WEALTH SOLUTIONS GROUP

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Grandparent Owned 529 College Savings Plan

Frequently Asked Questions

This flyer addresses questions on how grandparent or non-parental owned 529s are treated for financial aid purposes, control of the asset, 529 gift-tax consequences, as well as 529s and Medicaid.

529 College Savings Plans

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What is a 529 plan?	A 529 College Savings Plan is a qualified tuition program, created by Section 529 of the Internal Revenue Code in 1996, which is operated by a state or educational institution. Savings plans allow participants to save money on behalf of a designated beneficiary for qualified higher education expenses (QHEE), as well as up to $10,000 per year to cover the cost of K-12 expenses while enrolled in a public, private or religious school. Your investment grows tax-deferred, and distributions to pay for the beneficiary's educational costs are federal tax-free. Note that distributions for K-12 may trigger state income tax and penalty if your state has not adopted the K-12 tax code provision.
Am I hurting my grandchild's eligibility for financial aid by putting money into a 529 plan for him?	Simply owning a 529 account for your grandchild will not affect your grandchild's eligibility for need-based financial aid, but actually using the account could have a negative impact in subsequent years. The value of assets owned by a grandparent (or other non-parent) is not reportable on the FAFSA financial aid application. However, if a grandparent provides any type of financial support to the student, that support is reportable on the FAFSA as student income. The financial aid formula counts student income just as it counts student assets (although the assessment percentages and allowances are different).
When is the best time to use the 529 for my grandchild so as to not reduce federal financial aid?	A student's financial aid package can be reduced by as much as 50% of the value of student income reported on their FAFSA. That means if a grandparent gifts $10,000 to help pay for his grandchild's college this year, it could effect a future financial aid package and reduce the student's federal financial aid by $5,000. This includes withdrawals from a 529 plan. To avoid this, we typically advise grandparents to wait until the grandchild's sophomore year, after the second-to-last FAFSA is filed.
If I take a distribution to pay for my grandchild's education expenses, how does the school know that I provided the aid?	The school won't necessarily know the source of the funds. But, the FAFSA instructions require that any financial support to the student from a third party be included in the prior-prior year student income. The FAFSA notes state: *"Money received, or paid on your behalf, also includes distributions to you (the student beneficiary) from a 529 plan that is owned by someone other than you or your parents (such as your grandparents, aunts, uncles, and non-custodial parents). You must include these distributions amounts in question xx."* The school may and can inquire more deeply during its financial aid verification process. And of course, it can be fraud to knowingly exclude this source of the funds.

