Should You Use 529 Plan Funds on K-12 Education?

Federal law says you can, but you may want to think twice about it.

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When President Trump signed the Tax Cuts & Jobs Act into law late in 2017, new possibilities emerged for the tax-advantaged investment vehicles known as 529 college savings plans. Funds from these accounts may now be used to pay for qualified elementary and secondary school expenses under federal law.[1]

Unfortunately, some state laws for 529 college savings plans are just catching up with federal law or treat such withdrawals differently from a tax standpoint. Hopefully, these differences will be resolved with time.[2]

Federal law permits you to spend up to $10,000 of 529 funds on K-12 tuition per year.

Under the Tax Cuts & Jobs Act, you can use these funds to pay tuition at private and public elementary and secondary schools. If you do this, the withdrawal from your 529 plan is tax free or at least free from federal taxation.[1]

The question is how the state hosting the 529 account treats the withdrawal.

Some states, such as Missouri and Tennessee, quickly indicated they would allow 529 plan withdrawals for qualified K-12 education expenses

and treat the withdrawals in the same fashion as the new federal law. Other states took a different approach. Louisiana's state legislature, for instance, complemented the state's 529 college savings plan with new K-12 education savings accounts in June.[3]

While your state's 529 plan may allow you to withdraw funds to pay for qualified K-12 education expenses, the state and federal tax treatment of the withdrawal may differ. The distribution could be taxed at the state level, even if untaxed at the federal level. That is the case in Oregon, for example.[2,4]

You may or may not want to use 529 plan funds in this way.

The Tax Cuts & Jobs Act basically redefined 529 savings plans as education savings accounts rather than solely college savings accounts. The added versatility is nice, but chances are, you have been saving money for a college education in a 529. Do you really want to draw down a tax-favored account capable of compounding to pay K-12 education expenses today instead of college costs tomorrow? Like an early withdrawal from a retirement account, this may be a decision that you come to regret.

If you are independently wealthy or anticipate having the financial ability to cover college costs in some other way, then partly or wholly reducing your 529 plan balance might be bearable. If your household is middle class, it could simply be a bad idea.

Of course, 529 plans are just one of the ways available to save for college.

You should explore your options to build education savings. A chat with a financial professional well versed on the topic may give you some ideas.

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CITATIONS

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