

529 Plan Tax Benefits and New Rules on Roth Conversions

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Today's Presenter

- Lawrence Pon

- Lawrence Pon is a Certified Public Accountant, Personal Financial Specialist, Certified Financial Planner, Enrolled Agent, United States Tax Court Practitioner, and Accredited Estate Planner in Redwood Shores, CA
- Mr. Pon has been in practice since 1986 and speaks regularly to tax professionals on the latest tax planning and preparation topics.
- Mr. Pon teaches Income Tax at the College of San Mateo
- Mr. Pon received his BS in Business Administration from UC Berkeley and MS in Taxation from Golden Gate University in San Francisco

Objectives

- Tax Benefits of 529 Plans
- The Rules for Roth Conversions
- Strategies such as Dynasty 529 Plans

Ways to pay for college

- Community college
 - Save 39% by attending community college
 - \$3,800 average annual tuition and fees
 - Some cases free
 - Small class sizes
 - Taught by professor
 - Guarantee transfer to 4 year college

Ways to pay for college

- Financial Aid
 - Need-based aid
 - Scholarships
 - Merit based
 - Non-merit
 - Free rides
 - .3%
 - Sports scholarships
 - 1-2% of high school student athletes Division II college sports
 - New Supreme court ruling
 - FAFSA & CSAA

Ways to pay for college

- Loans
 - Private loans
 - Federal loans
 - Pandemic suspensions
- Average balances at graduation = \$39,351
 - Parent = \$28,777
 - Student = \$28,500
 - \$1.77 trillion
 - Auto loans = \$1.19 trillion
 - Credit cards = \$1.031 trillion
 - HELOC = \$335 billion

Ways to pay for college

- Saving and Investing
 - Families with a plan
 - 2 times more funds for college
 - More likely to start investing for college by age 6
 - 47% less student debt
- Custodial Accounts (UGMA/UTMA)
- Retirement Plans
- Life Insurance
- Home Equity Loan
- 401(k) loan
- 529 Plans

Custodial account (UGMA/UTMA)

- Kiddie tax considerations
- Child assumes control at age of majority
- Funds must be used for the child's benefit
 - Not necessarily for college
- High impact on financial aid eligibility
- Assets not removed from taxable estate if donor is also custodian

Pay For College with Retirement Funds?

- Less for retirement
- Penalty free for higher education costs
- Traditional IRA or Roth IRA
- Two in five Americans use retirement funds to pay for child's education
- 50% of withdrawals for college may count against federal aid as student income

Other Sources of College Funding

- Life insurance
 - Borrow against policy
- 401(k) loans
 - \$50,000 limit
 - What if you leave the company?
 - Interest rate?
 - Nondeductible interest
- Home Equity Loan
 - Not deductible
 - Interest rate?

529 Plans

- Tax free investing and withdrawals for qualified education expenses
- Account owner control for the life of the account
- No income limits on contributions or age restrictions on beneficiaries
- High contribution minimums
- Low impact on financial aid eligibility
- Assets removed from taxable estate
- Tax-free gifts of up to \$170,000 per beneficiary in a single year

Funding 529 Plans

- Gift Tax
 - \$17,000 annual gift tax exclusion per beneficiary
- Super-funding
 - 5 years of annual gift exclusion
 - 5 X \$17,000 = \$85,000
 - \$170,000 for Married Filing Jointly
- Annual gift exclusion used for 5 years
 - File Gift Tax Return
 - Form 709 – United States Gift Tax Return
 - Check box on Page 2, Schedule A, Line B
 - Check here if you elect under §529(c)(2)(B) to treat any transfers made this year to a qualified tuition program as made ratably over a 5-year period beginning this year.
 - Attach explanation

Funding 529 Plans

- Explanation on Form 709
 - The total amount contributed per individual beneficiary
 - The amount for which the election is being made
 - The name of the individual for whom the contribution was made
- Donor must outlive 5 years for a completed gift

