

## **College Savings: Revamping California's 529 ScholarShare Program**

**By Hosai Ehsan**

Although the State of California currently offers its residents a 529 college savings plan through the ScholarShare program, the investment vehicle lacks incentives that encourage low- and middle-income individuals to participate in the program. Other U.S. states offer a variety of attractive incentives, such as matching contributions and state tax deductions. Californians are ready to adopt a stronger and more incentive oriented 529 plan that will encourage families to build savings for their children's college education. Postsecondary educational attainment increases median income, tax revenues, civic engagement and mental health<sup>1</sup>. Similarly, it lowers unemployment rates, poverty rates, dependency on government programs and crime<sup>2</sup>. Strengthening the ScholarShare program is the steppingstone for an educated and a financially sound California.

### **Understanding the Need**

Increased tuition rates, lack of need-based scholarships and the government's failure to provide sufficient financial aid packages negatively affect the college attendance rates of lower- and middle-class California children. California's slowed economy, higher unemployment rates, stagnant median wages, increasing foreclosures, and climbing inflation rates, leaves little room for Californians to build savings without real incentives—especially those pertaining to savings for future costs, such as their children's higher education. This burden will result in minimizing access to higher education and skills training for the children of lower income families.

In the past five years, middle- and lower-income families have spent 16-39 percent of their household income to send one child to a public four-year university.<sup>3</sup> Without proper financial planning, households with multiple children, especially where siblings are close in age, will find it nearly impossible to send their children to four-year universities. Alternate options such as junior colleges and technical schools are less expensive, but often retention rates are lower, and a bachelor's degree is not granted.

### **Education is an Asset**

Recent research-based reports indicate that median annual earnings rise as higher education degrees are attained.<sup>4</sup> According to the College Savings Plan Network, average earning for an individual with a high school diploma is \$31,075, compared to \$38,579 for an individual with an associates degree, \$50,394 for an individual with a bachelor's degree and \$60,700 for an individual with a master's degree.<sup>5</sup>

With a population of 38 million, 10.4 percent of which are college-aged individuals (age 18-24 years), California is in desperate need of adapting or emulating innovative ways to build family savings for the

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<sup>1</sup> *Education Pays* (Washington, DC: College Board, 2007).

<sup>2</sup> *Ibid.*

<sup>3</sup> *Trends in College Pricing 2007* (Washington, DC: College Board, 2007).

<sup>4</sup> Rourke O'Brien. "The Asset Agenda: Policy Options to Promote Savings and Asset Ownership by Low- and Moderate-Income Americans," (New America Foundation, September 2008).

<sup>5</sup> College Savings Plan Network, *Why Save For College*.

higher education of future generations.<sup>6</sup> In 2007, 50 percent of entering freshman borrowed funds to pay for tuition.<sup>7</sup> Half of the students, who are currently enrolled in college, will not graduate, but will carry debt.<sup>8</sup> In California, students who do complete their postsecondary education, carry the burden of over \$17,000 in average postgraduate debt.<sup>9</sup> Savings plans are essential in offsetting these debts.

### **529 Policy Options**

The 529 ScholarShare program allows families to build savings or buy credits at the current rate for their children's college education. As an incentive to encourage low- and moderate-income families to save for higher education costs, states like Colorado, Louisiana, Maine, Michigan, Minnesota and Rhode Island provide limited matching funds for contributions.<sup>10</sup> Currently, Californians are not provided the incentive of matching funds nor state income tax advantages on 529 ScholarShare savings. Many low- and moderate-income families are reluctant to participate in 529s due to the fact that the program lacks incentives and are not well publicized.

What can California do to revamp its current 529 plan?

- Look at successful 529 models in other states and adopt a combination of those models that best suit the residents and economy of California.
- Research why many people have not invested in 529s and take appropriate steps to close those gaps.
- Similarly, research what additional incentives Californians will find most favorable and adapt policy to include those incentives.

### **Statewide Public Awareness Campaign**

Publicizing and facilitating educational seminars, supporting matching grants, requiring employers to offer payroll deduction, and creating innovation funds for the 529 ScholarShare program are various proposals that will offset the high cost of postsecondary education, reduce postgraduate debt and build savings. Californians need to be able to build savings that purchase a brighter future—a future that paves the roadway to the American Dream. Supporting 529 plan incentives is crucial for a financially sound California.

In 2007, a series of studies indicated that over half of all American parents (including California parents) were not aware of the 529 savings plans.<sup>11</sup> Californians need to be educated on the 529 investment vehicle via media outlets, publications, facilitating seminars in early childhood education settings and community events. Grassroots efforts in raising awareness is the primary step in getting Californians to strongly consider higher education for their children—and do away with the affordability worry.

Many U.S. states have better strategies to market their plans. The state of Maine has been successful in

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<sup>6</sup> US Census Bureau, American Community Survey, 2006.

<sup>7</sup> College Savings Plan Network, *Why Save For College*.

<sup>8</sup> U.S. Department of Education, Mapping California's Educational Progress, 2008.

<sup>9</sup> Project on Student Debt, State By State Data, 2007.

<sup>10</sup> Anne Stuhldreher. "California Asset Building Policy Options: Providing All Californians a Stake in the Economy and a Means to Get Ahead," policy issue brief, October 2005.

<sup>11</sup> Charles Paikert. "529 Industry Deals With Low Awareness," Investment News, November 5, 2007.

launching a Planning for College website which includes information on 529s.<sup>12</sup> Residents of other states like Colorado, Minnesota, and Michigan can resort to their state Department of Education websites to easily access information about 529s.

