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THE ROTH SOLUTION FOR COLLEGE SAVINGS

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If you have children or grandchildren whom you hope will go beyond high school and receive a college education, there's a good chance you've thought about setting some money aside to help pay their expenses. There are some terrific ways to do this, including utilizing 529 plans, but one savings vehicle that is often overlooked as a way to fund a child's college education is a Roth Individual Retirement Account (IRA).

Most people think of the Roth IRA as a terrific method to save for retirement — which it is — but it can also be a great tool to help you cover Junior's university tab. Unlike 529 plans, which can be used only to cover the costs associated with college, Roth IRAs can be used for both college expenses and retirement income.

While it's true that deposits into Roth IRAs receive no tax deduction, it's also true that these accounts then grow tax-deferred. So with a little planning, they can be an ideal source for funding a loved one's higher education.

Here's why: withdrawals from IRAs, including Roth IRAs, are actually exempt from withdrawal penalties if the funds are used specifically for qualified educational expenses, including tuition, fees, books and room and board.

For most people who are sending their kids off to college, only the contribution portions of their Roth IRA balances can be withdrawn tax free. (Any earnings in the account will be taxable for those people under 59, as well as for those over 59½ who haven't held the Roth for at least five years.)

But Roth IRAs enjoy a rather unique tax treatment. Withdrawals are treated as a "return of contribution" first and as earnings second. This means that a person who has been contributing $5,000 per year for the past five years can withdraw $25,000 tax free, provided the proceeds are used for qualified educational expenses.

Unfortunately, any money I've saved in the 529 plan that is not used for educational expenses will not only become fully taxable as ordinary income but will also be subjected to a 10 percent penalty. Unlike a 529 plan, a Roth IRA allows people who have funds left over after withdrawing for college expenses to convert those dollars to retirement income — with no tax consequences or penalties whatsoever. Simply put, this means that if Johnny or Jane doesn't use up all of the funds to pay for college, the remaining bucks can be used to supplement your own retirement income.

Roth IRAs do have some drawbacks. First, there are contribution limits. For 2015 the maximum, you can contribute is $5,500, or $6,500 for people age 50 and older. For a single taxpayer whose income exceeds $114,000, the Roth is phased out. For married folks the phase-out begins at $181,000.