Part 1 — General Information	1 Donor's first name and middle initial		2 Donor's last name		3 Donor's social security number		
	4 Address (number, street, and apartment number)				5 Legal residence (domicile)		
	6 City or town, state or province, country, and ZIP or foreign postal code				7 Citizenship (see instructions)		
	8 If the donor died during the year, check here <input type="checkbox"/> and enter date of death					Yes	No
	9 If you extended the time to file this Form 709, check here <input type="checkbox"/>						
	10 Enter the total number of donees listed on Schedule A. Count each person only once:						
	11a Have you (the donor) previously filed a Form 709 (or 709-A) for any other year? If "No," skip line 11b						
11b Has your address changed since you last filed Form 709 (or 709-A)?							
12 Gifts by husband or wife to third parties. Do you consent to have the gifts (including generation-skipping transfers) made by you and by your spouse to third parties during the calendar year considered as made one-half by each of you? (See instructions.) (If the answer is "Yes," the following information must be furnished and your spouse must sign the consent shown below. If the answer is "No," skip lines 13–18.)							
13 Name of consenting spouse				14 SSN			
15 Were you married to one another during the entire calendar year? See instructions							
16 If line 15 is "No," check whether <input type="checkbox"/> married <input type="checkbox"/> divorced or <input type="checkbox"/> widowed/deceased, and give date. See instructions:							
17 Will a gift tax return for this year be filed by your spouse? If "Yes," mail both returns in the same envelope							
18 Consent of Spouse. I consent to have the gifts (and generation-skipping transfers) made by me and by my spouse to third parties during the calendar year considered as made one-half by each of us. We are both aware of the joint and several liability for tax created by the execution of this consent.							
Consenting spouse's signature:				Date:			
19 Have you applied a DSUE amount received from a predeceased spouse to a gift or gifts reported on this or a previous Form 709? If "Yes," complete Schedule C							
Part 2 — Tax Computation	1 Enter the amount from Schedule A, Part 4, line 11					1	
	2 Enter the amount from Schedule B, line 3					2	
	3 Total taxable gifts. Add lines 1 and 2					3	
	4 Tax computed on amount on line 3 (see <i>Table for Computing Gift Tax</i> in instructions)					4	
	5 Tax computed on amount on line 2 (see <i>Table for Computing Gift Tax</i> in instructions)					5	
	6 Balance. Subtract line 5 from line 4					6	
	7 Applicable credit amount. If donor has DSUE amount from predeceased spouse(s) or Restored Exclusion Amount, enter amount from Schedule C, line 5; otherwise, see instructions					7	
	8 Enter the applicable credit against tax allowable for all prior periods (from Sch. B, line 1, col. C)					8	
	9 Balance. Subtract line 8 from line 7. Do not enter less than zero					9	
	10 Enter 20% (0.20) of the amount allowed as a specific exemption for gifts made after September 8, 1976, and before January 1, 1977. See instructions					10	
	11 Balance. Subtract line 10 from line 9. Do not enter less than zero					11	
	12 Applicable credit. Enter the smaller of line 6 or line 11					12	
	13 Credit for foreign gift taxes (see instructions)					13	
14 Total credits. Add lines 12 and 13					14		
15 Balance. Subtract line 14 from line 6. Do not enter less than zero					15		
16 Generation-skipping transfer taxes (from Schedule D, Part 3, col. G, total)					16		
17 Total tax. Add lines 15 and 16					17		
18 Gift and generation-skipping transfer taxes prepaid with extension of time to file					18		
19 If line 18 is less than line 17, enter balance due . See instructions					19		
20 If line 18 is greater than line 17, enter amount to be refunded					20		

Attach check or money order here.

Sign Here

Under penalties of perjury, I declare that I have examined this return, including any accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than donor) is based on all information of which preparer has any knowledge.

May the IRS discuss this return with the preparer shown below? See instructions. Yes No

Signature of donor _____ Date _____

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check <input type="checkbox"/> if self-employed	PTIN
Firm's name	Firm's EIN			
Firm's address	Phone no.			

SCHEDULE A Computation of Taxable Gifts (including transfers in trust) (see instructions)

A Does the value of any item listed on Schedule A reflect any valuation discount? If "Yes," attach explanation Yes No

B Check here if you elect under section 529(c)(2)(B) to treat any contributions made this year to a qualified tuition program as made ratably over a 5-year period beginning this year. See instructions. Attach explanation.

Part 1—Gifts Subject Only to Gift Tax. Gifts less political organization, medical, and educational exclusions. See instructions.

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was of securities, give CUSIP no. • If closely held entity, give EIN	C	D Donor's adjusted basis of gift	E Date of gift	F Value at date of gift	G For split gifts, enter 1/2 of column F	H Net transfer (subtract col. G from col. F)
1							

Gifts made by spouse—complete **only** if you are splitting gifts with your spouse and he/she also made gifts.

Total of Part 1. Add amounts from Part 1, column H

Part 2—Direct Skips. Gifts that are direct skips and are subject to both gift tax and generation-skipping transfer tax. You must list the gifts in chronological order.

