of parents in the bottom income quintile nearly quadrupled their chances of moving all the way to the top quintile by obtaining a college degree.[4]

**A high level of educational attainment is also good for the community-at-large in the immediate term.** A higher level of educational attainment in a community can attract business and investment and has been found nationally to correlate with job growth, greater economic vitality, community safety and more stable local revenue to support public services, including K-12 education.

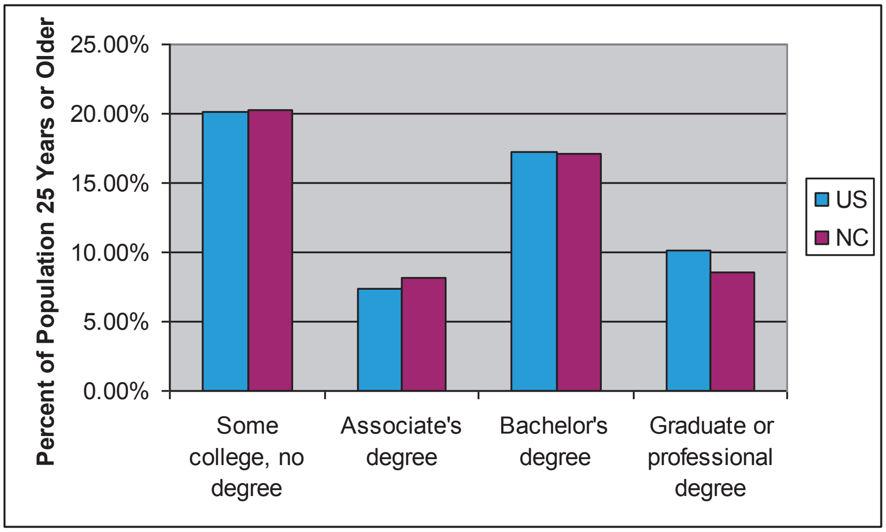
## The State of Higher Education Achievement in North Carolina

Despite a nationally-recognized public university and community college system, many North Carolinians do not enroll in ongoing educational opportunities after high school and still fewer complete degrees. While North Carolina is on par with the national average, less than 20 percent of the population over 25 years of age has a bachelor's degree.

Educational attainment has lagged even as the economic transformation of North Carolina has meant an advanced degree is one of the only guarantees of a living wage. The loss of manufacturing jobs has meant that many North Carolinians with high school diplomas have lost their livelihoods, and growing low-wage retail opportunities do not provide an adequate wage.

Many North Carolinians have recognized this new economic reality and pursued higher education, only to face significant barriers that bar them from completing a degree.

**For both N.C. and the United States, nearly 1 in 5 adults over the age of 25 started college but did not receive a degree.**




**Source:** American Community Survey, 2006-2008 Three-Year Estimates, U.S. Census Bureau.

As of 2009, at more than half of the colleges and universities in North Carolina, fewer than half of entering freshmen graduated in six years.[5] College completion, rather than college entrance, is increasingly being considered in North Carolina and the nation as the outcome upon which policy must focus. Nationally, an estimated 1 in 5 students leave college without a degree but with debt.[6] It is clear that the challenges North Carolina students face in pursuing higher education extends beyond enrollment.

## Financial Barriers to Higher Education

**The cost of higher education has outpaced federal and state investments in grant programs as well as changes in median family income.** Recent analysis found that between 1999 and 2009, tuition and fees at the average public university increased by 50 percent. During the same time period, Pell Grant awards increased by only 23 percent and median family income increased by only three percent.[7]

**Increasingly, households have relied on loans to finance higher education, undermining the returns to education at least in the immediate term.** In 1980, 55 percent of financial aid to undergraduate students came in the form of grants; in 2008 that percent had dropped to 26 percent.[8] Households are increasingly applying for private loans to cover the rising costs of higher education.

