

How Recent Rule Changes Make Grandparent-Owned 529 Plans More Attractive



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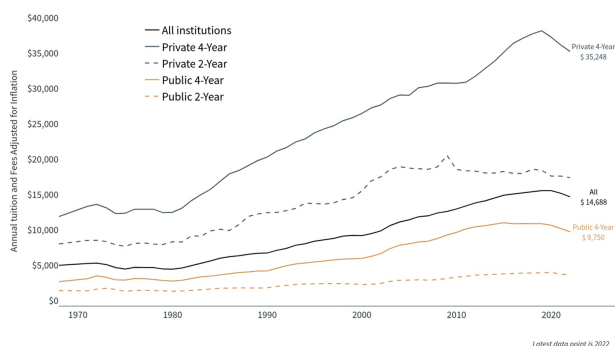
Nelson Mandela famously said that “education is the most powerful weapon which you can use to change the world.” For many families, funding a child's education is a core financial planning priority, yet the associated costs have risen sharply over time. Grandparents often want to contribute to their grandchildren's education as a meaningful and lasting legacy, one that goes beyond traditional gift-giving.

Historically, grandparents faced specific rules when gifting to grandchildren that could create unintended financial consequences, particularly around financial aid eligibility. Recent changes to federal financial aid rules now exclude grandparent-owned 529 accounts from the student assets portion of the aid calculation, removing a long-standing drawback. This makes grandparent-owned 529 plans worth a closer look as part of a comprehensive education funding strategy.

The rising cost of higher education puts pressure on family finances

The Cost of a College Education

Annual inflation-adjusted tuition and fees by institution type



The cost of a college education has grown well beyond the general rate of inflation over the past 40 years. According to the National Center for Education Statistics, average tuition and fees, adjusted for inflation, have risen substantially since 1963, with private 4-year institutions seeing particularly steep increases. Beyond tuition, families must also account for housing, food, books, transportation, and other education-related expenses, which now average over \$17,000 per year according to the College Board.¹

To manage these costs, families typically draw on a combination of sources, including parent and student income, savings, scholarships, grants, loans, and support from relatives. This is where grandparent-owned 529 accounts can add

meaningful value. Although parents often open 529 accounts for their children, grandparents can open accounts for grandchildren as well. Previously, distributions from grandparent-owned plans were reported as student income on the FAFSA, which reduced financial aid eligibility. Under the prior rules, student income was included in the Student Aid Index (SAI) calculation at a rate of 50%, and grandparent-owned 529 distributions were subject to this treatment.^{2,3} Recent changes now exempt grandparent-owned 529 accounts from this calculation entirely.

Investing in education can support a grandchild's long-term success

The Economic Benefits of Education

Unemployment rates and annual earnings by education level



Despite the rising cost of college, Bureau of Labor Statistics data confirms that the long-term returns to education remain strong. Each additional level of education is associated with higher average earnings and lower unemployment rates. For example, those with a high school diploma face an unemployment rate of 4.3%, while bachelor's degree holders average 2.8%, and those with professional or doctoral degrees see rates below 2%.⁴ Helping fund a grandchild's education is therefore a powerful way to establish a meaningful and lasting legacy.

Grandparent-owned 529 accounts offer notable flexibility, as the account owner retains control over assets, distributions, and the ability to change the beneficiary to another qualifying family member if

plans shift. The SECURE 2.0 Act also allows up to \$35,000 to be transferred from a 529 account into the grandchild's Roth IRA over their lifetime, free of taxes and penalties, provided certain conditions are met.⁵ The account must have been open under the grandchild's name for at least 15 years, and annual Roth IRA contribution limits along with earned income requirements still apply. Additionally, up to \$10,000 can be used to pay off qualified federal or private student loans for the primary beneficiary or their siblings.⁶ Starting in 2026, grandparents can also withdraw up to \$20,000 per grandchild annually for K-12 tuition, free of federal taxes.

529 accounts do not have an annual contribution cap, making them well-suited for estate planning and gifting. For 2026, a grandparent can gift up to \$19,000 per grandchild each year without triggering federal gift tax reporting.⁷ For those

who want to make a larger contribution, it is possible to front-load up to five years of gifts into a single contribution, translating to up to \$95,000, giving assets more time to compound on a tax-free basis.⁸ More than 30 states also offer an income tax deduction or credit for certain 529 contributions, with nine states providing “tax parity” for contributions to any state's plan.⁹

Of course, any contributions to a grandchild's education should be balanced against the grandparent's own retirement needs and long-term financial goals. When used thoughtfully, 529 plans represent a tax-advantaged tool that allows grandparents to play a meaningful role in helping families manage the growing cost of higher education.

The bottom line? Grandparents can leave a lasting legacy for their grandchildren in many different ways, including grandparent-owned 529 accounts. With careful planning, they can strategically invest in their grandchildren's future by helping with education costs using tax-efficient strategies.

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