

Quick-Take: We have previously covered recently the ‘new’ rule that permits the transfer of excess (or unused) funds from a 529 account to a Roth IRA. This rule came into play with the SECURE Act 2.0. This rule is intended to address a concern of many who funded a 529 account that they would be hit with a 10% penalty by over-funding a 529 account, e.g., the beneficiary earns a scholarship or decides to not attend college. Starting in 2024 the SECURE Act 2.0 allows a rollover from a 529 account with ‘excess’ funds to a Roth IRA. As reported previously, there are several limitations to deal with before this new rollover opportunity and be exploited.

529 to Roth IRA Limitations: The limitations on a rollover of unused 529 funds to a Roth IRA include the following:

1. **Roth IRA Owner:** The **529 beneficiary** must be the owner of the Roth IRA to which the ‘excess’ 529 funds are rolled over.
2. **Multiple 529 Accounts:** The Act allows the 529-to-Roth IRA limits to be applied per beneficiary. Therefore, if a parent has opened several 529 accounts, one for each child, thus the parent could rollover the ‘excess’ 529 funds, up to the maximum amount, into a Roth IRA established for each of his/her children.
3. **Maximum Lifetime Amount:** The maximum lifetime amount that can be rolled over from a 529 plan to a Roth IRA is **\$35,000**. At this point, this \$35,000 amount is not indexed to annual cost-of-living- it is a flat \$35,000.
4. **Limited to Annual Roth IRA Contribution Limit:** The maximum

amount that can be rolled into a Roth IRA in a year is limited to the **annual Roth IRA contribution limit**. If an individual is under the age of 50 years, the most that they can contribute to a Roth IRA in 2024 is \$7,000. Therefore, if a 529 account holds an excess of \$28,000 in it, the most that could be rolled from the account to the beneficiary's Roth IRA is \$7,000 in 2024. If the contribution limit is not changed for 2025, another \$7,000 could be rolled from the 529 account with excess funds to the Roth IRA in 2025, and so on.

5. **Long-standing 529 Account:** For the excess funds held in the 529 account to be eligible to be rolled over to a Roth IRA, the 529 account must have been in existence for **at least 15 years**. Currently it is unclear, and no doubt will remain unclear until the IRS gets around to publishing proposed Regulations, whether the 15-year 529 account durational requirement is determined from the inception of the 529 account, or will the 15 years be measured from when the last beneficiary became the beneficiary of the 529 account, since the owner of the 529 account is always free to change its beneficiary.
6. **Beneficiary's Earned Income:** The 529 account beneficiary who does the rollover **must have compensation in the year of the rollover at least equal to the amount being rolled over**. I've read a couple of articles where examples were provided that the parent to who opened the 529 account for their child could cause the rollover the excess funds from the 529 account to Roth IRAs established for their grandchildren ages 2 and 4. Since the grandchildren will have not earned income at those young ages, they will be ineligible to have Roth IRAs funded for them from their parent's 529 account. Without any compensation, the rollover from the 529 plan to the Roth IRA cannot happen.
7. **Beneficiary Contributes to Own Retirement:** Any amounts that the 529 beneficiary contributed to either a Roth IRA or traditional IRA will **count against the permitted rollover amount**. The

implication of this rule, or limitation, is that a full \$35,000 529-to-Roth IRA rollover will need to be spread out over several years.

8. **No Income Restrictions:** However, unlike normal Roth IRA contributions where there are earned income phase-out limitations that could prevent, or curtail, a Roth IRA contribution, there is **no income limit that restricts** the 529-to-Roth IRA rollover. For 2024, \$230,000-\$240,000 for a married filing jointly;\$146,000-\$161,000 for a single taxpayer.] Consequently, the 529 beneficiary could have reportable income that greatly exceeds the annual Roth IRA contribution limit without disqualifying the rollover. Some might view this as yet another ‘back-door’ Roth IRA opportunity for a high-earning 529 beneficiary.

9. **Ordering Rules:** Once the rollover from the 529 account to the Roth IRA is completed, and the former 529 dollars are later distributed from the Roth IRA, any of the funds rolled over will be treated as if they were rolled over from another Roth IRA. Accordingly, the **Roth distribution ordering rules will apply**. Contributions are tax and penalty-free and earnings are tax and penalty-free if the distribution is qualified (i.e., age 59 ½ , and the Roth IRA was open for at least 5 years.)

Limited Planning Opportunity? There *might* be a limited planning opportunity to ‘double-up’ or make two 529 account-to-Roth IRA rollovers this calendar year, but the beneficiary **must act before April 15, 2024**. The SECURE Act 2.0 provides that this new rollover rule is effective for 529 distributions ‘made after December 31, 2023.’ But it does not say that it is effective for tax years that begin after December 31, 2023. [IRS 1099-R Instructions.] Accordingly, a 529 distribution made after December 31, 2023 and before April 15, 2024 that is rolled over by the beneficiary to a Roth IRA by April 15, 2024, and is designated for 2023 would be reported as a Roth IRA contribution for 2023. In short, if the 529 beneficiary has not already made IRA contributions for 2023, up to the \$6,500 limit, he/she

still has time to do a 529-to-Roth IRA rollover in an amount equal to the unused part of the \$6,500 contribution limit for 2023.

Example: Charlie funded 529 accounts for each of his three grandsons, Tom, Dick, and Harry. Each of the grandsons has completed college and is in his mid-20's. Each grandson is gainfully employed. Each of Tom, Dick and Harry could potentially do two 529-to-Roth IRA rollovers in 2024 for a total of \$13,500 each. [\$6,500 for 2023 + \$7,000 for 2024 = \$13,500.]

Conclusion: This opportunity to rollover unused ('excess') 529 account funds to a Roth IRA carries with it several limitations and conditions, making it questionable how many will take the time to exploit it. That said, if a 529 beneficiary has graduated from college with unused dollars in their 529 account, this rollover opportunity may be a great way to get that young adult started saving for their own retirement decades from now.