IV. EDUCATION INCENTIVES

A. MODIFICATIONS TO EDUCATION IRAS (SEC. 401 AND 414 OF THE SENATE AMENDMENT AND SECS. 530 AND 127 OF THE CODE)

PRESENT LAW

In general

Section 530 of the Code provides tax-exempt status to education individual retirement accounts (“education IRAs”), meaning certain trusts or custodial accounts which are created or organized in the United States exclusively for the purpose of paying the qualified higher education expenses of a designated beneficiary. Contributions to education IRAs may be made only in cash. Annual contributions to education IRAs may not exceed $500 per beneficiary (except in cases involving certain tax-free rollovers, as described below) and may not be made after the designated beneficiary reaches age 18.

Phase-out of contribution limit

The $500 annual contribution limit for education IRAs is generally phased-out ratably for contributors with modified adjusted gross income above the phase-out range for married taxpayers filing a joint return ($150,000 to $160,000 of modified adjusted gross income). Individuals with modified adjusted gross income above the phase-out range are not allowed to make contributions to an education IRA established on behalf of any individual.

Treatment of distributions

Earnings on contributions to an education IRA generally are subject to tax when withdrawn. However, distributions from an education IRA are excludable from the gross income of the beneficiary to the extent that the total distribution does not exceed the “qualified higher education expenses” incurred by the beneficiary during the year the distribution is made.

If the qualified higher education expenses of the beneficiary for the year are less than the total amount of the distribution (i.e., contributions and earnings combined) from an education IRA, then the qualified higher education expenses are deemed to be paid from a pro-rata share of both the principal and earnings components of the distribution. Thus, in such a case, only a portion of the earnings are excludable (i.e., the portion of the earnings based on the ratio that the qualified higher education expenses bear to the total amount of the distribution) and the remaining portion of the earnings is includible in the beneficiary’s gross income.

The earnings portion of a distribution from an education IRA that is includible in income is also subject to an additional 10-percent tax. The 10-percent additional tax does not apply if a distribution is made on account of the death or disability of the designated beneficiary, or on account of a scholarship received by the designated beneficiary.

The additional 10-percent tax also does not apply to the distribution of any contribution to an education IRA made during the taxable year if such distribution is made on or before the date that a return is required to be filed (including extensions of time) by the beneficiary for the taxable year during which the contribution was made (or, if the beneficiary is not required to file such a return, April 15th of the year following the taxable year during which the contribution was made).

Present law allows tax-free transfers or rollovers of account balances from one education IRA benefiting one beneficiary to another education IRA benefiting another beneficiary (as well as redesignations of the named beneficiary), provided that the new beneficiary is a member of the family of the old beneficiary and is under age 30.

Any balance remaining in an education IRA is deemed to be distributed within 30 days after the date that the beneficiary reaches age 30 (or, if earlier, within 30 days of the date that the beneficiary dies).

Qualified higher education expenses

The term “qualified higher education expenses” includes tuition, fees, books, supplies, and equipment required for the enrollment or attendance of the designated beneficiary at an eligible education institution, regardless of whether the beneficiary is enrolled at an eligible educational institution on a full-time, half-time, or less than half-time basis. Qualified higher education expenses include expenses with respect to undergraduate or graduate-level courses. In addition, qualified higher education expenses include amounts paid or incurred to purchase tuition credits (or to make contributions to an account) under a qualified State tuition program, as defined in section 529, for the benefit of the beneficiary of the education IRA.

Moreover, qualified higher education expenses include, within limits, room and board expenses for any academic period during which the beneficiary is at least a half-time student. Room and board expenses that may be treated as qualified higher education expenses are limited to the minimum room and board allowance applicable to the student in calculating costs of attendance for Federal financial aid programs under section 472 of the Higher Education Act of 1965, as in effect on the date of enactment of the Small Business Job Protection Act of 1996 (August 20, 1996). Thus, room and board expenses cannot exceed the following amounts: (1) for a student living at home with parents or guardians, $1,500 per academic year; (2) for a student living in housing owned or operated by the eligible education institution; the institution’s “normal” room and board charge; and (3) for all other students, $2,500 per academic year.

