

## STUDENT LOANS

### **529s: No Longer the Ho-Hum Investing Device for College**

Changes to the plans allow for the savings to be rolled into a Roth IRA, as long as certain rules are met, if a child decides not to pursue their education.



(Image credit: Getty Images)

College 529 plans have been around for about 25 years. In fact, all those years ago, I launched the first public relations campaign explaining to parents and grandparents how they can save for their loved one's secondary education.

529 plans derive their name from Section 529 of the Internal Revenue Code. They were birthed because college tuition rates and costs were increasing at two to three times the rate of inflation. Student debt was mounting, and the government felt it had to offer tax-advantaged savings.

529s are a tax-advantaged savings plan to help pay for education. Originally, they were designed for post-secondary education costs, but in 2017, they were expanded to include K-12, and in 2019, they started including apprenticeship programs, as well.

#### **How popular are 529s?**

In 2021, total investment in 529s hit \$480 billion, but by 2022, that had fallen to \$411 billion, according to College Savings Plan Network. Some people started to back off from this investment because if you withdrew money from a 529 to use for a purpose other than the designated approved educational uses, you would have to pay a penalty.

## **New rules**

529 provisions in the SECURE 2.0 Act came into effect this year. SECURE 2.0 has lots of advantages, but with regard to 529s, it enables families to convert leftover 529 money into retirement savings that allows the avoidance of the penalty for non-educational withdrawals.

But there are a few rules you need to be aware of before setting up a 529, including:

- The 529 plan must be open for a minimum of 15 years before you can do a 529-to-Roth IRA transfer.
- The beneficiary of the 529 plan must also be the owner of the Roth IRA.
- 529 plan contributions made within the last five years aren't eligible for a tax-free transfer.
- There's a lifetime maximum of \$35,000 for 529-to-Roth IRA transfers.
- Roth IRA annual contribution limits apply.
- Always check into the fees that will be charged.

It can get confusing if you are not familiar with the Roth IRA rules.

You also can't contribute more in any given year to a Roth IRA than you earned in that year. So, if for example, a 529 plan beneficiary earns only \$3,000 in a year, that's the most they could transfer to their Roth IRA that year.

Finally, it's worth noting that if you do a 529-to-Roth IRA transfer, you may not put additional money into your Roth IRA that year if doing so would cause you to exceed the annual contribution limit. For example, the Roth IRA contribution limit is \$7,000 for 2024, which means you can transfer \$7,000 from your child's 529 plan to a Roth IRA in their name. They won't be able to make any additional IRA contributions in 2024 without incurring penalties. However, they could save for retirement in a 401(k) or some other tax-advantaged retirement plan.

## **Setting up a 529 for your loved ones**

There are over a hundred 529 plans in the U.S., and they are all offered via states. You don't have to use your state's 529 to get the benefits. They are tax-free at the federal level, and many states offer their residents a state income tax deduction or a tax credit for 529 contributions to one of their plans. Do some research into the plans available to you to learn more about the investment options you'll have and what kind of fees they charge before you open an account.

Once you've chosen your plan, you must fill out an application, providing information about yourself and your child. You can do this with help from your financial adviser.

Once your account is set up, you can fund it on the schedule that works best for you. That could mean making irregular contributions whenever you have the extra cash. Or you could set up automatic deposits on a recurring schedule. Many 529 plans are designed to easily accept financial gifts from other family members and friends as well.

I have always recommended that parents set up a 529 for their child at birth. Rather than receiving lots of scratchy baby clothes that need to be dry cleaned, wouldn't it be better to have your friends and family donate to your child's future?

## How a 529 plan works

Most 529 plans are pretty simple. You can have a savings plan locked-in rate or one that offers a variable rate. The IRS does not impose an annual contribution limit on 529s, but it does set limits on aggregate contributions, depending upon the state. In most cases, this means that you can contribute a large investment. But check with your accountant, because in most cases this contribution may be considered a gift by the IRS. The gift limit, without tax consequences, for this year is \$18,000 for an individual and \$36,000 for a married couple.

You'll also need to choose what to invest those 529 funds in. Just use common sense. When the child is young and has lots of time before college or other education, you can invest in a more aggressive portfolio. This provides time to recover from market downturns. But, as the withdrawal date gets closer, and you will need to count on the money being there, you should move the portfolio into more conservative investments.

I suggest that you try to have a regular investment schedule so you keep building the 529. One benefit is that you can change beneficiaries. That way, if one child decides not to pursue their education, you can switch — or you have the Roth IRA option.

My best advice is to remember that you should not compromise your own retirement savings to help your offspring with their education. They can always borrow for college; you can't borrow for your retirement. And frankly, if you have not saved enough for retirement, you may become an economic burden to your kids.

*This article was written by and presents the views of our contributing adviser, not the Kiplinger editorial staff. You can check adviser records with the SEC or with FINRA.*

### *About the Author*

#### **Neale Godfrey**

*Neale Godfrey is a New York Times #1 best-selling author of 27 books, which empower families (and their kids and grandkids) to take charge of their financial lives. Godfrey started her journey with The Chase Manhattan Bank, joining as one of the first female executives, and later became president of The First Women's Bank and founder of The First Children's Bank. Neale pioneered the topic of "kids and money," which took off after her 13 appearances on "The Oprah Winfrey Show."*

# Kiplinger