If I encounter unplanned medical expenses or other financial needs can I get my money back out of a 529 plan?	Yes. You have the ability to withdraw the funds at any time and for any reason. But, if the withdrawal is not for qualified higher educational expenses you will pay income tax and a 10% penalty on the earnings portion. This flexibility should relieve any concerns you might otherwise have about "giving" your money away. Other types of gifts (trusts, family partnerships, UTMA accounts, etc.) are not revocable, making the 529 plan unique in this respect. Even though your contributions to a 529 plan are revocable, they are treated as completed gifts from you to the 529 account beneficiary, and the 529 account value is removed from your taxable estate.
Can I make contributions to the 529 accounts my children have already established for my grandchildren?	Most 529 plans accept “third-party” contributions. You may make your contributions to your child’s account and not have to worry about opening and maintaining your own accounts. But, because you are not the owner of the 529 account, you will no longer have access to these funds. To make contributions to an account owned by someone else you will need: ▪ The 529 Plan account number and indicate that number on your check. ▪ Make the check is made payable to the 529 plan not the account owner. For the few 529 plans that do not accept third-party contributions, your options are: ▪ Open your own accounts ▪ Give the parents cash and request that they put it into the 529 accounts for your grandchildren.
Do my contributions to a 529 have gift-tax consequences?	You can contribute up to five times the annual gift allowance of $15,000, per beneficiary in a single year without gift tax as long as no additional gifts are made to the same beneficiary during the next four years. This means that you can contribute up to $75,000 for your beneficiary today and elect to treat your contribution as made over a five calendar-year period for gift tax purposes. Married couples who file jointly can contribute up to $150,000 per beneficiary. Your contribution is treated as a gift to the named beneficiary for gift tax and generation-skipping transfer tax (GSTT), thus the appreciation is out of your estate. You elect the 5-year gift averaging on IRS Form 709. State tax deductibility of your contributions is another issue you should understand. Many states provide their residents with a deduction for at least some of their contributions to the in-state 529 plan. Several states require that you be the account owner in order to claim the deduction.
What happens to my 529 plan if I die or become incapacitated?	Your 529 account will not terminate. When you establish a 529 account, the application lets you name a successor owner. We recommend that you make this designation, as it will allow ownership of the account to be transferred easily and automatically to your named successor. If you do not designate a successor, the new account owner may have to be decided through probate. The successor owner you name will assume all the rights of the original owner, including the right to request a refund. You must have confidence that the person you name as successor will fulfill your desires for the use of the 529 account. If you have any concerns about this, speak with your attorney about the possibility of naming a trust as successor.
If I ever need to go to a nursing home and apply for Medicaid benefits, will the 529 accounts I have set up for my grandchildren be counted as part of my assets?	Check to see if your state still applies an assets test for Medicaid eligibility purposes, and whether the test was eliminated or modified in 2014 as required by the Affordable Care Act. The states that considered assets when testing for Medicaid eligibility generally treat 529 accounts as "countable" assets. Because 529 plans permit you to take the money back, those funds could be considered available to pay for your nursing home and other medical expenses. If you are concerned about maximizing Medicaid eligibility you should discuss with your attorney your desire to use 529 plans. You may wish to make someone else the owner of the 529 account. If you establish the 529 account under your own name, and later transfer ownership of the account to someone else (or even use the account to pay for college expenses), your Medicaid eligibility may be restricted by the “look-back” rules which cover transfers up to 36 months or 60 months prior to application for Medicaid.

How can I select the right 529 plan if I don't know where my grandchildren will be attending college?	**529 saving programs** can be used at any educational institution where federal student aid is available, whether or not the school is located in the state sponsoring the 529 plan. Eligible institutions include private colleges, public universities, community colleges, graduate schools, and trade schools around the country. Foreign schools may also be eligible. You can check the eligibility of any specific institution, or find the federal school code on the FAFSA website, www.fafsa.ed.gov.
I make annual gifts to my grandchild's custodial account (UTMA) intending that those funds to be used for college. Is there anything wrong with this approach?	Remember that UTMA and UGMA accounts are treated as student assets and therefore count heavily against financial aid eligibility. And they become the direct property of the child at a certain age established under state law. At that time the child can use the funds for any purpose they want even if it's not what you or the parents want. Another consideration is the burden your gifts may place on the parents who may need to file income tax returns annually. The earnings in the UTMA account are subject to annual capital gains and income taxes at the new trust tax rates, and the kiddie tax rules may also apply. Kiddie taxpayers include children under the age of 18 (as of December 31), 18-years-olds who are not self-supporting*, and full-time college students ages 19 through 23 who are not self-supporting. **To be self-supporting, taxpayers must have earned income (i.e. wages) exceeding one-half their total support.* The revised kiddie tax rules expire after 2025 and revert back to the law in effect for 2017.
What happens if I have money in a 529 account for a grandchild who later decides to not attend college?	One option you have is to change the beneficiary to another member of the family. That could be the current beneficiary's brother or sister. It could also be the beneficiary's cousin. You could even move the beneficiary up or down the family tree, naming the beneficiary's child, parent, or even yourself as replacement beneficiary. Another option is to withdraw the funds from the 529 plan to use for yourself. However, you probably won't want to do this unless you have a real need for the funds because you will have to pay income tax and a 10-percent penalty on the earning. The fact that the account beneficiary can be changed as many times as you want means that any excess funds in your 529 plan can remain there to be passed down from generation to generation (check to see if your 529 plan has a restriction on how long the account can stay open—most do not).

Investors should consider the investment objectives, risks, charges and expenses associated with a 529 Plan before investing. This and other information is available in a Plan's official statement. The official statement should be read carefully before investing.

Depending on your state of residence, there may be an in-state plan that provides tax and other benefits such as financial aid, scholarships and creditor protection that are not available through an out-of-state plan. Before investing in any state's 529 plan, you should consult your tax advisor.