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was of securities, give CUSIP no. • If closely held entity, give EIN	C 2632(b) election out	D Donor's adjusted basis of gift	E Date of gift	F Value at date of gift	G For split gifts, enter 1/2 of column F	H Net transfer (subtract col. G from col. F)
1							

Gifts made by spouse—complete **only** if you are splitting gifts with your spouse and he/she also made gifts.

Total of Part 2. Add amounts from Part 2, column H

Part 3—Indirect Skips and Other Transfers in Trust. Gifts to trusts that are indirect skips as defined under section 2632(c) or to trusts that are currently subject to gift tax and may later be subject to generation-skipping transfer tax. You must list these gifts in chronological order.

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was of securities, give CUSIP no. • If closely held entity, give EIN	C 2632(c) election	D Donor's adjusted basis of gift	E Date of gift	F Value at date of gift	G For split gifts, enter 1/2 of column F	H Net transfer (subtract col. G from col. F)
1							

Gifts made by spouse—complete **only** if you are splitting gifts with your spouse and he/she also made gifts.

Total of Part 3. Add amounts from Part 3, column H

(If more space is needed, attach additional statements.)

SCHEDULE A Computation of Taxable Gifts (including transfers in trust) (see instructions)

A Does the value of any item listed on Schedule A reflect any valuation discount? If "Yes," attach explanation Yes No

B Check here if you elect under section 529(c)(2)(B) to treat any contributions made this year to a qualified tuition program as made ratably over a 5-year period beginning this year. See instructions. Attach explanation.

Part 1 – Gifts Subject Only to Gift Tax. Gifts less political organization, medical, and educational exclusions. See instructions.

A Item number	B • Donee's name and address • Relationship to donor (if any) • Description of gift • If the gift was of securities, give CUSIP no. • If closely held entity, give EIN	C	D Donor's adjusted basis of gift	E Date of gift	F Value at date of gift	G For split gifts, enter 1/2 of column F	H Net transfer (subtract col. G from col. F)
1							

Gifts made by spouse—complete **only** if you are splitting gifts with your spouse and he/she also made gifts.

Total of Part 1. Add amounts from Part 1, column H

State Tax Considerations

- 30 states offer state income tax deductions for 529 plan contributions
- Seven parity states offer state tax benefit for contributions to any 529 plan
 - Arizona
 - Arkansas
 - Kansas
 - Minnesota
 - Missouri
 - Montana
 - Pennsylvania

Two Types of 529 Plans

- College savings
 - Most common
 - Available nationwide
 - Covers tuition, room & board and other college fees
 - More control over investment selection
- Prepaid
 - State-sponsored plans for in-state public universities
 - Private college 529 if certain child will attend the university
 - www.privatecollege529.com
 - Only tuition is qualified expenses
 - Performance is tied to tuition inflation

529 Plans

- Qualified higher education expenses
 - Tuition
 - Room and board
 - Books
 - Computer equipment
- Does affect financial aid
 - But not that much
 - 5.64%

529 Plan Withdrawal

- Non-qualified
 - 529 plan contributions are tax-free
 - Income tax on earnings
 - 10% penalty on earnings
 - Watch out for state penalties

529 Plans

- Leftover money
 - Beneficiary can be changed at any time to yourself or to *beneficiary's*
 - Child, stepchild, or legally-adopted child
 - Niece or nephew
 - Aunt or uncle
 - First cousin
 - If not used for higher education expenses
 - 10% federal tax penalty
 - Can be rolled over into ABLE account in the case of a disability.

Family Members

- Member of the family of the beneficiary
 - Son or daughter
 - Or a descendant of either
 - Stepson or stepdaughter
 - Brother, sister, stepbrother, stepsister
 - The father or mother
 - Or an ancestor of either
 - Stepfather or stepmother
 - Son or daughter of a brother or sister
 - Brother or sister of the father or mother
 - Son-in-law, daughter-in-law, father-in-law, mother-in-law, BIL, SIL
 - The spouse of the beneficiary
 - Or of any of the other forgoing individuals
 - First cousin of the beneficiary

K-12 Distributions from 529

- TCJA - \$10,000 from 529 for K-12 tuition
- State tax considerations
- Less money for college costs
- Time value of money

Why We Need to talk about 529s

- 57% of Americans are unfamiliar with a 529 college savings plan
- Only 23% of respondents to a survey have ever contributed to a 529 plan
- However student loan debt is very likely or somewhat likely for 54% of respondents

Is a Roth IRA an Alternative?

