

**COMPARISON OF REVENUE PROVISIONS OF H.R. 2646
RELATING TO CERTAIN EDUCATION SAVINGS TAX INCENTIVES
AS PASSED BY THE HOUSE AND THE SENATE**

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of the

JOINT COMMITTEE ON TAXATION

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INTRODUCTION

This document,¹ prepared by the staff of the Joint Committee on Taxation, provides a description of the revenue provisions of H.R. 2646, the “Education Savings Act for Public and Private Schools,” as passed by the House, and the “Parent and Student Savings Account PLUS Act,” as passed by the Senate. The non-revenue provisions of H.R. 2646 as passed by the Senate are not described in this document.

H.R. 2646 was passed by the House on October 20, 1997.² H.R. 2646 was passed by the Senate, as amended, on April 23, 1998.³

This document contains a description of the revenue provisions in the House and Senate versions of the bill. A separate document provides a comparison of the estimated budget effects of the House and Senate versions of the bill.

¹ This document may be cited as follows: Joint Committee on Taxation, *Comparison of Revenue Provisions of H.R. 2646 Relating to Certain Education Savings Tax Incentives* (JCX- 33-98), May 11, 1998.

² See, also, House Ways and Means Committee Report on H.R. 2646 (H. Rept. 105-332, October 21, 1997).

³ See, also, Senate Committee on Finance Report on S. 1133 (S. Rept. 105-164, February 19, 1998).

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COMPARISON OF REVENUE PROVISIONS

<i>Item</i>	<i>Present Law</i>	<i>House Bill</i>	<i>Senate Amendment</i>
<p>A. Modifications to Education IRAs (sec. 2 of the House bill and sec. 101 of the Senate amendment)</p>	<p><u>In general.</u>--Under Code section 530, taxpayers may establish "education IRAs" which are accounts created exclusively for the purpose of paying qualified higher education expenses of a named beneficiary. Until a distribution is made from an education IRA, earnings on contributions generally are not subject to tax. In addition, distributions from an education IRA are excludable from gross income to the extent that the distribution does not exceed qualified higher education expenses incurred by the beneficiary during the year the distribution is made (provided that a HOPE credit or Lifetime Learning credit is not claimed with respect to the beneficiary for the same taxable year).</p> <p><u>Contribution limits.</u>--Annual contributions to education IRAs may not exceed \$500 per designated beneficiary.</p>	<p><u>Contribution limits.</u>--For the period 1998 through 2002, the House bill increases the present-law annual contribution limit to</p>	<p><u>Contribution limits.</u>--Same as the House bill, except that the Senate amendment increases the present-law annual contribution</p>

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	<p>Contributions to an education IRA may not be made after the designated beneficiary reaches age 18.</p> <p><u>Eligible contributors.</u>-- Contributions to an education IRA may not be made by certain higher-income taxpayers--i.e., the contribution limit is phased out for individuals with modified adjusted gross income between \$95,000 and \$110,000 (\$150,000 and \$160,000 for taxpayers filing joint returns). No contribution may be made to an education IRA during any year in which any contributions are made by anyone to a qualified State tuition program on behalf of the same beneficiary.</p>	<p>\$2,500. For 2003 and later years, the annual contribution limit for education IRAs will be \$500. Contributions may continue to be made after the designated beneficiary reaches age 18 in the case of a special needs beneficiary (as defined by Treasury Department regulations).</p> <p><u>Eligible contributors.</u>--The House bill clarifies that corporations and other entities are permitted to make contributions to education IRAs, regardless of the income of the corporation or entity during the year of the contribution.</p>	<p>limit to \$2,000, and only for the period 1999 through 2002.</p> <p><u>Eligible contributors.</u>--Same as the House bill.</p>

