

What is a 529 Plan?

Dear Client,

Saving for your children's or grandchildren's college costs can seem daunting, however 529 plans offer a tax-advantaged solution to help prepare for those bills. Let's take a look.

What is a 529 Plan?

A 529 plan, named after Section 529 of the Internal Revenue Code, is a state-sponsored savings vehicle to help families save for education expenses. The most common type, the college savings plan, allows tax-deferred growth and tax-free withdrawals for qualified education expenses. Anyone 18 or older can open a 529 plan for a beneficiary with no residency restrictions.

Tax Advantages

Earnings grow tax-deferred, and withdrawals for qualified expenses are free from federal income tax and California state income tax. While California does not offer a state tax deduction for contributions, many other states do, making out-of-state plans an option.

Contribution Limits:

The contributions you make to the 529 plan are treated as gifts to the student. In 2025, you can gift up to \$19,000 (or \$38,000 if you're married and file taxes jointly) per beneficiary of the plan, without these gifts being counted towards your lifetime gift tax exemption.

If you want to contribute more to a 529 account in a single year without counting against your lifetime gift tax exemption, the account can be "superfunded." You can fund a 529 plan with up to 5 years' worth of contributions all at once. That means an individual can contribute up to \$95,000 in a single year to a particular 529 plan in 2025. But you couldn't give more money to that same recipient within that 5-year period without counting against your lifetime gift tax exemption.

Qualified Distributions

Withdrawals from a 529 plan are tax- and penalty-free when used for qualified education expenses, including:

- Tuition, fees, books, supplies, room/board and equipment at eligible colleges, trade schools, or vocational programs.
- Up to \$10,000 per year for K-12 tuition at private, public, or religious schools.
- Up to \$10,000 lifetime per beneficiary (and per sibling) for student loan repayments.
- Expenses for registered apprenticeship programs (e.g., fees, books, supplies).

Options If the Beneficiary Doesn't Go to School

If the beneficiary does not pursue college or other qualified education, you still have several options to manage the funds:

1. *Change the Beneficiary*: Switch to another eligible family member (e.g., siblings, parents, children, grandchildren, first cousins, nieces, nephews, or even the account owner (e.g., for their own education) for their qualified education expenses, with no tax or penalty.
2. *Roll Over to a Roth IRA*: Since 2024, up to \$35,000 can be transferred to the beneficiary's Roth IRA, tax- and penalty-free, if the account is at least 15 years old and the beneficiary has earned income (subject to annual Roth contribution limits for the beneficiary, e.g., \$7,000 in 2025).
3. *Non-Qualified Withdrawals*: Withdraw funds for non-education purposes, but earnings are subject to federal income tax and a 10% penalty, unless an exception applies.
4. *Special Exceptions*: For example, children born with disabilities or special needs can allow you to convert a 529 plan into an ABLÉ (Achieving a Better Life Experience) account to help pay for additional qualifying expenses. Other extenuating circumstances include: military academy, scholarships, death, and disability.

Where to Find a 529 Plan

In California, the ScholarShare 529 College Savings Plan is the state's official plan.

As always, please feel free to contact us if you have any questions.

Yours truly,

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