- 100% of growth is tax-exempt
- Less worry with “leftover funds”; still your money to withdraw
- No required minimum distributions
 - Except for five-year rule in the case of an inherited Roth.
- Convertible Accounts
 - Traditional IRAs
 - 401(k) plans
 - Profit sharing plans
 - 403(b) & 457 plans
- Beneficiary definition is less limiting
- Potentially simpler at tax time

Disadvantages of Roth IRA

- After-tax contributions
- Tax due on Roth conversions
- Income eligibility restrictions
 - \$218,000 for MFJ; \$153,000 for single
 - Some higher-income taxpayers might (very carefully) consider a back door Roth
- Penalties for early withdrawals
 - However, withdrawals can occur before 59 ½ if for education expenses.
 - Withdrawals are considered contributions until total is exhausted.
- May count more than 529 plans against financial aid.
- Consider both Roth and 529
 - Spend 529 funds first.

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PAYER'S/TRUSTEE'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone no.		1 Gross distribution	OMB No. 1545-1760 Form 1099-Q (Rev. November 2019) For calendar year 20 ____	Payments From Qualified Education Programs (Under Sections 529 and 530) Copy A For Internal Revenue Service Center File with Form 1096. For Privacy Act and Paperwork Reduction Act Notice, see the current General Instructions for Certain Information Returns.
		\$ _____		
PAYER'S/TRUSTEE'S TIN		RECIPIENT'S TIN		
		2 Earnings	3 Basis	
RECIPIENT'S name		\$ _____	4 Trustee-to-trustee transfer <input type="checkbox"/>	
		5 Distribution is from:		
Street address (including apt. no.)		<ul style="list-style-type: none"> • Qualified tuition program— Private <input type="checkbox"/> or State <input type="checkbox"/> • Coverdell ESA <input type="checkbox"/> 		
City or town, state or province, country, and ZIP or foreign postal code				
Account number (see instructions)				

Form **1099-Q** (Rev. 11-2019)

Cat. No. 32223J

www.irs.gov/Form1099Q

Department of the Treasury - Internal Revenue Service

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FILER'S name, street address, city or town, state or province, country, ZIP or foreign postal code, and telephone number		1 Payments received for qualified tuition and related expenses \$	OMB No. 1545-1574 2023 Form 1098-T	Tuition Statement Copy A For Internal Revenue Service Center File with Form 1096. For Privacy Act and Paperwork Reduction Act Notice, see the 2023 General Instructions for Certain Information Returns.
FILER'S employer identification no.	STUDENT'S TIN <input type="checkbox"/>	2	3	
STUDENT'S name		4 Adjustments made for a prior year \$	5 Scholarships or grants \$	
Street address (including apt. no.)		6 Adjustments to scholarships or grants for a prior year \$	7 Checked if the amount in box 1 includes amounts for an academic period beginning January–March 2024 <input type="checkbox"/>	
City or town, state or province, country, and ZIP or foreign postal code				
Service Provider/Acct. No. (see instr.)	8 Checked if at least half-time student <input type="checkbox"/>	9 Checked if a graduate student <input type="checkbox"/>	10 Ins. contract reimb./refund \$	

Form **1098-T**

Cat. No. 25087J

www.irs.gov/Form1098T

Department of the Treasury - Internal Revenue Service

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529 Rollover to Roth IRA

- 529 plan must be open for at least 15 years
 - What happens if the 529 beneficiary is changed?
 - New 15 year period?
- \$35,000 lifetime limit
 - Per 529 owner?
 - Per beneficiary?
 - Lucrative for a 529 owner with multiple beneficiaries
- Begins in 2024

529 Rollover to Roth IRA

- Roth IRA must be in the name of the beneficiary of the 529 plan
- Any contributions within the last 5 years (and earnings on those contributions) are ineligible to be moved to the Roth IRA
- Annual limit = IRA contribution limit for the year
 - Less any other IRA contributions
- Trustee to trustee
 - Plan to plan rollover

Sally's 529 Plan

- Remaining balance in 529 Plan = \$40,000
- 2024 Roth IRA contribution limit = \$6,500
- Sally transfers trustee to trustee \$6,500 from 529 Plan to her Roth IRA
 - No AGI limit
 - Earned income at least \$6,500
 - Cannot make additional Roth IRA contributions that year
- Continue until \$35,000 life time limit
 - Five years?

