TESTIMONY

OF

MARIN GIBSON

ASSISTANT VICE PRESIDENT AND GENERAL COUNSEL
SECURITIES INDUSTRY ASSOCIATION

STATE GOVERNMENT AFFAIRS

BEFORE THE FINANCE COMMITTEE IN SUPPORT OF PENNSYLVANIA 529 PLANS, HB 529 AND HB 2096

FEBRUARY 2, 2006

Good morning, Chairmen Leh and Levdansky and Committee members. My name is Marin Gibson, and I am Assistant Vice President and Counsel, State Government Affairs, for the Securities Industry Association.[1] SIA brings together the shared interests of more than 600 large, medium, and small securities firms. We support state legislation across the country that extends equal tax treatment to all qualified 529 plans. It is therefore a pleasure to be here today to express SIA's strong support for HB 529 and HB 2096.

The timing of these bills to help Pennsylvanians finance higher education could not be better. There is a perfect storm brewing right now that will seriously threaten our ability to ensure a college education for our children:

* College Costs are Rising – Quickly!
For each of the past ten years, college costs have risen faster than inflation. Last year, four year public college/university costs rose 6.6% and four year private college/university costs rose 5.7%. It is projected that the cost of college in 15 years will be over $100,000 for public schools and $200,000 for private schools, assuming even a 5% annual cost increase.

* Families Are Not Saving Enough
This week, the U.S. Commerce Department announced that the personal savings rate of Americans dropped below zero. That's right: zero. The national savings rate as a percentage of disposable income was – 0.5%, the first negative savings rate since 1933 – the Great Depression.

* Student Loan Programs Under Pressure
Last month, Congress passed a funding cut for federal student loan programs of $12.7 billion over 5 years. This would increase interests costs by over $2000 on a $20,000 / ten year Stafford Loan.

Ensuring a strong public commitment to supporting Pennsylvania families saving for college will go a long way to helping turn the tide.

How does the average family even begin trying to save for such an important and daunting expense? Kiplinger, Savingforcollege.com, and a host of other entities consider 529 plans to be the best place to invest college savings.

What makes 529 plans so attractive? Earnings on most other college investment options, such as stocks, CDs, or mutual funds, are taxed at the *investor's* rate. A parent putting money away for college in one of these vehicles might have to give roughly 30% of any earnings back to the federal government in taxes. If, instead, the parent puts college savings money into a 529 plan, any earnings accrued are free from federal tax so long as those earnings are used for qualified education expenses.[2] This is a huge benefit, which effectively and dramatically increases the rate of return on the investment and results in more money to pay tuition and costs. This benefit was further improved upon when most states conformed their tax laws to ensure that 529 earnings were likewise not taxed at the state level.

SIA strongly supports HB 529 and HB 2096 because they will make 529 plans an even more attractive savings option for Pennsylvania residents.

There are two separate types of taxation that may affect 529 college savings accounts, and they are generally referred to as "front-end" and "back-end." I'll start with describing front-end tax treatment.

Currently, more than 25 states give their residents a state tax deduction for contributions made to a specific, state sponsored 529 plan. Clearly recognizing that encouraging college savings by Pennsylvania residents is good public policy, HB 2096 would extend this tax benefit to Pennsylvania residents who contribute to *any* qualified 529 plan.

There are several reasons why it is important to ensure an up-front tax incentive for savings in any qualified 529 plans.

First, limiting a state tax deduction to a single, state-sponsored plan effectively limits consumer choice. We want people to pick the 529 plan that is best suited for them. We want them to look at factors such as investment options, risk, manager reputation, expense ratio, and sales load. We do not want preferential tax status to be the sole or primary reason people select a particular 529 plan, yet that is the basis for a plan decision by far too many people.

Second, HB 2096 and HB 529 encourage competition among plans. When the tax playing field is level, 529 plans will compete for business based on factors such as plan performance, customer service, and fees. It is important to understand that when we come out to support tax parity legislation, we are not saying that the state sponsored program is not a good option. Indeed, the Pennsylvania TAP 529 program is a highly regarded college savings plan. What we are saying is that competition is good, and it will result in even better options for consumers. Pennsylvania's TAP 529 plan will not fall apart. Rather, it will continue to work hard to remain an attractive option for people living in Pennsylvania, and across the country.

Third, many Pennsylvania residents rely upon investment professionals to help meet their college savings needs. Because these investment professionals are knowledgeable about the family's entire financial plan, they are in a unique position to help Pennsylvania residents select the 529 plan that best fits their needs and goals. Extending equal tax treatment to all 529 plans allows Pennsylvania residents to continue working with trusted advisers, and allows those advisers to explore a wider variety of options before making investment recommendations.

Now to move from a discussion of front-end tax treatment to back-end tax treatment (or taxation on account earnings), an area in which Pennsylvania is somewhat unique. Most states do not tax earnings of 529 accounts. In fact, only two (2) states in the country tax their citizen's 529 account earnings from out-of-state plans, and Pennsylvania is one of those two states. HB 529 would bring Pennsylvania into alignment with the other states and provide parity, equity and clarity to Pennsylvania college savings investors. (fyi, Illinois, the other state with back end disparity, is moving forward to repeal the provision and expects repeal this session).

Finally, both HB 529 and HB 2096 are consistent with the original objectives of 529 plans. Qualified tuition plans are designed to be a flexible and portable investment option, since:

(1) they can be used equally at any accredited public or private undergraduate, graduate or professional program in the country;
(2) they are open to any investor, regardless of state residency; and
(3) they can be opened by any investor (whether a parent, grandparent or non-relative) for the benefit of any future student.

Proprietary state tax advantages are inconsistent with plan portability.

Thank you for the opportunity to appear today before the Finance Committee.
I would be happy to take any questions.

Footnotes:

1. The Securities Industry Association brings together the shared interests of approximately 600 securities firms to accomplish common goals. SIA's primary mission is to build and maintain public trust and confidence in the securities markets. SIA members (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. According to the Bureau of Labor Statistics, the U.S. securities industry employs nearly 800,000 individuals, and its personnel manage the accounts of nearly 93 million investors directly and indirectly through corporate, thrift, and pension plans. In 2004, the industry generated $236.7 billion in domestic revenue and an estimated $340 billion in global revenues.

2. As initially conceived, 529 plan earnings were taxed not at the parent/investor's rate but rather at the presumably lower tax rate of the child/beneficiary. The federal Economic Growth and Tax Relief Reconciliation Act (EGTRRA) of 2001 made earnings on 529 plans free from federal tax.