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	<p><u>Distributions</u>.--The legislative history of the 1997 Act provides that any balance remaining in an education IRA will be deemed to be distributed within 30 days after the date that the named beneficiary reaches age 30 (or, if earlier, within 30 days of the date that the beneficiary dies). (A technical correction to this effect is included in H.R.2676, the "Internal Revenue Service Restructuring and Reform Act," as passed by the House.)</p> <p><u>Qualified education expenses</u>.--The term "qualified higher education expenses" means tuition, fees, books, supplies, and equipment required for the enrollment or attendance of a designated beneficiary at an "eligible educational institution" (defined by reference to sec. 481 of the Higher Education Act of 1965). Expenses incurred in connection with elementary and secondary education are not</p>	<p><u>Distributions</u>.--The House bill provides that, in the case of a special needs beneficiary, a deemed distribution of any balance in an education IRA will not be required when the beneficiary reaches age 30.</p> <p><u>Qualified education expenses</u>.--The House bill provides that, with respect to contributions made during the period 1998 through 2002 (and earnings attributable to such contributions), the definition of qualified education expenses is expanded to include "qualified elementary and secondary education expenses," meaning tuition, fees, tutoring, special needs services, books, supplies,</p>	<p><u>Distributions</u>.--Same as the House bill.</p> <p><u>Qualified education expenses</u>.--The Senate amendment provides that, with respect to contributions made during the period 1999 through 2002 (and earnings attributable to such contributions), the definition of qualified education expenses is expanded to include "qualified elementary and secondary education expenses," meaning (1) tuition, fees, academic tutoring, special needs services,</p>

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	<p>qualified education expenses.</p> <p>Certain room and board expenses also may be qualified higher education expenses, but only if the student is enrolled at an eligible educational institution on at least a half-time basis.</p>	<p>computer equipment (including related software and services) and other equipment, transportation, and supplementary expenses required for the enrollment or attendance of a designated beneficiary at a public, private, or religious elementary or secondary school (through grade 12). Qualified elementary and secondary education expenses also include certain homeschooling expenses. For contributions made in 2003 or later years, the definition of qualified education expenses will be limited to post-secondary education expenses.</p>	<p>books, supplies, and equipment (including computers and related software and services) incurred <u>in connection with</u> the enrollment or attendance of the designated beneficiary as an elementary or secondary student at a public, private, or religious school providing elementary or secondary education (grades K-12), <u>and</u> (2) room and board, uniforms, transportation, and supplementary items and services (including extended-day programs) <u>required or provided by</u> such a school for such enrollment or attendance of the designated beneficiary. For contributions made in 2003 or later years (and for earnings attributable to such contributions), the definition of qualified education expenses will be limited to post-secondary education expenses.</p> <p>The Senate amendment also expands the definition of</p>

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		<p><u>Technical corrections.</u>--No provision. [Technical corrections provisions similar to those contained in the Senate amendment are included in the House-passed version of H.R. 2676 (the "Internal Revenue Service Restructuring and Reform Act")]</p> <p><u>Effective date.</u>--The House bill provisions are effective for</p>	<p>qualified education expenses with respect to post-secondary education to include (1) tuition, fees, academic tutoring, special needs services, books, supplies, and equipment (including computers and related software and services) incurred <u>in connection with</u> the enrollment or attendance of the designated beneficiary at an eligible post-secondary educational institution, and (2) certain room and board expenses (as under present law).</p> <p><u>Technical corrections.</u>--The Senate amendment includes several technical amendments to the education IRA provisions enacted in 1997.</p> <p><u>Effective date.</u>--The Senate amendment provisions are</p>

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	<p>withdrawal. However, the earnings portion of distributions from qualified State tuition programs are includible in the gross income of the distributee.</p> <p>To the extent that a distribution from a qualified State tuition program is used to pay qualified higher education expenses, a HOPE credit or Lifetime Learning credit potentially may be available with respect to such expenses.</p> <p><u>Qualified higher education expenses.</u>--The term "qualified higher education expenses" includes expenses for (1) tuition, fees, books, supplies, and equipment <u>required</u> for the enrollment or attendance at an eligible post-secondary educational institution, and (2) room and board expenses (meaning the minimum room and board allowance applicable</p>	<p>No provision.</p>	<p>distributions from qualified State tuition programs are excludable from gross income to the extent used to pay qualified higher education expenses (defined below).</p> <p>If a HOPE or Lifetime Learning credit is claimed on behalf of a student, then the earnings portion of a distribution made to the student from a qualified State tuition program will be includible in the gross income of the student.</p> <p><u>Qualified higher education expenses.</u>--Under the Senate amendment, "qualified higher education expenses" are defined the same as for purposes of education IRAs (see above), meaning (1) tuition, fees, academic tutoring, special needs services, books, supplies, and equipment (including computers and related software and services) incurred <u>in connection</u></p>