529 Rollover to Roth IRA

- Not subject to income limitations
- Tax planning consideration
 - Open 529 when child is born
 - Super 529
 - At age 16
 - Start moving funds to Roth IRA
 - Child will need earned income up to amount of IRA contribution limit
 - Summer job, part time job
 - Keep doing this until \$35,000 lifetime transfer limit is reached

529 Rollover to Roth IRA

- 529 Plans
 - No federal deduction for contributions
 - Withdrawals are tax-free used to pay eligible education expenses
 - Tuition
 - Fees
 - Books
 - Supplies
 - Equipment
 - Computer, software and internet access
 - Not gaming computer
 - No software for games

529 Rollover to Roth IRA

- Eligible expenses
 - Room and board if student is enrolled at least half time
 - Students living and eating off campus can use 529 funds for rent and grocery bills
 - Up to limits that are often similar to the school's charges for room and board
 - Typically cannot be used for transportation
 - Special-needs students can use them for a broad array of expenses that include transportation
 - Up to \$10,000 can be used to pay student-loan debt for beneficiary
 - Also siblings and stepsiblings

529 Rollover to Roth IRA

- Eligible expenses
 - Graduate as well as undergraduate expenses
- Taxable withdrawals
 - If 529 distribution larger than total eligible expenses
 - Tax plus 10% penalty is due on the earnings
 - Earnings reported on Form 1099-Q

529 Rollover to Roth IRA

- Transfers
 - 529 owners can switch the beneficiary on an account without tax consequences if it is to a family member
 - Broadly defined
 - Spouses
 - First cousins
 - Descendants
 - Siblings
 - 529 owners can leave accounts to others at death
 - Account can exist in perpetuity
 - Unlike IRAs and HSAs
 - No RMDs
- See Publication 970 - Tax Benefits for Education

Estate Planning & 529s

- Gift Tax Planning
 - Transfers not considered gifts
 - Payment of tuition to a qualifying educational organization
 - Unlimited amounts may be paid for tuition
 - Not part of the annual gift tax exclusion
 - Full-time and part-time students
 - Payments made directly to the educational institution
 - No exclusion for:
 - Books
 - Supplies
 - Dormitory fees
 - Board
 - Similar Expenses

Estate Planning & 529s

- Payment of tuition
 - Day care facilities that have an education curriculum
- PLR 200602002 & PLR 199941013
 - Prepaid tuition if payments made directly to a qualifying educational institution on behalf of a designated student enrolled in that school
 - Irrevocable
 - Cannot be transferred to another student
- Contributions to 529 Plan do not qualify for this exclusion

Estate Planning & 529s

- Leslie entered into 6 agreements with the Sandpiper College Preparatory School to prepay tuition for each of her six grandchildren
- Each agreement provides:
 - The funds would be used for the grandchildren's tuition
 - Any shortfalls caused by unforeseen tuition increases would be made up by Leslie or the child's parents
 - Any amounts not used for tuition for that grandchild would not be refunded or transferred to another grandchild
 - But would be forfeited and become the property of the school
- No gift tax consequences
- Death bed planning
 - No requirement for donor to be alive during the entire educational period

Estate Planning & 529s

- 529 contributions and earnings are generally removed from the donor's gross estate
 - Donor maintains total control over the account
 - Only contributions being spread over the five-year election are potentially includible in the donor's gross estate
 - Donor can name initial beneficiary
 - Can change beneficiaries at any time
 - New beneficiary must be a member of the previous beneficiary's family to avoid a taxable distribution
 - Note: If beneficiary dies
 - 529 included in beneficiary's gross estate

Estate Planning & 529s

- If beneficiary dies, account owner names new beneficiary, or
- Switches to a secondary beneficiary following the first beneficiary's death
 - Since no distribution from account, no taxable distribution
 - Proposed Regulations 1.529-8(d)(3)
 - Watch for guidance from IRS

Estate Planning & 529s

- Donald establishes 529s for two daughters – Ivanka and Tiffany
 - Ivanka goes to college and uses the 529
 - She has a daughter, Arabella.
 - Tiffany did not go to college
 - Her 529 is worth \$125,000
 - Donald rolls her 529 to Arabella
 - Rollover is to a generation below Tiffany
 - Treated as Tiffany making a \$125,000 taxable gift to Arabella, her niece

Estate Planning & 529s

- When opening 529 Plan
 - Designate Successor Participant
- Creating a family educational endowment
 - Designate children as successor owners
 - Dynasty 529 Plans

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