

### What Can I Do with Excess 529 Balances?

by Adam Leone, CFP®, ChFC®

We have received several questions lately about what to do with funds left in a 529 account after a child has graduated college. While this prospect seems to generate ominous feelings, saving too much money is not a bad thing. Faced with this scenario, there are several options to turn lemons into lemonade.

The first group of options involves simply leaving the funds in a 529 account. Just because the beneficiary of the account has earned their undergraduate degree does not mean the funds can't stay in the account. In fact, while a 529 plan may have its own rules, there is no IRS-imposed age deadline to make withdrawals from a 529. If there is a chance that the student will attend graduate school, simply leave the remaining balance in the account and enjoy tax-deferred growth. Another option is to change the beneficiary of the 529 account. If there is another child or family member who will be attending college or graduate school, the account owner could name them as the account beneficiary and request a withdrawal to pay for qualified educational expenses. The account owner can potentially change the beneficiary of a 529 account to his/her self or a member of their family. "Family" is defined by the IRS Publication 970. There may be tax consequences if the transferee does not fall in this stated definition of family.

If the account owner is the beneficiary's parent, naming the parent/account owner as the beneficiary may be an attractive option. Have you wanted to take a college course? If so, you can also use the 529 balance. One of the more interesting options involves so called experiential learning. The key point with 529 withdrawals is that to optimize the tax-free nature of the account, the funds must be used for qualified education expenses at an eligible institution that generally is eligible to participate in a student aid program administered by the Department of Education. However, qualified education expenses can also be somewhat non-traditional! Through a partnership with a University Extended Studies program, the outdoor education program Outward Bound has recently started accepting 529 funds as payment for their programs.

If none of these options are attractive, you can simply withdraw the remaining balance in your 529 account. Your balance is composed of principal and earnings, each of which should be detailed on your statement. There is no tax or penalty on the withdrawal of your principal, but the earnings portion of your balance will be taxed as ordinary income and will be subject to a 10% penalty. Note that all withdrawals are composed of both earnings and principal; you cannot withdraw just your principal. A simple example can illustrate the concept. Assume that you have \$50,000 left in a 529 account, which is comprised of \$30,000 of principal and \$20,000 of earnings. Liquidating the account would produce ordinary income of \$20,000 and a penalty tax of \$2,000. Assuming a combined tax bracket of 35%, the total tax owed on the distribution would be \$9,000. While individual circumstances will vary, the total tax owed is likely not very different from what would have been paid over time had the funds been saved outside of the 529 account.

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