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	<p>to the student as determined by the institution in calculating costs of attendance for Federal financial aid programs under sec. 472 of the Higher Education Act of 1965) for any period during which the student is at least a half-time student.</p>		<p><u>with</u> the enrollment or attendance of a designated beneficiary at an eligible post-secondary educational institution (i.e., colleges, universities, and certain vocational schools), and (2) certain room and board expenses (as under present law).</p> <p>Effective date.--The provisions apply to distributions made in taxable years beginning after December 31, 1998.</p>
<p>C. Extension of Exclusion for Employer-Provided Educational Assistance (sec. 105 of the Senate amendment)</p>	<p>Under present law Code section 127, an employee's gross income and wages do not include amounts paid or incurred by the employer for educational assistance provided to the employee if such amounts are paid or incurred under an educational assistance program that meets certain requirements. This exclusion is limited to \$5,250 of educational assistance with respect to an</p>	<p>No provision.</p>	<p>The Senate amendment reinstates the exclusion for graduate-level education, and extends the exclusion (as applied to both graduate and undergraduate courses) through December 31, 2002.</p> <p>Effective date.--The extension of the exclusion to graduate-level education is effective for expenses with respect to courses beginning after December 31,</p>

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<p>D. Arbitrage Rebate Exception for Governmental Bonds of Certain Small Governments (sec. 106 of the Senate amendment)</p>	<p>individual during a calendar year. The exclusion does not apply with respect to graduate-level courses. The exclusion is scheduled to expire with respect to courses beginning after May 31, 2000.</p> <p>Arbitrage profits earned on tax-exempt bonds generally must be rebated to the Federal Government. An exception is provided for profits earned on governmental bonds issued by certain governmental units that issue no more than \$5 million of such bonds in the year when the bonds benefitting from the exception are issued. The \$5 million limit is increased to \$10 million if bonds equal to at least the excess over \$5 million are used to finance public schools.</p>	<p>No provision.</p>	<p>1997. The extension of the exclusion (with respect to both graduate and undergraduate courses) expires with respect to courses beginning after December 31, 2002.</p> <p>Allows an additional \$5 million of public school bonds to be issued without loss of eligibility for the small-issuer arbitrage rebate exception (for total issuance of up to \$15 million per year if bonds equal to at least the excess over \$5 million are used to finance public schools).</p> <p><u>Effective date.</u>--Bonds issued after December 31, 1998.</p>

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<p>E. Exclusion of Certain Amounts Received under the National Health Corps Scholarship Program (sec. 107 of the Senate amendment)</p>	<p>Code section 117 excludes from gross income amounts received as a qualified scholarship by an individual who is a degree candidate and used for tuition and fees required for the enrollment or attendance (or for fees, books, supplies, and equipment required for courses of instruction) at a primary, secondary, or post-secondary educational institution. The tax-free treatment provided by section 117 does not extend to scholarship amounts covering regular living expenses, such as room and board.</p> <p>Section 117(c) specifically provides that the exclusion for qualified scholarships does not apply to amounts received by a student as payment for teaching, research, or other services by the student required as a condition for receiving the scholarship.</p>	<p>No provision.</p>	<p>Under the Senate amendment, amounts received by an individual under the National Health Corps Scholarship Program are eligible for tax-free treatment as a qualified scholarship under section 117, without regard to the fact that the recipient of the scholarship is obligated later to provide medical services in a geographic area (or to an underserved population group or designated facility) identified by the Public Health Service as having a shortage of health care professionals. The tax-free treatment does not apply to amounts received by students to cover regular living expenses, such as room and board.</p> <p><u>Effective date.</u>--The provision applies to amounts received in taxable years beginning after December 31, 1993.</p>