Qualified higher education expenses generally include only out-of-pocket expenses. Such qualified higher education expenses do

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Special estate and gift tax rules apply to contributions made to and distributions made from education IRAs.
not include expenses covered by educational assistance for the benefit of the beneficiary that is excludable from gross income. Thus, total qualified higher education expenses are reduced by any such recognized post-secondary expenses that are excludable from gross income under section 127. Present law also provides that if any qualified higher education expenses are taken into account in determining the amount of the exclusion for a distribution from an education IRA, then no deduction (e.g., for trade or business expenses), exclusion (e.g., for interest on education savings bonds) or credit is allowed with respect to such expenses.

Eligible educational institutions are defined by reference to section 481 of the Higher Education Act of 1965. Such institutions generally are accredited post-secondary educational institutions offering credit toward a bachelor’s degree, an associate’s degree, a graduate-level or professional degree, or any other recognized post-secondary credential. Certain proprietary institutions and post-secondary education institutions and other recognized post-secondary institutions, non-profit private schools primarily involving sports, games, or hobbies that do not primarily involve instruction or training for educational benefits, such as employer-provided educational benefits, are excluded from the list. A new provision provides that rule prohibiting contributions to an education IRA after the beneficiary attains age 18 does not apply in the case of a special needs beneficiary. Finally, the age 30 limitation does not apply in the case of a rollover contribution for the benefit of a special needs beneficiary or a change in beneficiaries to a special needs beneficiary.

The Senate amendment clarifies that corporations and other entities (including tax-exempt organizations) are permitted to make contributions to education IRAs, regardless of the income of the corporation or entity during the year of the contribution.

Coordination with qualified tuition programs

The Senate amendment modifies the definition of room and board expenses considered to be qualified higher education expenses. The conference agreement modifies the provisions relating to qualified tuition programs, below.

Coordination with qualified tuition programs

The Senate amendment modifies the definition of room and board expenses considered to be qualified higher education expenses. The conference agreement modifies the provisions relating to qualified tuition programs, below.
Coordination with HOPE and Lifetime Learning credits

The Senate amendment allows a taxpayer to claim a HOPE credit or Lifetime Learning credit for a taxable year and to exclude from gross income (and earnings portions) from a qualified tuition program on behalf of the same student as long as the distribution is not used for the same expenses for which a credit was claimed.

Rollovers for benefit of same beneficiary

The Senate amendment provides that a transfer of credits (or other amounts) from one qualified tuition program to a qualified tuition program for the benefit of the same beneficiary is not considered a distribution. This rollover treatment does not apply to more than one transfer within any 12-month period with respect to the same beneficiary.

Memorandum

The Senate amendment provides that, for purposes of tax-free rollovers and changes of designated beneficiaries, a "member of the family" includes first cousins of the original beneficiary.

Effective date

The provisions are effective for taxable years beginning after December 31, 2001, except that the exclusion from gross income for certain distributions from a qualified tuition program established and maintained by an entity other than a State (or agency or instrumentality thereof) is effective for taxable years beginning after December 31, 2003.

The conference agreement follows the Senate amendment, with modifications. The conference agreement modifies the definition of qualified higher education expenses to include amounts used for qualifying higher education expenses at a qualified educational institution established and maintained by entities other than States (or agencies or instrumentality thereof).26 A special needs beneficiary would be defined as under the provisions relating to education IRAs, described above.

The conference agreement repeals the prior year rollover rules for qualified tuition programs.27 A qualified tuition program must impose a more than de minimis monetary penalty on any refund of earnings not used for qualified higher education expenses. Thus, for example, the earnings portion is includible in gross income (like the additional tax that applies to such distributions from education IRAs). The same exceptions that apply to the 10-percent additional tax with respect to education IRAs apply. A special rule applies because the exclusion for earnings on distributions used for qualified higher education expenses does not apply to qualified tuition programs of private institutions until 2004. Under the special rule, the 10-percent additional tax does not apply to any payment in a taxable year beginning before January 1, 2004, which is includible in gross income but used for qualified higher education expenses. Thus, for example, the earnings portion of a distribution from a qualified tuition program of a private institution that is made in 2003 and that is used for qualified higher education expenses is not subject to the additional tax, even though the earnings portion is includible in gross income. Conforming the penalty to the education IRA provisions will make it easier...
C. EXCLUSION FOR EMPLOYER-PROVIDED EDUCATIONAL ASSISTANCE (SEC. 117 OF THE CODE)

Education expenses paid by an employer for its employees are generally deductible by the employer. Employer-paid educational expenses are excludable from the gross income and wages of an employee if provided under a section 127 educational assistance plan or if the expenses qualify as a working condition fringe benefit.

