

COVID-19 higher education refunds

If you receive a refund or partial refund of money paid for the spring semester of 2020, there is a potential tax risk if these costs were paid for using withdrawals from 529 College Savings Plans.

The IRS could recharacterize the refunded amounts as taxable distributions since these funds aren't being used for qualified educational expenses. These taxable distributions would incur a 10% penalty and income taxes on the earnings portion of the distribution, while the distribution of principal would be subject to the 10% penalty (no income taxes are due on a return of principal).

To avoid a taxable distribution, 529 account owners have two options:

- Pay for other qualified higher education expenses incurred by the beneficiary in the same calendar year.
- Recontribute the refunded amount into the 529 account. The amount recontributed cannot exceed the amount of the refund. For refunds between February 1 and May 16, 2020, the IRS has extended the time to recontribute funds to the greater of 60 days or July 15, 2020.

Please consult with your tax or financial advisor regarding your specific situation.

Sources:

<https://www.brightdirections.com/updates-on-covid-19-and-recent-market-volatility/>

https://www.kiplinger.com/article/college/T002-C032-S014-the-coronavirus-529-plan-tax-risk-you-can-t-ignore.html?rid=SQC-facebook#Xpltcf_PBX4.facebook

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