DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, DC 20224

OFFICE OF THE CHIEF COUNSEL

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The Honorable Scott Fitzgerald
Member, U.S. House of Representatives
120 Bishops Way, Suite 154
Brookfield, WI 53005

Attention:

Dear Representative Fitzgerald:

I am responding to your inquiry on September 29, 2021, on behalf of your constituent, . wrote about his Individual 529 College saving plan (529 account).

Specifically, wants to close the 529 account and give the remaining account balance to his daughter—the designated beneficiary—so she can pay off her student loans. He also explained notified him that he could remove $10,000 from the 529 account without penalty; the remainder would be subject to a 10% penalty.

requested information on the laws and/or regulations establishing the 10% penalty and any available avenues or exceptions to have the penalty lifted or waived. He is worried this will also happen with a 529 account for his second daughter, who is currently attending college on an academic and athletic scholarship.

Based on the information provided to your office, it appears 529 account is a Qualified Tuition Program (QTP) under Section 529 of the Internal Revenue Code (IRC). A QTP is a program established and maintained by a state, or an agency or instrumentality of a state, allowing a contributor to either prepay a beneficiary's qualified higher education expenses at an eligible educational institution or contribute to an account for paying those expenses.

QTP distributions for qualified higher education expenses are not taxable to either the contributor or the designated beneficiary. Under IRC Section 529(c)(9), qualified higher education expenses include QTP distributions to pay principal or interest on a designated beneficiary's student loan. However, under IRC Section 529(c)(9)(B), there is a $10,000 lifetime limit for this special treatment of loan repayment distributions.

Generally, any QTP distribution not used for qualified higher education expenses is a taxable distribution under IRC Section 529(c), and is subject to a 10% additional tax on the amount included in income. A QTP distribution for loan repayment in excess of the $10,000 limit is a taxable distribution subject to the 10% additional tax. Congress has not provided any avenues or exceptions to have the additional tax lifted or waived.

To the extent second daughter does not use QTP distributions for qualified education expenses, she may need to pay income taxes on the distribution. However, under IRC Section 529(c)(6), the 10% additional tax doesn't apply to distributions included in income because the designated beneficiary received a tax-free scholarship.

can find additional information on QTPs in IRS Publication 970, Tax Benefits for Education, and on IRS.gov at the Tax Benefits for Education: Information Center. These additional resources may help determine the federal tax implications of the activities he described.

I hope this information is helpful. If you have questions, please contact at .

Sincerely,

/s/

Taina Edlund
Senior Technical Reviewer
Exempt Organizations Branch 2
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Employment Taxes