Section 127 education assistance plan provided by an employer for its employees is a qualified educational assistance plan that includes programs maintained by private institutions.

No provision.

HOUSE BILL

No provision.

SENATE AMENDMENT

The Senate amendment increases the income phase-out ranges for eligibility for the student loan interest deduction to $20,000 to $65,000 for single taxpayers and to $40,000 to $130,000 for married taxpayers filing joint returns. These income phase-out ranges are adjusted annually for inflation after 2002.

The Senate amendment eliminates the income threshold for taxpayers to allocate expenses between contributions to an employer-sponsored educational savings program and a qualified education program for the benefit of the same designated beneficiary to another qualified tuition program maintained by the same State and between a private prepaid tuition program and a savings program.

The conferees intend that this provision will be the taxpayer. The educational assistance program for which the credit or deduction is allowable must be maintained by the same State and between a private institution.

The conferees expect that the Secretary will exercise authority under sections 502(a)(7) and 513(h) to require appropriate reporting, e.g., the amount of distributions and the earnings portions of distributions (taxable and nontaxable), to facilitate the determinations under section 408(a)(2) and 409(a)(1).

In general, education expenses are deductible by an individual under section 164 if the education expenses, other than amounts covering regular living expenses, are paid by an employer and are incurred for the benefit of the individual as a condition of continued employment. However, education expenses are generally not deductible if they do not qualify as a working condition fringe benefit.

The conference agreement provides that, in order for a tuition program to be a private prepaid tuition program, assets of the program must be held in a trust created or organized in the United States for the exclusive benefit of designated beneficiaries.

As under the Senate amendment, the conference agreement provides that a transfer of credits (or other amounts) from one private prepaid tuition program to another private prepaid tuition program or to an individual if that individual is claimed as a dependent of the taxpayer as of the time the education expenses are paid by an employer.

The educa-

No provision.

HOUSE BILL

No provision.

SENATE AMENDMENT

The Senate amendment increases the income phase-out ranges for eligibility for the student loan interest deduction to $20,000 to $65,000 for single taxpayers and to $40,000 to $130,000 for married taxpayers filing joint returns. These income phase-out ranges are adjusted annually for inflation after 2002.

The Senate amendment repeals both the limit on the number of months during which interest paid on a qualified education loan is deductible and the requirement that voluntary payments of interest are not deductible.

Effective date.—The provision is effective for interest paid on qualified education loans after December 31, 2001.

CONFERENCE AGREEMENT

The conference agreement follows the Senate amendment.


PRESENT LAW

Section 117 excludes from gross income amounts received as a qualified scholarship by an individual who is a candidate for a degree 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. In addition to the exclusion for qualified scholarships, section 117 provides an exclusion from gross income for qualified tuition reductions for certain educational expenses provided to employees (and their spouses and dependents) of certain educational organizations.

The exclusion for qualified scholarships and qualified tuition reductions does not apply to any amount received by a student that represents payment for teaching, research, or other services by the student received in exchange for providing the scholarship or tuition reduction.

The National Health Service Corps Scholarship Program (the “NHSC Scholarship Program”) and the F. Edward Hebert Armed Forces Health Professions Scholarship and Financial Assistance Program (the “Armed Forces Scholarship Program”) provide educational awards to participants on the condition that the participants provide certain services. In the case of the NHSC Program, the recipient of the scholarship is obligated 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 healthcare professionals of the Armed Forces Scholarship Program, the recipient of the scholarship is obligated to
serve a certain number of years in the military at an armed forces medical facility. Because the recipients are required to perform services in exchange for the education awards, the awards used to pay higher education expenses are taxable income to the recipient.

**HOUSE BILL**

**No provision.**

**SENATE AMENDMENT**

The Senate amendment provides that amounts received by an individual under the NHSC Scholarship Program or the Armed Forces Scholarship Program are eligible for tax-free treatment as qualified scholarships under section 117, without regard to any service obligation by the recipient. As with other qualified scholarships under section 117, these amounts are included in gross income and are not refunded to the Federal Government.

Effective date.—The provision is effective for education awards received after December 31, 2001.

**CONFERENCE AGREEMENT**

The conference agreement follows the Senate amendment.

