

# Questions and Answers about the Education Savings Bonds

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## **What is the Education Savings Bond Program?**

The Education Savings Bond Program permits qualified taxpayers to exclude from their gross income all or a portion of the interest earned on eligible Series EE Savings Bonds bearing issue dates after 1989 and registered in the name of a taxpayer age 24 or older at the time of issuance. To qualify for this exclusion, tuition and other educational expenses must be incurred by the taxpayer, the taxpayer's spouse or the taxpayer's dependent at certain post-secondary educational institutions. In addition, there are income limitations on those eligible to participate in the program. The Education Savings Bond Program was authorized by the Technical Corrections and Miscellaneous Revenue Act of 1988.

**Is there a new series of Bonds which must be purchased to take advantage of the program?**

No, Series EE Savings Bonds, widely available for purchase through financial institutions and through payroll savings plans, are used for the program.

## **What educational expenses are eligible for the program?**

Eligible educational expenses include tuition and fees (such as lab fees and other required course expenses) required for the enrollment of or attendance by the taxpayer, or the taxpayer's spouse or dependent at an eligible educational institution. However, expenses relating to any course or other education involving sports, games, or hobbies are eligible only if required as part of a degree or certificate granting program. Room and board, as well as books are not included as eligible expenses. Eligible expenses are calculated net of scholarships, fellowships, employer-provided educational assistance, and other tuition reduction amount and must be incurred during the same tax year in which eligible Bonds are redeemed.

## **What qualifies as an eligible educational institution?**

Post-secondary institutions, including vocational schools, that meet the standards for participation in federal financial aid programs (such as guaranteed student loan programs) qualify for the program. Proprietary institutions, such as beautician or secretarial schools, generally do not qualify.

## **Can all outstanding bonds be used in the program?**

No, the program took effect on January 1, 1990, and applies only with respect to Series EE Bonds issued after December 31, 1989. No Savings Bonds issued before that date will provide excludable interest nor is any other series of Bonds (e.g., Series HH) eligible for the program.

## **Can anyone purchase these Bonds and take advantage of the exclusion?**

No, to exclude interest earnings on Series EE Bonds issued after 1989, a taxpayer must be at least 24 years old before the Bonds' issue date. Since a Series EE Bond's issue date is the first day of the month in which the taxpayer purchases the Bond, the taxpayer must be 24 years old before the first day of the month in which the Bond is purchased. Furthermore, if the taxpayer is married, the taxpayer must file a joint return in order to exclude the Bond interest from income.

## **Can anyone take advantage of the interest exclusion by purchasing Bonds as gifts?**

No, the purpose of this program is to benefit the taxpayer(s) paying for qualified educational expenses of the taxpayer, taxpayer's spouse, or taxpayer's dependent within the meaning of section 151 of the Internal Revenue Code. To exclude the Bond interest from gross income, the Bond must be in the name of the taxpayer or in the name of the taxpayer and the taxpayer's spouse who pays qualified educational expenses and not in the name of the dependent. The designation of the dependent as beneficiary is permitted.



## **What about registering the Bond in the parent and child's name as coowners?**

For purposes of eligibility for this program only, the designation of a child as coowner with his or her parent is not permitted. Bonds must be in the name of the taxpayer, with or without a beneficiary, or in the name of the taxpayer and the taxpayer's spouse as coowners to exclude the Bond interest from the taxpayer's gross income.

## **Does the Education Bond feature affect Savings Bonds that have been or are being purchased by a parent registered in the name of a child alone, or the child's name with the parent as beneficiary?**

No, the Federal income tax rule that applies to such Bonds remains the same. For a child under 14, only the interest and dividend income in excess of \$1,200 is taxed at the parent's rate in 1993. (This figure is indexed for inflation annually). If the child is 14 or older, all income is taxed at the child's rate. You may choose between annual or deferred reporting. Either method, used properly, and taking into account your child's age and expected future earnings should reduce tax liability. However, interest earnings on such Bonds do not qualify for gross income exclusion under the terms of the education feature.

**Do both the principal and interest from Bonds redeemed during the year have to be used for qualified educational expenses to exclude the Bond interest from gross income?**

Yes, only if the taxpayer pays qualified education expenses equal to or greater than all proceeds (i.e., interest and principal) from Bonds redeemed during the year can all interest accrued on such Bonds be excludable from his or her gross income.

## **What if the amount of the Bond redemption proceeds exceeds the amount of the qualified educational expenses?**

If the amount of the redemption proceeds from all eligible Bonds redeemed during the year exceeds the amount of the qualified educational expenses paid during such year, the amount of excludable interest will be reduced by a pro rata amount. For example, if the Bond proceeds amounted to \$10,000 (\$5,000 principal and \$5,000 interest) and the qualified educational expenses are \$8,000, the taxpayer would only be able to get an exclusion for 80 percent of the interest earned or \$4,000.