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<i>Item</i>	<i>Present Law</i>	<i>House Bill</i>	<i>Senate Amendment</i>
<p>F. Tax-Exempt Bonds for Privately Owned Public Schools (sec. 108 of the Senate amendment)</p>	<p>Interest on State and local government bonds generally is tax-exempt if the bond proceeds are used to carry out governmental functions of the issuer and the debt is repaid with governmental funds. Interest on bonds used to finance private business activities is taxable unless the Internal Revenue Code includes an exception for the activity involved. The Code does not include an exception for bonds to finance public schools owned by for-profit private businesses.</p>	<p>No provision.</p>	<p>Allows States to issue up to \$10 per resident (\$5 million, if greater) per year in tax-exempt bonds for public schools that are owned by for-profit, private businesses, but that are operated by States or local governments as part of the public school system. Except for an amount not exceeding \$5 million per year, each State could use these bonds only for public elementary and secondary schools located in "high-growth" school districts. High-growth school districts would be defined as districts having an enrollment of at least 5,000 students in the second preceding academic year <i>and</i> having experienced student enrollment increases of 20 percent or more during the 5-year period ending with that second year.</p> <p><u>Effective date.</u>--Bonds issued after December 31, 1998.</p>

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<i>Item</i>	<i>Present Law</i>	<i>House Bill</i>	<i>Senate Amendment</i>
<p>G. Employer Deductions for Vacation and Severance Pay (sec. 3(a) of the House bill and sec. 201 of the Senate amendment)</p>	<p>In general, contributions under a deferred compensation plan (other than certain pension, profit-sharing and similar plans) are deductible in the taxable year in which an amount attributable to the contribution is includible in income of the employee. However, vacation pay which is treated as deferred compensation is deductible for the taxable year of the employer in which the vacation pay is paid to the employee (sec. 404(a)(5)).</p> <p>A plan, method or arrangement is not considered to defer the receipt of compensation or benefits to the extent that compensation or benefits are received by the employee on or before the 15th day of the 3rd calendar month after the end of the employer's taxable year in which the related services are rendered ("the applicable 2-1/2 month period").</p>	<p>The House bill overrules <u>Schmidt Baking</u>. The House bill provides that, for purposes of determining whether an item of compensation is deferred compensation, the compensation is not considered to be paid or received until actually received by the employee. In addition, an item of deferred compensation is not considered paid to an employee until actually received by the employee.</p> <p>It is intended that similar arrangements, such as trust arrangements, in addition to the letter of credit approach used in <u>Schmidt Baking</u>, do not constitute actual receipt by the employee, even if there is an income inclusion on the part of employees.</p>	<p>Same as the House bill, except that the provision does not apply to severance pay.</p>

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	<p>In <u>Schmidt Baking Co., Inc.</u>, 107 T.C. 271 (1996), the Tax Court held that severance pay and vacation pay were paid to employees within the applicable 2-1/2 month period and were not deferred compensation if the taxpayer provided for its accrued vacation and severance pay liabilities by purchasing an irrevocable letter of credit after the end of the taxable year, but within the applicable 2-1/2 month period. The vacation pay and severance pay were deductible by the taxpayer for the taxable year pursuant to its normal accrual method of accounting.</p>	<p>Effective date.--The provision is effective with respect to taxable years ending after October 8, 1996.</p>	<p>Effective date.--The provision is effective with respect to taxable years ending after the date of enactment.</p>

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<p>H. Modification to Foreign Tax Credit Carryback and Carryover Periods (sec. 202 of the Senate amendment)</p>	<p>U.S. persons may credit foreign taxes against U.S. tax on foreign-source income. The amount of foreign tax credits that can be claimed in a year is subject to a limitation that prevents taxpayers from using foreign tax credits to offset U.S. tax on U.S.-source income. The amount of creditable taxes paid or accrued (or deemed paid) in any taxable year which exceeds the foreign tax credit limitation is permitted to be carried back two years and forward five years. The amount carried over may be used as a credit in a carryover year to the extent the taxpayer otherwise has excess foreign tax credit limitation for such year.</p>	<p>No provision.</p>	<p>The carryback period for excess foreign tax credits is reduced from two years to one year. The excess foreign tax credit carryforward period is extended from five years to seven years.</p> <p><u>Effective date.</u>--The provision applies to foreign tax credits arising in taxable years beginning after December 31, 2000.</p>