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LEGISLATIVE EDUCATION STUDY COMMITTEE
BILL ANALYSIS
56th Legislature, 1st Session, 2023

Bill Number	<u>HB342/aHFL#1</u>	Sponsor	<u>Lane/Wirth</u>
Tracking Number	<u>.224158.3</u>	Committee Referrals	<u>HEC/HGEIC</u>
Short Title	<u>Education Savings Plan Uses</u>		
Analyst	<u>Estupiñan</u>	Original Date	<u>2/15/2023</u>
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BILL SUMMARY

Synopsis of HFL#1 Amendment

The House Floor Amendment #1 to House Bill 342 (HB342/aHFL#1) amends the definition of base income in the Income Tax Act pertaining to taxpayers that have a deduction for payments to the education trust fund. This language would change “qualified higher education expenses” to mean “federally allowable qualified higher education expenses” set out in the Internal Revenue Code Section 529.

Synopsis of Original Bill

House Bill 342 (HB342) would amend Section 7-2-32 NMSA 1978 to align provisions of state law with Section 529 of the Internal Revenue Code, which covers qualified tuition programs. This revision would align New Mexico statute with federal code and allow New Mexico’s 529 college savings plan established in Section 7-2-32 NMSA 1978, to be used for “any college, university, vocational school or other post-secondary institutions recognized by the United States Department of Education.”

FISCAL IMPACT

The bill does not contain an appropriation.

HB342/aHFL#1 would expand allowable educational uses for the holders and beneficiaries of 529 accounts, which may encourage additional people to open and contribute to 529 accounts. This may have a fiscal implication as contributions to 529 accounts are eligible to be claimed as a deduction on state income taxes.

New Mexico is one of only four states that does not impose a cap on the amount an individual can contribute to a 529 account and subsequently claim as a deduction from their state income tax liability. Individuals can contribute to their 529 plan until their account balance reaches \$500 thousand.

SUBSTANTIVE ISSUES

About 529 College Savings Plans. A 529 college savings plan, often called a 529 plan or 529 account, is a tax-advantaged savings account designed to be used for education expenses. These plans typically have high contribution limits designed to assist an individual in paying for a range of qualified education expenses including college, tuition expenses in kindergarten through 12th grade, certain apprenticeship programs or costs, and student loan repayments. These 529 plans have various federal and state tax advantages, are professionally managed, and may benefit from investment returns.

A child’s parents or guardians can open a 529 account to pay for their children’s future educational expenses. Pursuant to federal law, a 529 account can be opened by anyone who is a United States resident, over the age of 18, with a United States mailing address, and a social security number or Tax ID. Anyone of any age can be a beneficiary.

New Mexico’s 529 College Savings Plans. Pursuant to New Mexico’s Education Savings Act, the Education Trust Board of New Mexico (NMETB), a self-sustaining state entity that was established by the state’s Education Trust Act, sponsors 529 accounts in the state, offering both a direct-sold plan and an advisor-sold plan.

- New Mexico’s Education Plan is a direct-sold plan that allows an individual to open a tax-advantaged account and choose from a variety of investment options that are geared to the risk-tolerance of the account owner. This option is a less expensive plan as it allows its owner to choose how to invest the account’s funds without the guidance of a financial advisor.
- New Mexico’s Scholar’s Edge program is an advisor-sold plan that provides the account owner with the guidance of a financial advisor who counsels the account owner on a range of investment options. These plans may levy fees and commissions on the account owner but are intended for individuals who may not have the capacity to navigate the various complexities of diverse investment options.

Because the funds in a 529 college savings plan are considered to belong to a student’s parents, the funds in the account do not generally affect a student’s ability to qualify for financial aid opportunities.

HB342/aHFL#1 Changes. Because New Mexico has not updated its statute to align with the federal definition of “qualified higher education expenses,” some federally-qualified withdrawals from 529 accounts are not eligible for tax benefits under the New Mexico tax code. HB342/aHFL#1 would align state statute with the broader federal definition of “qualified higher education expenses.” This would allow 529 accounts to be used for a broader range of educational expenses, rather than for “college,” as is currently noted in state law.

HB342/aHFL#1 would change “qualified higher education expenses” to mean “federally allowable qualified expenses set out in the Internal Revenue Code Section 529 and includes other expenses allowed under that section as qualified education expenses.” This new definition would mean that 529 accounts could be used for the following expenses :

- Up to \$10 thousand a year for tuition in kindergarten through 12th grade;
- Transfers up to \$15 thousand a year to an ABLE account—accounts for individuals with disabilities—for the beneficiary;

- Apprenticeship expenses; and
- Up to \$10 thousand for student loan repayment.

Additional Qualified Educational Expenses. According to The Education Plan, funds in a 529 account can currently be used for a variety of educational expenses, including:

- Tuition and fees;
- Books and supplies;
- Room and board for beneficiaries attending on at least a half-time basis;
- Computer technology, equipment, internet access; and
- Expenses for educational special needs services.

ADMINISTRATIVE IMPLICATIONS

According to the New Mexico Education Trust board, a conflict in statute currently exists between the state and federal government because of numerous rounds of revisions that have been made to Section 529 of the Internal Revenue Code over the last several years.

OTHER SIGNIFICANT ISSUES

Tax Benefits for 529 Account Holders and Beneficiaries. Earnings and withdrawals from a 529 account are exempt from federal taxation if they are used for qualified educational expenses. If a resident of New Mexico contributes to a 529 account with The Education Plan, 100 percent of their contribution is deductible from their state taxable income in the year they contributed to the account. If the account beneficiary is also a resident of New Mexico, earnings and withdrawals from their 529 account are exempt from state taxation if the money is used for qualified educational expenses. Contributors who are not residents of New Mexico can still receive the aforementioned federal benefits.

If an individual is contributing to a 529 account, the first \$16 thousand (or \$32 thousand for a married couple) is exempt from federal gift taxes. This is because the contribution is considered to be a completed gift from the contributor to the beneficiary. Of note, the IRS code has a provision that allows a tax filer to use a five-year gift tax averaging when contributing to a 529 plan, which essentially allows them to contribute up to \$80 thousand (or \$160 thousand for a married couple) in a single year and have it treated as if they contributed that over a five-year period. This allows a 529 account holder to begin building their account balance and investment returns on an accelerated basis without incurring federal gift taxes.

SOURCES OF INFORMATION

- LESC Files
- The Education Trust Board of New Mexico (NMETB)

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