## **Are there income limitations on the program?**

Yes, the full interest exclusion is only available for married couples filing joint returns with incomes of up to and including \$68,250 (modified adjusted gross income) and for single filers with incomes of up to and including \$45,500 (modified adjusted gross income). These are the limits in effect in 1993.

## **What is modified adjusted gross income?**

For purposes of this program, modified adjusted gross income means the sum of the taxpayer's adjusted gross income for the taxable year, including interest on U.S. Savings Bonds before exclusion. It also includes the gross income earned by citizens or residents of the U.S. living abroad and income from sources within Guam, American Samoa, the Northern Mariana Islands, and Puerto Rico.

## **What benefits, if any, are there for taxpayers who file jointly with modified adjusted gross incomes above \$68,250 (or \$45,500 for single filers)?**

The interest exclusion benefits will phase out for joint filers with 1993 modified adjusted gross incomes of between \$68,250 and \$98,250 (\$45,500 and \$60,500 for single filers) by a decreasing percentage above the threshold income level. For example, a taxpayer filing jointly with a modified adjusted gross income (AGI) of \$83,250 would only be able to take advantage of one-half of the exclusion, while a taxpayer filing jointly with a modified AGI of \$92,250 would only be allowed an exclusion of 20 percent of the eligible interest income. A similar phase out plan will be employed for the single filer. Note: Married individuals filing separately will not be able to take advantage of the program regardless of their incomes.

## **Are these income limits adjusted for inflation?**

Yes, these income limits are indexed for inflation and then rounded to the nearest multiple of \$50.



## **How does one buy an "Education Savings Bond?"**

Since the program utilizes the Series EE Bond, there are no differences in purchase procedures except (1) the Bond must have been purchased after December 31, 1989, (2) it must be registered in the taxpayer's name alone, with or without a beneficiary, or in the name of the taxpayer and spouse (not a dependent child) as coowners, and (3) the taxpayer must be at least 24 years old before the issue date of the Bond. Otherwise, the Bonds may be purchased in the same manner as any other Series EE Bond.

## **Where can I buy Series EE Bonds?**

Savings Bonds can be purchased through more than 40,000 financial institutions nationwide or through employers offering the payroll savings plan. Participants enrolled in payroll savings plans who intend to use the redemption proceeds of Series EE Bonds issued after December 31, 1989, for eligible educational expenses should review the form of registration being used to ensure it meets the requirements of the law.

## **Are there limitations on the denomination of the Bonds used in the program?**

No, any Series EE Bond denomination, from \$50 to \$10,000, is eligible for the education Bond program as long as the other criteria for the program are met.

## **What are the redemption procedures for holders of qualified Bonds?**

There are no changes in the redemption procedures for paying agents. It is the Bond owner's responsibility to maintain a record of Bond redemption transactions to support claims for exclusion from gross income in the year that qualified Bonds are redeemed and qualifying educational expenses are incurred. However, if an owner redeeming Series EE Bonds issued after 1989 states his or her intention to exclude interest from gross income in accordance with the education feature, and is at the same time redeeming Bonds issued prior to January 1, 1990 the paying agent should provide separate redemption values and accrued interest subtotals for Bonds issued prior to January 1, 1990 and for those issued on or after January 1, 1990. If the Bond owner has not made a record of the serial numbers, face amounts, and issue dates, the agent should advise the customer to do so prior to redeeming the Bonds. An optional IRS Form 8818 which provides instructions and space to record this information, can be obtained, like other tax forms, from an IRS distribution center.

## **How does one exclude the interest income on the tax form?**

Form 8815, available from the IRS, includes the necessary worksheet and instructions to taxpayers for use in connection with tax returns.

**Will the educational institution be required to verify the educational expenses of the taxpayer, taxpayer's spouse or the taxpayer's dependent?**

Generally no. However, the taxpayer should retain receipts or canceled checks for educational expenses as part of the taxpayer's record to substantiate his or her claim to an exclusion from income of the Bonds cashed.

## **What happens if Bonds dated before January 1, 1990, are redeemed and new Bonds bought with the proceeds?**

Accrued interest earnings on the Bonds redeemed are taxable to the owner in the year of the redemption regardless of whether the proceeds are used to purchase new Series EE Bonds.

## **Who can buy Education Savings Bonds?**

Anyone, including grandparents and other relatives, so long as the Bonds are registered according to the specifications listed in A16.



