

Qualified State Tuition Program Basics

Eligibility:

There are no income or age restrictions on participating in a qualified state tuition program, also known as a Section 529 plan. In addition, some state plans are available to non-residents of that state.

Contributions:

The maximum amount that can be contributed to a Section 529 plan varies from state to state, but can be substantial.

Deductibility:

Contributions to a Section 529 plan are not deductible for federal income tax purposes. Some states, however, allow residents to deduct contributions from state tax returns.

Earnings:

Earnings on Section 529 plan contributions grow tax free for as long as the money remains in the plan.

Distributions:

Qualified distributions: If used to pay for qualified higher education expenses (e.g., tuition, fees, books, supplies, computers and computer technology), distributions from both state-sponsored and privately-sponsored tuition plans are free from federal income tax.

Non-qualified distributions: The earnings portion of the distribution is subject to federal income tax plus a 10% penalty tax.

Flexibility:

- The donor remains in control and decides when withdrawals are taken and for what purpose.
- Amounts can be rolled over tax free from one Section 529 plan to another as often as once every 12 months without the need to change beneficiaries.
- States offering prepaid tuition plans generally will allow the value (as determined by the state) to be transferred for use at a private or out-of-state school.
- The qualified beneficiary of the plan can be changed at any time.
- While subject to income tax and possibly a penalty tax (see above), non-qualified withdrawals can be made from the plan for any purpose.
- Made permanent by the Pension Protection Act of 2006.