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What's New in College Savings Plans

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Conventional wisdom says 529 plans are the best way to save for college. These plans, based on rule No. 529 of the federal income tax code, are investment accounts that allow tax-free savings and withdrawals for qualified higher-education expenses. But as the economic climate has shifted dramatically, so have 529 options.

With a student's education depending on a solid 529 plan, what are the latest developments in these offerings? How can you take advantage of them if you've saved in another type of account or aren't happy with your current 529 plan? And has the economic crisis changed the rules of college savings?

No more 'set it and forget it'

Early on, most 529s offered age-based, asset-allocation strategies, says John Carl, president of Brainerd, Minn.-based Retirement Learning Center, which counsels financial advisers. The older your child grew, the more the plans shifted to a conservative mix of more bonds and less stocks.

Those plans still exist, but financial experts suggest you keep an eye on them nonetheless. The market has changed, and you'll want to take advantage of an array of new options.

For instance, if your plan's automatic rebalancing schedule says it's time to sell stocks and buy bonds as your child reaches college age, you might want to make a change, says Larry Glazer, managing partner at Mayflower Advisors, a financial consulting firm in Boston. It's probably not wise to sell stocks now after they've already fallen so far.

"The idea that you can park your money and not worry about it doesn't work," says Glazer. "You need to examine your funds periodically."

Index funds and ETFs

In recent years, index funds have become a hot item among 529 plans, says Joseph Hurley, a Bankrate adviser and founder of Savingforcollege.com (a Bankrate company), a Web site that provides information about funding higher education. Index funds invest in a basket of stocks or bonds that represents a particular benchmark, such as the Standard & Poor's 500. They are not "actively managed," meaning there's no trading of securities in reaction to changing market conditions. This keeps their fees lower than other funds'.

Also popular are exchange-traded funds, or ETFs, which are special securities designed to track groups of stocks or bonds, usually market benchmarks as index funds do, Hurley says. The primary difference between ETFs and index funds is that ETFs are traded like individual stocks, he says. Their price changes throughout the trading day while index funds have their value calculated only once a day.

ETFs tend to have an even lower expense ratio than index funds, except with ETFs you have to pay fees because they can only be bought and sold through brokers. "Among broker-sold (college) plans, ETFs are a fairly new development," Hurley says.

But if recent market volatility has soured you on stock funds, a number of more conservative instruments are available, including a variety of banking products.

"More 529 programs are offering FDIC-insured banking CDs or savings accounts," Hurley says. These certificates of deposit are insured by the Federal Deposit Insurance Corp. for up to $250,000.