## **Can a child be named as beneficiary on a Series EE Bond for which the interest exclusion will be taken?**

Yes. Any person may be named as beneficiary without affecting the eligibility of the Bond for exclusion. A child may not be a coowner of such a Bond.

## **Is there a limit on the amount of Savings Bonds a person may buy?**

Yes. The annual limit on the amount of Series EE Bonds an individual may buy is \$15,000, issue price (\$30,000, face amount). This limit applies to the amount of Bonds that may be purchased in the name of any one person in any one calendar year; it has no effect on cumulative holdings. Purchasing Bonds in coownership form can effectively double the limit, assuming the coowner has purchased no other Bonds. There is no limit on the amount of HH Bonds that may be issued in exchange for Series E and EE Bonds and Savings Notes, or purchased with the redemption proceeds of matured Series H Bonds.

## **Is there a limitation on the number or amount of Bonds one can buy for use in the program?**

Yes, the standard limitation of \$30,000 face value or \$15,000 purchase price (\$60,000/\$30,000 for husband and wife holding Bonds as coowners) in Bonds per year also applies to the education Bond program. However, there is no limit to the amount of Bonds that can be accumulated for educational expenses over time as long as these Bonds do not exceed the annual purchase limitations discussed above and otherwise comply with program requirements.

## **No Probate**

If, upon the death of an owner, there is a surviving co-owner or beneficiary named on the Bonds, the Bonds do not form a part of a decedent's estate for probate purposes. Subject to applicable estate or inheritance taxes, if any, they become the sole and absolute property of the survivor.

## **Payment of Interest**

Interest on EE Bonds issued March 1993 or later accrues through monthly increases in redemption value, and is payable when a Bond is cashed. Interest accrues semiannually on most older EE and E Bonds. The redemption value reflects the principal amount plus interest accrued during the holding period. Interest on HH Bonds is paid semiannually.

## Redemption Date

From this menu, you can enter in a new redemption date to see what your bonds will be worth in the future. You can only type in dates that would be valid during the interval that is covered for this redemption period. The program will scan the loaded Table of Redemption Values (GOVTLB.DB) and check to see if the date that you specified falls within the range of the table. The date that you see when you bring up this item is the date from your system. Change this date and generate the new reports. When you come back into this field, you will see the system date again. Your changes to the redemption date will be valid until you select this option again, when once again the redemption date will revert back to the system date. You can change the fields by either clicking twice with your mouse or using the TAB key until the field is highlighted.

## **Tax Benefits**

Reporting of interest for Federal income tax purposes may be deferred until EE Bonds are cashed, disposed of, or reach final maturity, whichever comes first. Reporting of accrued interest on Bonds and Notes presented in exchange for HH Bonds may continue to be deferred, for Federal tax purposes, until the HH

Bonds are cashed, disposed of, or reach final maturity, whichever comes first. EE and HH Bonds are exempt from state and local income and personal property taxes but are subject to inheritance and estate taxes levied by states and localities. Subject to certain income and other limitations, Bonds purchased beginning January 1, 1990, may be free of Federal income tax if their owners pay qualified educational expenses for themselves or their dependents in the year the Bonds are redeemed.

## **What is the best way to buy Savings Bonds?**

The simplest, most convenient way to purchase Bonds is through the payroll savings plan offered by thousands of companies and organizations, including the U.S. government and many state and local governments. Through the plan, an employee can arrange with his or her company to set aside a certain amount of money each payday to buy Savings Bonds. Savings Bonds may also be purchased through most commercial banks and other financial institutions throughout the country.



## **What is the market-based interest formula for Savings Bonds?**

The market-based rate formula sets interest yields on Series EE Bonds held five years or longer and outstanding Series E Bonds and U.S. Savings Notes (Freedom Shares). Market-based rates are set semiannually, in May and November, and Bonds held five years or longer receive the average of semiannual rates in effect during the holding period, compounded semiannually, if it averages more than the guaranteed minimum rate. For Bonds issued since March 1, 1993, there is a guaranteed minimum annual rate of 4 percent no matter how long the Bond is held, up to original maturity, a term of 18 years; these Bonds reach face value in no more than 18 years and will continue to pay interest for 30 years from issue.

## **Where can I get more information on Savings Bonds?**

Current rate information can be obtained toll-free by calling a recorded message at 1-800-4US BOND (1-800-487-2663). Other information can be obtained from many financial institutions, Federal Reserve Banks and Branches, and Savings Bonds Division District Offices. Information on replacing lost or stolen Bonds, or reissuing existing securities, can be obtained by writing to the Bureau of the Public Debt, Parkersburg, WV 26106-1328.



