What Can I Do With Leftover 529 Funds?

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In a world of skyrocketing tuition rates, it may come as a surprise that some beneficiaries don't use all the money in their 529 plan. On the other hand, some never touch the account, either because they decide not to pursue higher education or because they receive full financial aid coverage. If your beneficiary is left with extra funds, don't worry – there are a handful of options on what to do with the account.

What Are My Options?

Save for future educational needs

Even if the beneficiary doesn't need the funds right now, keeping the money in the 529 plan may make sense down the road. It'll be ready and waiting for them in case they decide to go to graduate school or pursue another degree.

Transfer to a qualified family member

If the current beneficiary doesn't need the funds, you can transfer the 529 plan to one of their family members. This includes siblings, step-siblings, parents, children, first cousins, nieces, and nephews. For instance, if your son decides not to attend college, you can easily switch the account to your daughter or even to yourself.

It's best to transfer the account to a qualified family member, as transferring it to anyone else could result in tax consequences. If you plan to transfer the account, note that you can only change the beneficiary twice a year.

Pay off student loans

Leftover funds can be used to pay off the beneficiary's or their sibling's private or federal student loans. If neither has student loans, you can transfer the account to another qualified family member who does. However, there is a maximum lifetime limit of $10,000 per borrower and the portion used to pay student loan interest is not eligible for the student loan interest deduction.

Roll it over to a Roth Individual Retirement Account (IRA)

Under the SECURE 2.0 Act, unused 529 funds can be transferred to the beneficiary's Roth IRA without taxes or penalties starting in 2024. However, there are a few stipulations to this rule:

- The 529 plan must have been opened for at least 15 years
- The amount being transferred was contributed to the 529 plan at least five years prior
- You need to follow the Roth annual contribution limit ($6,500 in 2023)
- The total lifetime maximum for a 529-to-Roth rollover is $35,000

Withdraw it

If all else fails, you can always make a non-qualified distribution which will result in ordinary income tax and a 10% penalty. Taxes are only levied on the investment earnings within the account – your original contribution will be distributed tax-free. Since this can be a significant chunk of your distribution, withdrawing the money for non-qualified expenses should be treated as a last resort.

There are some exceptions to the 10% penalty. If the beneficiary died, became disabled, or decided to join a U.S. military academy; then you may be able to take a non-qualified withdrawal without the penalty. If the beneficiary received a qualified scholarship, you could withdraw the scholarship amount from the 529 plan penalty-free. However, earnings are still subject to income tax.

The Bottom Line

When it comes to 529 plans, individuals often open them with the expectation that their beneficiary will attend college. However, circumstances may change, and they may not need as much funding as anticipated. If you find yourself with an unused account or leftover funds, you have several available options to make the most of your savings.