**Higher costs generate financial stress on the household and student.** College students are increasing their work hours in order to pay for school. Nearly half of students in four-year colleges work more than 20 hours a week, while 61 percent of community college students do so.[9] Research suggests that the driving force for dropping out of college is financial stress.[10]

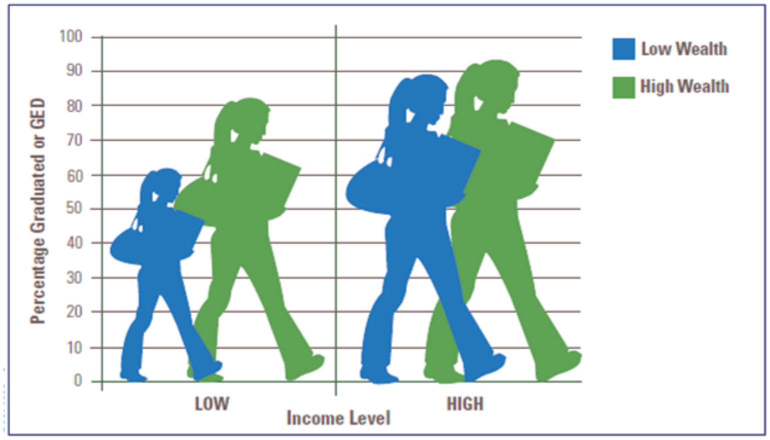
**Some North Carolina students bear a disproportionately high financial burden to complete their degrees.** Students at North Carolina's historically black colleges and universities (HBCUs) hold the highest aggregate amount of student debt in the country, compared to those enrolled in HBCUs nationwide.[11]

## A Role for Savings

A growing body of evidence suggests that college savings products can play a complementary role to a sound financial aid system.[12] Such products—from Coverdell ESAs to Roth IRAs to 529 plans—provide households with the opportunity to plan for their children's future education expenses, thus establishing an expectation of enrollment. Increasingly, 529 plans have been identified as an important platform for more inclusive college saving, targeted toward low- and moderate-income households.[13]

**Savings are likely to have an impact on the affordability of higher education at the margins.** Interest on savings can't keep pace with tuition cost increases. Even an aggressive saver (contributing $200 a month beginning when a child is born) would only be able to accrue enough savings to pay for one year at a private university. Savings, however, can reduce the work burden on students and provide a cushion for students at risk of dropping out because of financial shocks to themselves or their families.

**Evidence suggests that college savings could also go a long way toward raising expectations of college achievement.** A national study found that only 54 percent of poor children and 57 percent of asset-poor children expect to attend college, while 81 percent of poor children who hold a savings account for college expect to attend.[14] Importantly, children's college expectations for those with savings accounts were found to improve math achievement. The research suggests that closing the gap between aspirations and expectations may therefore additionally impact achievement.



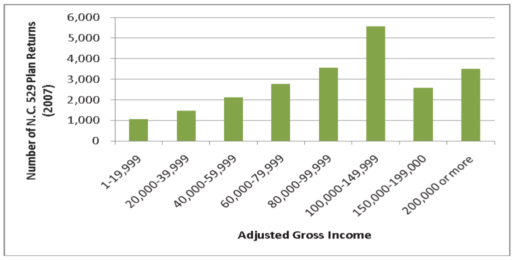

Source: Destin, Mesmin. 2009. "Assets, Inequality and the Transition to Adulthood: An Analysis of the Panel Study of Income Dynamics." Aspen Institute, Initiative on Financial Security: Washington, D.C.

## College Saving by North Carolinians

**Measuring household savings is difficult at the state level.** Capturing savings for children and savings by low- and moderate-income households is even more difficult. The best available data are provided by an analysis of state tax returns that have information regarding participation in the N.C. 529 College Savings Plan. The N.C. 529 plan has a tax-preferred status that allows households to claim their annual contributions as deductions. Information provided on the tax return can therefore provide some insight into the college savings activities of households statewide. While not the only savings vehicle available to households saving for college, the 529 plan can provide us with preliminary insights.

