

## Always Have a Plan for Leftover 529 Plan Money

With the high cost of education, it's hard to envision that there might be money left over, but it does happen. Kids get scholarships; they might finish early; sometimes they quit school never to return.

In the case of 529 college savings plans, it's particularly important to have a backup plan for the possibility of leftover funds, not only to support another family member's educational goals, but as a potential addition to your estate planning.

As a refresher, a 529 college savings plans – named for the federal law that created them in 1996 – allow a parent to open a tax-deferred college savings plan with as little as \$25 to start in some states. You should know that a 529 college savings plan is NOT the same thing as a 529 prepaid college tuition plan. Prepaid tuition plans are just that – tax-deferred savings plans that allow you to save for tuition for in-state schools [though some plans allow you to transfer out a portion of those assets to out-of-state schools]. Also, it's important to note that prepaid tuition plans are not an automatic guarantee a student will get into that college.

As part of sweeping pension reform signed into law by President Bush in 2006, withdrawals from 529 plans are now permanently tax-free. In some states, contributions may also be deductible on state tax returns. All 50 states now have 529 plans college savings plans, and a majority of them provides additional incentives, such as a state-tax deduction to in-state residents who invest in their respective plan.

It's a good idea to have your financial adviser help you sort through the details of various state plans. There are various services – including Morningstar Inc. – that now rank the offerings of each state's plan. [SavingforCollege.com](http://SavingforCollege.com) and [finaid.org](http://finaid.org) are leading sites to help educate you in how these plans work.

So, if you've made all these moves, how should you handle surplus 529 funds? There are a few options:

**Change the beneficiary:** If Student #1 doesn't spend out the funds, you can replace the beneficiary with another blood relation – that means brother, sister, first cousin, even you or your spouse – to continue spending down those funds for educational expenses. Also, if you have a grandchild headed for college, you can arrange for your 529 plan to make the withdrawal payable to your grandchild as the beneficiary.

**Take a penalty and spend the money on whatever you want:** This isn't the most sensible financial option, but you do have the option to take leftover funds as a nonqualified distribution for your own non-educational use. However, you'll owe ordinary federal tax with an additional 10 percent on the earnings portion of the distribution. Don't forget state tax, either.

**Let your successor owner make the decisions.** When you apply for the account, you are asked to name a successor owner. When you die, you can simply trust the successor owner or the beneficiary of the funds to do what they want with the money.

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