

Difference Between Coverdell ESA and 529

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Key Difference – Coverdell ESA vs 529

Education expenses are a considerable cost for a child, and many parents start saving when their children are at a very young age in order to ensure they receive a good education. Coverdell ESA (Coverdell Education Savings Account) and 529 plan are two widely used options in the United States to save for the above purposes. The key difference between Coverdell ESA and 529 is that **Coverdell ESA is a tax-advantaged educational savings plan to cover future elementary and secondary educational expenses** whereas **529 is also a similar education savings plan that helps set aside funds for future college costs.**

What is Coverdell ESA?

A Coverdell ESA is a tax-advantaged educational savings plan that a parent/guardian can apply for on behalf of a [beneficiary](#) (probably a child or a grandchild) to cover future elementary and secondary educational expenses. Information regarding qualifying educational expenses for Coverdell ESA can be found in Section 530 of the Internal Revenue Code. Withdrawals made for qualifying educational expenses are tax deferred and funds are allowed to grow tax-free as well.

The sponsor cannot contribute funds to a Coverdell ESA after the beneficiary reaches the age of 18 years nor can a Coverdell ESA be opened for a beneficiary above the age of 18 years. Funds in a Coverdell ESA must be disbursed on qualified education expenses by the time the beneficiary is 30 years old or instead given to another family member below the age of 30. Another element that clearly contrasts Coverdell ESA from a 529 plan is that the limited annual contribution limits where the limit cannot exceed \$2,000 per beneficiary until age 18.



Figure 01: Coverdell ESA saves funds for future elementary and secondary educational expenses

Funds in a Coverdell ESAs can allow a range of investment options including [shares](#), [bonds](#), and [mutual funds](#). If the funds are withdrawn for non-educational purposes, a tax of 10% is charged as a penalty.

What is 529?

529 is also a tax-advantaged education savings plan that a parent/ guardian can apply for on behalf of a beneficiary to set aside funds for future college costs. 529 plans are officially named as qualified tuition plans and are sponsored by states or educational institutions and are authorized by Section 529 of the Internal Revenue Code. Most 529 plans offer lifetime contribution limits of at least \$300,000. Prepaid tuition plan and college savings plan are the two main types of 529 plan.

Prepaid Tuition plan

In prepaid tuition plan, the parents/guardians can prepay a child's future tuition and fees at present rates

College Savings Plan

This gives the opportunity for parents/ guardians to contribute to an account established to pay for higher education of the child at any eligible educational institution.



Figure 02: 529 plan saves funds for future college expenses

Unlike in Coverdell ESA, 529 plans do not have an age limit at which the funds have to be disbursed. With regard to investments, 529 does not have a wide range of options like in Coverdell ESA.

Withdrawals of 529 plans are not subjected to income tax. However, if the funds are withdrawn for non-educational purposes, a tax of 10% is charged as a penalty. As per fees, annual maintenance fees and [asset management](#) fees are charged from 529 plans where an initial investment is also specified.

What are the similarities between Coverdell ESA and 529?

- Funds contributed for both Coverdell ESA and 529 are tax-free.
- A penalty of 10% for early withdrawal is applicable for both Coverdell ESA and 529.

What is the difference between Coverdell ESA and 529?

Coverdell ESA vs 529

A Coverdell ESA is a tax-advantaged educational savings plan that a parent/ guardian can apply for on behalf of a beneficiary to cover future elementary and secondary educational expenses.

529 is a tax-advantaged education savings plan that a parent/ guardian can apply for on behalf of a beneficiary set aside funds for future college costs.

Contribution Limit

Annual contribution limit for Coverdell ESAs is \$2,000 per beneficiary until age 18.

Lifetime contribution limits of at least \$300,000 is available in most 529 plans.

Investment Options

Funds in Coverdell ESAs are allowed to be invested in a range of investment options including shares, bonds, and mutual funds.

529 plans have a limited number of investment options.

Summary – Coverdell ESA vs 529

The difference between Coverdell ESA and 529 mainly depends on the type of education expenses each plan will cover. While Coverdell ESA accumulates funds for future elementary and secondary education expenses, 529 specifically accumulates funds for college education. A number of other differences such as the contribution limit and investment options can also be found between the two plans. Further, both incur penalties for withdrawing funds for qualified educational expenses.

References:

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