

Using 529 Education Savings Plans to Fund a Roth IRA



At the start of 2024, a new saving opportunity began that allows you to shift certain unused funds from a 529 education savings plan tax free to a Roth IRA. This ability to move tax-advantaged education savings to retirement savings, free of federal income tax or penalties¹, is one of a kind.

The new provision is designed specifically for long-term unused 529 education savings plan balances (those at least 15 years old) and will permit up to a lifetime limit of \$35,000 to be used to fund a Roth IRA. This may offer some peace of mind for parents (or other 529 plan account owners) concerned about beginning a 529 education savings plan for children who may not go to college or in situations where students have completed their educational journey and have funds left over. Considering that nonqualified 529 education savings plan withdrawals result in income taxes and a 10% penalty on the tax-deferred earnings distributed, this new alternative is

an excellent way to continue to defer income taxes while beginning or enhancing a retirement savings strategy.

How It Works

To take advantage of this new opportunity, here are a few things you need to keep in mind:

- **15-Year Rule.** The 529 plan must be established for at least 15 years before a transfer to a Roth IRA can occur.
- **5-Year Rule.** Contributions (and associated earnings) in the 529 plan during the prior five years are not eligible to be transferred to a Roth IRA.
- **Same Person.** The Roth IRA must be established in the name of the 529 plan beneficiary.

¹State income tax treatment will vary. Recapture of state income tax deductions may apply. Check with your tax advisor.

Retirement Planning

- **Earned Income Is Required.** The account owner of the Roth IRA is subject to the same earned income requirement that applies to all IRA contributions. In order to fund a Roth IRA, you (or your spouse, if married and filing a joint income tax return) must have employment income.
- **Roth IRA Annual Contribution Limits Apply.** Annually, only amounts up to the Roth IRA contribution limit may be moved from the 529 plan to the Roth IRA. The maximum Roth IRA contribution limit is 100% of earned income or \$7,000 (for 2024), whichever is less.
- **Roth IRA AGI Limits Do Not Apply.** However, the modified adjusted gross income (MAGI) limits that typically apply to Roth IRA contributions do not apply when using a 529 plan to fund the Roth contributions.

Additional Clarity Needed

There are some questions remaining that future guidance hopefully will address. For example, it is not clear what rules will apply if the beneficiary of the 529 plan is changed to another eligible family member or if a 529 savings plan is moved from one state's plan to another. It is not known if either of these events will require a reset of the 15-year rule discussed above.

How Benjamin F. Edwards Can Help

If you have long-term unused 529 plan balances and would like to explore funding a Roth IRA, or you would like to begin or enhance your 529 savings plan strategy, reach out to Benjamin F. Edwards for help. A financial advisor can review your situation and work with you and your tax advisor to develop a strategy that will best meet your needs. ■

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