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FAFSA rule change: Grandparents get another reason to own 529 accounts

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There are exciting new changes coming to the Federal Application For Student Aid (FAFSA), making it significantly more attractive for grandparents to own a 529 for their grandchildren: Very soon, **distributions from grandparent-owned 529s will no longer count toward student income and impact the student's needs-based financial aid.**

Currently, distributions from grandparent owned 529s raise the student's Expected Family Contribution (EFC)—the amount the family is expected to contribute towards the cost of college in any given year—under FAFSA by 50% of the prior year's distribution.

If Grandma withdraws $10,000 for college for her grandchild, in the following year, the EFC would increase by $5,000.

Under the new rule change, however, if a doting Grandma pays $10,000 out of a 529 she owns, the distribution would not be counted on the next year's FAFSA form. This applies not just to grandparents, but any 529 not owned by a parent or the student.

Though this change goes into effect for FAFSA filed for the 2024-2025 school year, it will be based on tax information from two years prior, which means grandparent distributions taken beginning in 2022 will not affect the EFC and won't reduce eligibility for needs-based financial aid.

529 Ownership	Treatment of Asset Ownership	Treatment of 529 Savings Balances	Treatment of 529 Distributions	Treatment of Income
Custodial Parent or Guardian 529 UGMA/UTMA[1]	Parent or Guardian	EFC increased by 2.64-5.64% of balance	No effect on EFC	EFC increased by 22-47% of income
Grandparents or Other Owner	Not counted/No effect on EFC[2]			

[1] With the Free Application for Federal Student Aid, FAFSA, assets in an UGMA/UTMA and outside of a 529 are considered the child's assets and assessed at 20%.

[2] Distributions from accounts not owned by the student or parent/guardian will no longer be considered for purposes of the EFC calculation effective with the FAFASA form filed for the 2024-2025 school year. Because the FAFSA is based on tax information from two years prior, distributions taken beginning in 2022 will not effect EFC or needs-based financial aid. Talk to your tax advisor for more information.

What makes 529 plans especially attractive for Grandparents?

In addition to the new FAFSA rules, grandparents have a lot of reasons to invest in a 529:

- **Gifting:** 529s allow grandparents to gift up to $30,000 per year as a couple ($15,000 per grandparent) free of gift taxes. All contributions are removed from the grandparents' taxable estate.
- **Accelerated Gifting:** A special provision of 529 allows for accelerated gifts of up to $150,000 (married filing jointly) or $75,000 (single) to each grandchild's 529 account. No further gifts can be made for 5 years. These gifts reduce the size of the grandparent's taxable estate by the amount of the contribution.
- **Multiple Grandchildren Savings:** If a couple has 5 grandchildren, they could feasibly reduce the size of their taxable estate by $750,000 in a single tax year while leaving an education legacy for their grandchildren.
- **Control:** The grandparent always has control of the account and can name a successor owner.
- **Flexibility:** If the beneficiary decides not to attend college, the account holder can change the beneficiary at any time.

Conclusion: 529s look more attractive for Grandparents than ever before

529 plans are powerful vehicles that make saving for college easier. In the past, distributions from grandparent owned 529s could impact a student's need-based financial aid. Despite this, the exclusive gifting and estate tax benefits combined with tax-free qualified distributions made 529s attractive vehicles for contributing to a grandchild's higher education. With the FAFSA rule change coming into effect soon, grandparents have a much stronger incentive to open 529 accounts for their grandchildren to take advantage of these added benefits.

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