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How to hit two targets with one account

Families with children typically have three important financial objectives: buying a home, saving for college, building retirement capital. That is a daunting challenge.

There are savings plans that come with tax benefits, which makes growing the account easier. For example, the traditional IRA offers tax deductions for contributions, and the Roth IRA provides the potential of tax-free payouts (contributions are subject to income limits). Both accounts defer taxes on account earnings.

The 529 plan is a popular approach for saving for college. Again, account earnings accumulate tax-deferred, and withdrawals used for qualified education expenses are tax free. However, earnings on funds not used for education may be subject to taxes and penalties. Many families cannot fund both education and retirement, so which one is better?

A new, bipartisan proposal made in June would resolve that question for many. The "College Savings Recovery Act," proposed by Democratic Senator Bob Casey of Pennsylvania and Republican Senator Richard Burr of North Carolina, would permit a direct rollover of unused 529 account assets into a Roth IRA. Funds not spent for education would be eligible for retirement funding.

There are some limits imposed on the rollover, however. The contribution limits for 529 plans are far greater than those for Roth IRAs. There is the potential for abuse of 529 plans to get around the Roth IRA limits, and that would be foreclosed in the legislation by requiring that the 529 plan be in existence for at least ten years and the rollover be no larger than the plan balance five years earlier.

Still, if this liberalization of 529 plans is adopted, it may tilt the savings priority decisively in that direction.