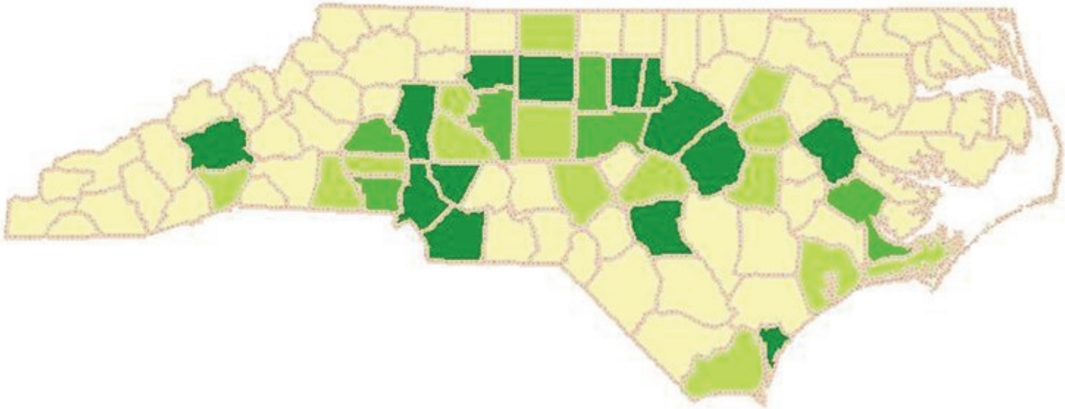
**College savings in the N.C. 529 plan is limited.** In 2007, approximately 22,000 tax returns were filed that included 529 plan information. This represents less than one percent of the total returns filed that year. Only one percent of the more than two million children in North Carolina receive contributions to a 529 account.

**Participation in the NC 529 plan is concentrated among higher income groups.** The tax benefits under federal regulations governing 529 plans benefit higher income households and encourage their participation. Similarly, the tax deduction offered by the state for the N.C. 529 plan benefits households with higher tax liability. For example, in the chart below, which shows the number of N.C. state tax returns with 529 plan deductions by income level, participation rises steadily as household income rises up to $150,000, after which it drops off slightly.

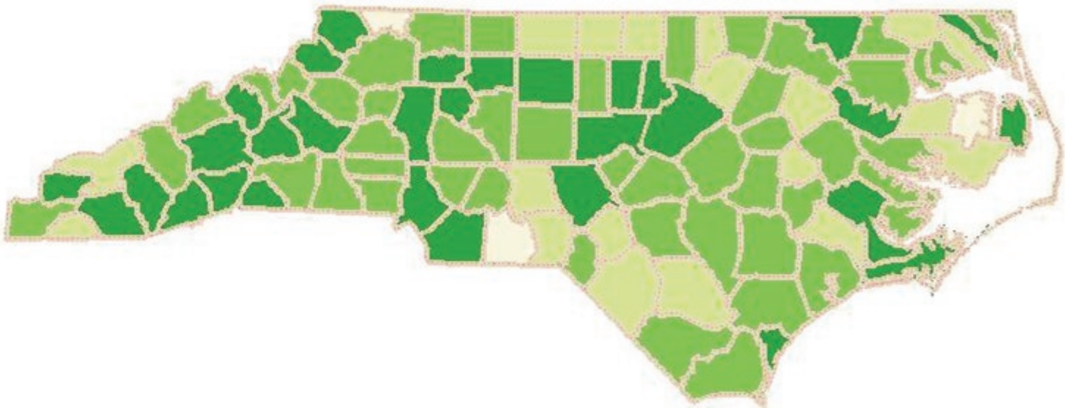



Source: Special Data Request, January 2010, N.C. Department of Revenue

**High levels of participation in the N.C. 529 plan are centered around urban centers.**



**However, high average annual contributions are found in communities throughout the state.**



Source: Special Data Request, January 2010, N.C. Department of Revenue

**The aggregate amount saved in the state is high, considering recent findings regarding the levels of asset poverty among North Carolinians and their struggles during the current economic downturn.**[15]

