ROUND TABLE
WEALTH MANAGEMENT

Five Common Questions on 529 College Savings Plans

BY FREDERIC BEHRENS

Paying for college is one of the largest financial obligations for most parents. To make things more difficult, the cost of attending many public and private colleges has consistently increased at a rate above inflation for the past 30 years.[1] Fortunately, there are tax-efficient ways to save for college expenses.

One of the most common methods is using a Section 529 college savings plan. These special accounts are easy to establish and offer important tax benefits. 529 accounts are similar to brokerage and retirements accounts in that they may be invested into diversified mutual funds. The money in a 529 college savings plan may be used to pay for the college expenses and certain K-12 tuition of the beneficiary, tax-free. On the following pages are a few common questions related to using a 529 college savings plan.

1. What are the 529 plan's tax benefits?

The main 529 tax benefit is that earnings are tax-deferred while invested and tax-free when used for qualified expenses. Contributions to a 529 plan are made using after-tax dollars. In addition, some states allow for a small tax deduction each year for funds put into a plan. For example, contributions to a New York 529 plan of up to $5,000 per year by a resident individual ($10,000 per year by a married couple) can be deducted on a NY state tax return.

2. How much can I contribute each year to a college savings plan?

529 contribution limits are linked to the federal gift tax exemption limits published by the IRS. In 2019, gifts totaling up to $15,000 per recipient will qualify for the annual exclusion. There is, however, a special exception to 529 contribution limits, referred to as "super funding." Super funding allows for pre-funding up to five years of contributions in a lump sum (i.e. up to $75,000 individually or $150,000 jointly with a spouse). If the total lump sum allowance is utilized, no more contributions to the 529 plan may be made for five years. Reporting of super funding is required on a gift tax return.

[1] https://www.usatoday.com/story/college/2017/06/09/private-college-tuition-is-rising-faster-than-inflation-again/37432483/

3. Where can I spend 529 funds?

529 funds may be used at a wide variety of schools. This includes standard four-year universities, graduate schools, vocational/technical colleges, and even the Golf Academy of America (PGA pro school). Qualified higher educational expenses at an approved school include tuition, fees, room and board, books, supplies, computer technology, and special equipment. Schools publish an official annual cost of attendance which includes estimates for these expenses.

Starting in 2018, funds from 529 plans can also be used to cover tuition expenses at K-12 public, private, and religious schools. Parents can withdraw up to $10,000 per student annually to spend on tuition, but not on additional expenses or activities (529 funds may not be used for field trips or sports).

4. Which state 529 plan should I choose?

529 plans are run individually by different states. This does not mean you have to spend your 529 funds at a school located in the same state where the plan is located, and there is no requirement to select the plan for the state in which you currently reside. 529 funds may be used in any state and even some international schools for qualified expenses. If your home state offers a state tax deduction, it is usually recommended to use that plan. Otherwise, you should evaluate the investment options and fees of other states' 529 plans.

5. What happens if money is left over in a 529 college savings plan?

Funds in a 529 plan may be left in a plan after a beneficiary completes their education. It possible to transfer funds to another qualified beneficiary (most commonly a sibling). Leaving funds in a 529 plan may also be a great estate planning tool. Funds in a 529 plan are removed from the donor's estate and will continue to grow tax free. This could provide for many years of tax-free compounding for future generations. As a last resort, funds may be withdrawn from the 529 plan for non-qualified expenses, however, ordinary income tax plus a 10% penalty would be owed on any investment earnings in the account.

If you think a 529 Plan can help you reach your future college funding goals, contact your Round Table Wealth Advisor. They can help you determine which state's 529 plan is best, how much you should be saving into the plan each year, and how the account should be invested so that you are best prepared to fund ever-increasing college costs.

Frederic Behrens
Wealth Advisor

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