

## Arizona Republic

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### STATE STRUGGLES WITH PUBLICITY, PARTICIPATION IN 529 PROGRAM

*Russ Wiles, The Arizona Republic*

A recent article in the Wall Street Journal proclaimed Ohio soon would become the first major state-sponsored college-savings program to offer certificates of deposit as an investment option.

Ouch. It was another unintentional media slap at Arizona.

Arizona's Section 529 college program has offered the CD option for six years, one of the few states that do so. The oversight -- Arizona wasn't even mentioned in the article -- pointed up how the state has done little to promote investment and attention to its program.

Arizona's plan, with \$265 million in assets, has taken justified lumps in recent years for offering high-cost mutual-fund choices and lacking a state income-tax deduction.

It also can point to some strengths, including the CD option, which pays a yield tied to college-tuition inflation. That is coming at a good time, as investors grow more knowledgeable and picky about 529 features.

In trying to improve its 529, Arizona recently signed up Fidelity Investments to provide mutual funds for the program, and the company plans an advertising campaign that should boost general awareness, said Dr. April Osborn, executive director of the Arizona Commission for Postsecondary Education, which oversees the 529 plan.

"We've done a good job offering choices," said Dale Walters, a Phoenix certified public accountant and chairman of the Arizona 529 program's oversight committee. "But we've done a poor job of marketing and explaining the program."

Named after a section of the Internal Revenue Code, 529 plans have emerged as popular ways to save for higher education, combining tax breaks and other features. Every state but Washington offers its own plan, with the different programs in heated competition since investors, for the most part, are free to shop around.

Arizona's still is licking its wounds about studies in 2004 and 2005 by researcher Morningstar Inc. that branded Arizona's mutual funds as pricey. Morningstar labeled Arizona one of the five worst 529 plans. The same study cited 529 plans offered by Alaska, Colorado, Kansas, Michigan, Utah and Virginia among the best.

The negative publicity has left a bad taste in the mouths of some advisers.

"I think Arizona's plans are terrible, to be honest," said David Fernandez of Wealth Engineering LLC in Scottsdale.

Proponents insist the Arizona program is on the upswing, and landing Fidelity in June was a coup. The company is a giant in its industry and a pioneer in 529 plans, with a deep investment-research staff and several competitively priced funds. Bringing Fidelity on board should improve the program's standing by providing more moderate-cost fund choices.

Fidelity also agreed to develop a Spanish-language marketing brochure at the request of Arizona officials -- something that could bolster generally low minority participation rates in 529 plans.

Other changes made within the past year or so also are designed to improve the Arizona 529 program:

\* The state broadened the number and types of legal entities that can own 529 accounts. "Before, it was just individuals and charities," said Walters, chief executive officer at Keats, Connelly & Associates in Phoenix. Now corporations, partnerships,

trusts and other entities can own 529 accounts.

\* An effort to streamline marketing literature is under way. "Mutual funds are confusing to people in general," Osborn said. "That's why we're simplifying our materials."

\* Arizona accounts can be transferred to new owners -- as in the case of grandparents seeking to pass the torch to parents. Before, that wasn't allowed. This new provision shouldn't be confused with beneficiary changes, which routinely are allowed.

\* Arizona's Legislature strengthened the 529 program's oversight committee by adding more financial-industry practitioners.

\* Waddell & Reed, a provider of mutual funds to the Arizona plan, earlier this year agreed to cut expenses on its portfolios permanently. The Morningstar study cited high-cost funds from Waddell & Reed, Pacific Life Insurance and Securities Management & Research.

Looking ahead, any move by the Legislature to allow a state income-tax deduction on 529 contributions would enhance the plan's appeal.

Walters senses some support in the Legislature and Governor's Office for a tax break, although the timetable is uncertain.

Twenty-six states offer tax deductions to their residents, Osborn said.

#### Assistance with funding education

Here's how several local financial advisers view Section 529 college-investing plans:

Stephen Barnes, Barnes Investment Advisory, Phoenix

Cites the Nebraska program that features mutual funds from the Vanguard Group as a solid low-cost choice. He thinks 529 plans have drawbacks, including the potential for 529 assets to have a negative impact on financial aid. Also, Barnes considers the tax benefits relatively minimal since the plans lack a federal tax deduction.

Lynda Elley, Copperwynd Financial, Scottsdale

Likes 529 plans for college planning and recommends Virginia's CollegeAmerica program, which uses mutual funds from the American Funds. "They're good, steady and you can rely on them," she said of the American selections.

Elley favors individual funds, rather than portfolios with set asset allocations geared to kids of a certain age.

One caveat with the Virginia plan: The American Funds impose fairly high minimum investments of \$250 per fund.

David Fernandez, Wealth Engineering LLC, Scottsdale

Recommends 529 plans for clients and especially likes the Nevada program run by Vanguard.

"The fees are rock-bottom," he said, "and Vanguard provides good educational help and customer service."

Fernandez generally favors age-based funds, which Vanguard and others provide. These are portfolios with set asset allocations geared to children of various ages.

Timothy Radden, Northwestern Mutual Life, Phoenix

Generally doesn't recommend 529 plans and has no favorite state program. Among his concerns, Radden points out investments in 529 plans could hurt eligibility for financial aid. Also, if the named beneficiary doesn't go to college and the funds aren't transferred to someone who does attend, you will incur taxes and a penalty on the earnings portion when you reclaim the money, he said.

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