

## COLLEGE SAVINGS

### 529 Plans: What Are the Differences Between the Two Types?

Carrying a lot of student debt can be daunting. Luckily, 529 plans are designed to help head off that debt. Here are the main types of 529s and how they work.



(Image credit: Getty Images)

It's no secret that getting a college degree comes with a hefty price tag.

According to a report from Education Data Initiative, the average annual cost of tuition in the United States in 2024 is \$38,270. This price includes books, supplies and living expenses. That number goes down a bit for students attending college in-state, with the average annual cost being \$27,146, or \$108,584 for four years.

Entering the workforce with a six-figure debt can be debilitating, especially when entry-level job salaries aren't keeping up. According to a report from ZipRecruiter, the national starting salary for a recent college graduate is \$62,609, which is just over half the cost of getting a degree at an in-state school.

When it comes to employment, a report from Strada Institute for the Future of Work and the Burning Glass Institute found that 52% of recent four-year college graduates are underemployed a year after graduation. That number drops slightly for those who graduated a decade ago, with 45% still holding a job that doesn't require a four-year degree. When you couple that with current inflation rates, it can be extremely difficult to pay that debt off, bogging down some Americans for decades. Of course, there are scholarships and grants available to

help offset these costs, but there's another option families can take advantage of known as a 529 plan.

### **What is a 529 plan?**

Named after Section 529 of the Internal Revenue Code, 529 plans are tax-advantaged accounts that can be used to pay for educational expenses from kindergarten through graduate school. There are two types: education savings plans and prepaid tuition plans.

Education savings plans grow tax-deferred, and account holders can make tax-free withdrawals when the money is used for qualified education expenses. Prepaid tuition plans allow account holders to secure current tuition rates for future attendance. These funds can be used only for tuition and related fees. All other expenses, such as meal plans or room and board, will be charged at the institution's current rate.

Despite these plans being offered by all 50 states, only 30% of Americans utilized them in 2023, according to data from Education Data Initiative. The same report showed that 54% of parents were unaware that 529 plans existed. These plans are available to anyone and are typically opened by parents or grandparents for their children or grandchildren, who are listed as beneficiaries on the account. Each state has its own rules, fees and tax benefits associated with these accounts. Another nice perk is that qualified withdrawals aren't subject to federal or state taxes. However, for K-12 students, tax-free withdrawals are limited to \$10,000.

In addition to their various structures, there are some stark differences between the two types of 529 plans. With education savings plans, funds contributed to the plan are invested in a preset selection of investments. Account holders can choose what kinds of investments to make, and the account grows based on how those investments perform over time. Many plans offer target-date funds, which typically become more conservative as the beneficiary nears college age.

### **What 529 plans cover has been expanded**

The money can be used to cover tuition, fees, room and board and other related costs for both college and K-12 students. However, the federal government has made some expansions to the plans in recent years. Under the SECURE Act of 2019, the federal government allowed beneficiaries to use account funds to cover registered apprenticeship program expenses. These tax-free withdrawals can also be used to cover student loan repayments of up to \$10,000 for beneficiaries and their siblings. In 2022, the government expanded the plan further to help boost retirement savings. Under the SECURE 2.0 Act, \$35,000 of unused funds in education savings plans can be rolled into a Roth IRA account.

Prepaid tuition plans are a little different. These plans are offered only in a few states, along with select colleges and universities. As mentioned, these plans allow account holders to lock in current rates, even if the beneficiary isn't college-age. These plans are not eligible for any K-12 education expenses — and they don't cover the cost of room and board for college students. Similar to 529 education savings plans, withdrawals from prepaid tuition plans are not taxed, and the funds grow over time. It's important to note these plans are not guaranteed by the

federal government and may not be guaranteed by some states, depending on where you live, so make sure you understand those risks before opening an account.

529 plans are a great way for families to save money on education costs — especially when it comes to paying for college. Opening one of these accounts could lessen or even eliminate the amount of debt your child accrues until they graduate, saving them years of student loan payments. Furthermore, the funds in these accounts grow over time, allowing you to maximize your contributions. You may also be eligible for various tax benefits depending on where you live.

Despite continuous talk of student loan forgiveness and free tuition, a 529 plan can be a great way to help ensure your child has access to higher education, which will open a world of opportunities for them as they enter adulthood.

**NYSUT NOTE: Need advice on saving for college? Check out the NYSUT Member Benefits Corporation-endorsed [Financial Counseling Program](#) whose Certified Financial Planners® can provide objective and customized advice on college savings strategies and other planning needs.**

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