FPA FINANCIAL PLANNING PERSPECTIVES

Understanding 529 Plan Distributions.

Parents looking to take advantage of the many benefits of saving for college with a 529 plan will want to know the full details on which educational expenses qualify for tax-free distribution status -- and which do not.[1] In Publication 970, the IRS gives detailed guidance on qualified expenses. Here are a few important points.

What's Covered

- Tuition and fees are covered in full.
- Room and board, if the student is enrolled at least half time. But such expense must be not more than the greater of (1) the allowance for room and board, as determined by the school, that was included in the cost of attendance; or (2) the actual amount charged if the student is residing in housing owned or operated by the school.
- Food. If you spend a certain amount for a meal plan, that entire amount can be deducted, even if used for coffee or ice cream and not a full meal. Weekend meals can also be included if the dining halls are not open.
- Books and supplies. Any fees associated with purchasing school textbooks are considered qualified, as are required equipment or supplies such as notebooks and writing tools.
- Computers/laptops, but only if required by the school. If required, Internet fees and PDAs or "smartphones" may also qualify. The Savings Enhancement for Education in College Act (H.R. 529) that is currently being considered by Congress would expand this definition to apply to all computer technology used by the student.
- Special needs services required by special-needs students that are incurred in connection with enrollment or attendance at school.

What's Not Covered

- Student loans. Interest on or repayment of student loans is not considered a qualified expense by the IRS.
- Insurance, sports or club activity fees, and many other types of fees that may be charged to students but are not required as a condition of enrollment.
- Transportation to and from school.
- Concert tickets or other entertainment costs, unless attendance is requisite to a course or curriculum.

Note that expenses must apply to a qualified college, university, or vocational school for post-secondary educational expenses. Also keep in mind that taxes and a possible 10% penalty will apply to all distributions that are not considered qualified educational expenses by the IRS, so be sure to check first.

[1]By investing in a 529 plan outside of the state in which you pay taxes, you may lose the tax benefits offered by that state's plan. Withdrawals used for qualified expenses are federally tax free. Tax treatment at the state level may vary.

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