Aggregate savings in the N.C. 529 plan, as taken from tax return data, were $62.5 million. The average savings per return were $2,310, which represents a monthly contribution of $200. Savings, too, have increased since 2007, despite the economic downturn and the more than 30 percent decline in net worth experienced by North Carolina families prior to 2006.[16]

## Saving for Children's Futures

**Promising programs across the country promote saving for children's futures by using the 529 college savings plan structure.** Eleven states provide a match to low- and moderate-income households through their progressive 529 plans. The Aspiring Scholars Matching Grant Program, a pilot initiative in Arkansas, leveraged $250,000 in public dollars to encourage savings for nearly 500 children now planning to go to college. In Maine, a contribution by a private philanthropist now provides an initial deposit into the 529 plan for every child born in the state.[17]

**Long-term saving for children's futures needs to be supported by better public policy.** Saving for college is a difficult task, especially for low - and middle-income households that have constrained budgets. Saving could be made much easier if public policy supported it.

**Savings held in 529 accounts are counted toward asset limits in public benefit programs.** For most public benefit programs, savings held in 529 accounts and many other savings vehicles are counted as household assets. In North Carolina, assets in excess of $2,500 disqualify a household from receiving most benefits. Asset limits have been shown to discourage benefit recipients from saving, meaning that children in these households are denied the encouragement that a college savings account can provide.

**Savings are counted in the determination of financial aid packages.** Nearly six percent of the value of a 529 account is considered in determining the expected amount that a family of a beneficiary is expected to pay toward that beneficiary's higher education. This percentage is usually lower for lower income families and, depending on the parents' income at the time of college, money saved in a 529 may not be considered. However, the federal rules and formulae for calculating aid are so complicated and difficult to communicate that many low- and moderate-income families may conclude that having college savings will impede their eligibility for need-based financial aid.[18]

## Conclusions

North Carolina's policymakers have long recognized the importance of education to achieving a stable economy that can continue to grow and deliver prosperity to all. However, current state policies unnecessarily limit the ability of North Carolina's young people to attend and succeed in post-secondary institutions. Few North Carolinians take advantage of the 529 College Savings Plan as a way to plan for some of the costs of higher education. Public policy should make the plan more accessible to low- and moderate-income North Carolinians. Increasing college savings may also help young people realize that college is within their reach. Delivering such hope for the future, beginning with a child's earliest classroom experiences, can go a long way to improving a child's outcomes throughout both his/her educational and working lives.

## Recommendations

1) **Target outreach and education about the N.C. 529 College Savings Plan to communities with low levels of college attainment.** Outreach could include providing parents of entering kindergarteners with information regarding the 529 plan, or establishing bricks and mortar presence in communities by partnering with financial institutions. Educating the public about the importance of a strong financial aid system and college savings for preparing young people for higher education can improve college attainment levels.

2) **Make the 529 College Savings Plan work for all children by providing: a) an initial deposit to a 529 account for every low-income child born, and b) matching contributions by low-income households through a state tax credit.** Enrolling every child at birth or kindergarten and providing low-income children with an initial deposit to jump start their savings would help families plan for education. Delivering the match at tax time either by making the current tax deduction for contributions to 529s a refundable tax credit or by ensuring an annual matching grant at tax time would provide an annual support to income-eligible households who have committed to saving and do not benefit from the government subsidy offered to those with higher tax liabilities. Funding for such a program could be generated by allocating a portion of the 529 plan administrative fees to match savings.

3) **Exempt 529 contributions from public benefit asset limits and state need-based financial aid calculations.** Need-based financial aid is the primary tool to finance higher education for low-income households. Contributions to 529s should not be considered assets when households are applying for financial aid or income support.

4) **At the federal level, expand the Saver's Credit to include 529 plans as qualified savings vehicles.** Reps. Pomeroy (D-ND) and Tiberi (R-OH) introduced H.R. 1351, the Savings Enhancement for Education in College Act (SEE College Act). This legislation will make improvements to 529 College Savings Plans and boost participation in the plans by moderate- and low-income families by expanding the Saver's Credit, which currently only applies to contributions to retirement plans, to cover 529 plans as well.