What can California do to raise awareness of the existence and benefits of 529s?

- Launch a user friendly 529 education website.
- Facilitate 529 seminars in major early childhood education settings, such as pre-schools, elementary schools and after school programs.
- Distribute 529 literature at a variety of community events.
- Advertise 529s via local television channels, radios and newspapers.
- Identify communities that can benefit most from 529s and take the awareness campaign on the road.

### **Matched Savings**

Californians who are aware of 529 plans will agree that saving for postsecondary education reduces reliance on loans, earns interest versus paying interest, and essentially leads to being debt free.<sup>13</sup> A \$100,000 education will cost \$145,000 for an individual who borrows money, compared to \$65,000 for an individual who had savings and investments.<sup>14</sup> Clearly saving for a college education is the logical and successful method.

All U.S. residents benefit from federal tax-free qualified expenditures of the 529 savings. However, residents of Colorado, Louisiana, Maine, Michigan, Minnesota and Rhode Island enjoy matching grants for contributions towards their children's 529 investment.<sup>15</sup>

In California, both state and private sectors can join to adopt various matching grants for 529 plans. State entities, community organizations, banks, employers and even investment firms can offer incentives like matching grants to promote 529 savings and postsecondary education attainment. These entities can cap the amount of investment they are willing to match. Currently, states like Colorado, Maine and Rhode Island offer annual matching contributions of \$200 to \$500 per beneficiary.<sup>16</sup> Some states match contributions dollar for dollar, while other states match a portion of the capped contributions.

In 2008, the California legislature created the Golden State ScholarShare Trust act, a trust account established to provide financial aid for participating college students through the California ScholarShare Advancement Vehicle for Education (CalSAVE).<sup>17</sup> The trust account is administered by the ScholarShare Investment Board, and open to all public entities for contributions. Using CalSAVE funds, California can begin to offer matching 529 contributions to identified groups.

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<sup>12</sup> Finance Authority of Maine, *Planning for College*, 2008.

<sup>13</sup> College Savings Plan Network, *Why Save For College*.

<sup>14</sup> *Ibid*.

<sup>15</sup> Anne Stuhldreher. "California Asset Building Policy Options: Providing All Californians a Stake in the Economy and a Means to Get Ahead," policy issue brief, October 2005.

<sup>16</sup> For information on other states go to [http://www.savingforcollege.com/compare\\_529\\_plans/](http://www.savingforcollege.com/compare_529_plans/).

<sup>17</sup> For more information on Senate Bill No. 1457 go to [http://www.leginfo.ca.gov/pub/07-08/bill/sen/sb\\_1451-1500/sb\\_1457\\_bill\\_20080928\\_chaptered.pdf](http://www.leginfo.ca.gov/pub/07-08/bill/sen/sb_1451-1500/sb_1457_bill_20080928_chaptered.pdf).

What can California do to match 529 savings?

- Using CalSAVE funds, begin by offering matching all or partial 529 contributions to participants in identified groups. .
- Identify entities in the private and government sectors that can contribute to CalSAVE or directly match individual 529 contributions.

### **Tax Incentives: Income-Tax Deduction and Purchase 529 Directly on the Tax Form**

Residents of twenty five U.S. states have the benefit of annual state income tax advantages on all contributions.<sup>18</sup> Californians would strongly benefit from similar programs. Although in most states the income tax deductions are small, studies have shown that even such small savings increase the takeup of 529s.

Reintroducing the Taxation Deposits and Qualified Tuition Bill (Senate Bill 918) may be an appropriate step towards adapting attractive and automatic savings methods.<sup>19</sup> SB 918 would allow California residents to designate an amount of their taxrefund to be applied towards their 529 savings.

Many studies show that people are far more likely to save if the money is taken directly from their paycheck.<sup>20</sup> Requiring California employers to offer payroll deductions will encourage more individuals to invest. Many larger employers already offer payroll deductions for IRAs and 401(K)s, so costs associated with payroll deductions for 529s will not be a large burden. For smaller employers, 529 management organizations, such as Fidelity in California, can offer to cover the cost.

What can California do to provide 529 tax advantages?

- Offer a capped state income tax deduction.
- Make the 529 savings process automatic by reinstating SB 918 which allows taxpayers to designate amounts of their tax refund to be directly applied to their 529.
- Encourage smaller employers to offer payroll deductions by giving them tax advantages and/or requiring investment organizations to cover a portion of the cost.

Now, more so than ever, California needs to offer its residents an incentive-rich education savings program. Adapting various forms of 529s that are currently in use in other states is a steppingstone to promoting savings for higher education in California. Conducting further research pertaining to what sorts of incentives will best encourage people to invest in 529s is yet another important step in enabling Californians to attain the American Dream of higher education and be better equipped to climb up the economic ladder.

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<sup>18</sup> David Braveman. *The Standard and Poor's Guide to Saving and Investing for College*. (New York: The McGraw Hill Companies, 2004).

<sup>19</sup> For more information on SB918 go to [http://www.leginfo.ca.gov/pub/07-08/bill/sen/sb\\_0901-0950/sb\\_918\\_bill\\_20070604\\_amended\\_sen\\_v96.pdf](http://www.leginfo.ca.gov/pub/07-08/bill/sen/sb_0901-0950/sb_918_bill_20070604_amended_sen_v96.pdf)

<sup>20</sup> Allison Ivey. *The Geek's Guide to Personal Finance*. (Crane Hill Publishers, 2006).