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## CLIENT ALERT: 529 PLANS AND DIVORCE

Highlighted by *In re Marriage of Daon and Stewart*

With educational expenses on the rise, planning for your children's education while they are still young is usually advisable. Many families find that a "section 529 education savings plan," or more commonly known as a "529 plan," works well for this purpose, but there are potential pitfalls to 529 plans. *In re Marriage of Daon and Stewart* illustrates one such pitfall that can occur when a married couple gets divorced and assets, including 529 plans, are divided.

**What is a 529 plan:** A 529 plan, so named after section 529 of the tax code, is a tax-advantaged planning tool utilized to save money to pay for educational expenses. Anyone can create a 529 plan by opening a 529 investment account (the "account owner") for the benefit of a child (the "account beneficiary"). The 529 plan allows for contributions into the plan to grow tax deferred and be withdrawn tax free if the withdrawn funds are applied toward qualified education expenses. The withdrawn funds must be used to pay for K-12 programs, college, graduate school, or other accredited schools (including vocational schools), or for certain related expenses, including books, room, and board.

**Background of *In re Marriage of Daon and Stewart*:** During their marriage, Emmanuel Daon and Maria Stewart opened 529 plans for each of their two minor sons. In 2012, the couple separated and entered into an agreement dividing their property, including the 529 plans. The agreement provided that each 529 plan is to be held in constructive trust for that child/beneficiary, with Emmanuel and Maria distributing the funds as they agree to be in the child's best interest until such time as the funds belong to the child i.e., the child reaches majority.

In 2020, their eldest son, Alexander, turned eighteen-years-old and was admitted to college. Maria requested Emmanuel to provide an accounting for Alexander's 529 plan so they could confer and decide on how to pay for Alexander's school. Emmanuel refused to provide the accounting and further noted that he was not comfortable making any distributions from the 529 account because Alexander did not involve him in his college plans. Maria sued Emmanuel to make the distributions and argued that per the asset division agreement, the money in the 529 plan for Alexander's benefit had to be released to him when he reached the age of majority. Emmanuel counterargued that he retained discretion over disbursements from the 529 plan, as the account owner.

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The Kansas District Court ruled in Emmanuel's favor and expressed concerns that Alexander might mismanage such funds. The Kansas Appellate Court reversed the lower court's ruling and ruled in favor of Maria. The Appellate Court reviewed this case as a matter of contract law and found that the asset division agreement entered into by Emmanuel and Maria was thorough and clear, thereby creating an unambiguous contract between the parties. As a result, the Appellate Court ordered a full distribution of funds to Alexander. The Appellate Court also noted that the parties could have deferred distribution until some later age if the asset division agreement contemplated such a scenario and included language to that effect in the terms of the contract.

**Takeaways:** The ruling of the Kansas Appellate Court in *In re Marriage of Daon and Stewart* illustrates that the planning that went into a properly funded 529 plan can be thwarted by an overly restrictive asset division agreement, usually in relation to divorce or separation proceedings. In this case, the result was a distribution of large amounts of money to a young adult. If the asset division agreement in this case specified that the former two spouses needed to agree on any distribution of funds, or at the very least contemplated the deferment of a full distribution of funds at a later age, then the outcome of this case would likely have been different.

Please contact a Wiggin and Dana attorney if you have questions about protecting existing 529 plans in the event of divorce or if you are seeking advice on opening a 529 account and we would be happy to speak with you.

*This publication is a summary of legal principles. Nothing in this article constitutes legal advice, which can only be obtained as a result of a personal consultation with an attorney. The information published here is believed accurate at the time of publication, but is subject to change and does not purport to be a complete statement of all relevant issues.*