**Note:** For specific legislative and administrative examples of selected recommendations, see: Lassar, Terry, Margaret Clancy & Sarah McClure. January 2010. "Toward More Inclusive College Savings Plans: Sample State Legislation," Washington University Center for Social Development.

## Endnotes


1. National Center for Public Policy and Higher Education. 2008. "Measuring Up 2008: North Carolina State Report Card on Higher Education."

2. Ibid.

3. Center for Social Development. College Savings Initiative. Research catalogues available online at: www.collegesavingsinitiative.org

4. Haskins, Ron, Harry Holzer, & Robert Lerman. May 2009. "Promoting Economic Mobility by Increasing Post-Secondary Education," Economic Mobility Project, Pew Charitable Trusts.

5. Data from The Education Trust, College Results online tool. Available online at: http://www.collegeresults.org/search2d.aspx?so=NC&y=2008

6. Demos. Winter 2007. "Higher and Higher Education: Trends in Access, Affordability, and Debt."

7. Haskins, Ron, Harry Holzer, & Robert Lerman. May 2009. "Promoting Economic Mobility by Increasing Post-Secondary Education," Economic Mobility Project, Pew Charitable Trusts.

8. Orozco, Viany. 2009. "Fact Sheet: Student Debt 101," Demos.

9. Cauthen, Nancy K. and Viany Orozco. September 2009. "Work Less, Study More, & Succeed: How Financial Supports can Improve Post Secondary Success," Demos.

10. Cauthen, Nancy K. and Viany Orozco. September 2009. "Work Less, Study More, & Succeed: How Financial Supports can Improve Post Secondary Success," Demos.

11. N.C. Institute of Minority Economic Development. 2007. "Removing the Millstone: Student Debt and the Growing Wealth Gap."

12. CFED, *2009-2010 Assets & Opportunity Scorecard.* 2009. "College Savings Incentives;" and Center for Social Development.

13. Sherraden, Michael. July 2009. "A Promising Platform for College Savings," Washington University Center for Social Development and New America Foundation, College Savings Initiative.

14. Elliott, William & Sondra Beverly. 2010. "The Role of Savings and Wealth in Reducing 'Wilt' between Expectations and College Attendance," Washington University Center for Social Development.

15. N.C. Assets Alliance. September 2009. "Asset Poverty Increases and Net Worth Declines for North Carolina Households." Available online at: http://www.ncassets.org/documents/AssetPovertyandNetWorth_FactSheet_FINAL.

16. North Carolina Assets Alliance and CFED, *2009-2010 Assets & Opportunity Scorecard*. September 2009. "Fact Sheet: Household Net Worth Declines and Asset Poverty Grows for North Carolina's Households."

17. Lassar, Terry & Margaret Clancy. Forthcoming. "College Savings Plan Accounts at Birth: Maine's Statewide Program."

18. Lassar, Terry, Margaret Clancy & Sarah McClure. January 2010. "Toward More Inclusive College Savings Plans: Sample State Legislation," Washington University Center for Social Development.


---


### Acknowledgements

Action for Children North Carolina would like to thank the Annie E. Casey Foundation's KIDS COUNT project for support of this publication. Editors of this publication include Steve Brooks, Executive Director, N.C. State Education Assistance Authority; and Margaret M. Clancy, Director, College Savings Initiative and Policy Director, Center for Social Development, Washington University in St. Louis. The findings and conclusions do not necessarily reflect the opinion of financial supporters or editors.


kids count


**Action for Children North Carolina**

**1300 St. Mary's Street, Ste. 500**

**Raleigh, NC 27605**

**www.ncchild.org**


Action for Children
Celebrating 25 Years
North Carolina

Find us on Facebook

Action for Children North Carolina

1300 St. Mary's Street, Ste. 500

Raleigh, NC 27605

www.ncchild.org