F. **TAX BENEFITS FOR CERTAIN TYPES OF BONDS (SECS. 142, 146, 145) — FEDERAL, STATE AND LOCAL GOVERNMENTS**

**PRESENT LAW**

Tax-exempt bonds

**In general.**

Interest on debt, incurred by States or local governments is excluded from income if the proceeds of the borrowing are used to carry out governmental functions of those entities in accordance with governmental funds (sec. 103). Like other activities carried out or paid for by States and local governments, the construction, renovation, and operation of public schools is an activity eligible for financing with the proceeds of tax-exempt bonds.

Interest on bonds that nominally are issued to finance certain private activities is taxable, unless the proceeds of the borrowing are spent for the purpose of the borrowing. The Code or in a non-Code provision of a revenue act, financing an activity that is reasonably required to be financed.

Many exceptions are made to the general rule. In most cases, the aggregate volume of private activity bonds is restricted by annual aggregate volume limits imposed on bonds issued by issuers within each State. These limits are determined by the Treasury Department. Present law includes several exceptions to the tax-free treatment of proceeds of tax-exempt bonds. In general, arbitrage restrictions limiting the ability to profit from investment of tax-exempt bond proceeds. In general, arbitrage profits may be earned only during specified periods before funds are needed for the purpose of the borrowing (or on specified types of investments with a term of 10 years or more) on the bonds. Subject to limited exceptions, profits that are earned during these periods or on such investments must be rebated to the Federal Government.

**Arbitrage restrictions on tax-exempt bonds**

The Federal income tax does not apply to the income of States and local governments that is derived from the exercise of an essential governmental function. To prevent these tax-exempt activities from issuing more Federal subsidized tax-exempt bonds than is necessary for the activity being financed or from issuing such bonds earlier than needed for the purpose of the borrowing, the Code includes arbitrage restrictions limiting the ability to profit from investment of tax-exempt bond proceeds. In general, arbitrage profits may be earned only during specified periods before funds are needed for the purpose of the borrowing (or on specified types of investments with a term of 10 years or more).

Subject to limited exceptions, profits that are earned during these periods or on such investments must be rebated to the Federal Government. Present law includes three exceptions to the arbitrage rebate requirements applicable to education-related bonds. First, issuers of all types of tax-exempt bonds are not required to rebate arbitrage profits if all of the proceeds of the bond proceeds for the purpose of the borrowing within six months after issuance. 

Second, in the case of bonds to finance certain construction activities, including school construction, the construction period is extended to 24 months. Arbitrage profits earned on construction proceeds are not required to be rebated if all such proceeds (other than amounts spent by the end of the 24-month period and prescribed intermediate spending periods are satisfied. Issuers qualifying for this “construction bond” exception may elect to be subject to a fixed penalty payment regime in lieu of rebate if they fail to satisfy the spending requirements.

Third, governmental bonds issued by “small” governments are not subject to the rebate requirement. Small governments are defined as general purpose governmental units not based on annualized expenditures of charitable organizations deemed to be taxable income. The 0.1% arbitrage profits earned during the six-month period are not required to be rebated if all such proceeds (other than amounts spent by the end of the 24-month period and prescribed intermediate spending periods are satisfied. Issuers qualifying for this “construction bond” exception may elect to be subject to a fixed penalty payment regime in lieu of rebate if they fail to satisfy the spending requirements.

**Qualified zone academy bonds**

As an alternative to traditional tax-exempt bonds, States and local governments are given the authority to issue “qualified zone academy bonds.” Present law, a total of $400 million of qualified zone academy bonds may be issued in each of 1998 through 2001. The $400 million aggregate bond authority is allocated each year to the States according to their respective populations of individuals below the poverty line. Each State, in turn, allocates the credit to qualified zone academies within such State. A State may carry over any unused allocation for up to two years (three years for authorization before 2000).

**Tax benefits**

An eligible financial institution holding a qualified zone academy bond on the credit allowance date (i.e., one-year anniversary of the issuance of the bond) is entitled to a credit. The credit amount is subject to a cap (3% of bond proceeds or $187.5 million if greater). The volume limits are extended to 24 months. Arbitrage profits earned on qualifying zone academy bonds may be issued in each of 1998 through 2001. The $400 million aggregate bond authority is allocated each year to the States according to their respective populations of individuals below the poverty line. Each State, in turn, allocates the credit to qualified zone academies within such State. A State may carry over any unused allocation for up to two years (three years for authorization before 2000).
for free or reduced-cost lunches under the school lunch program established under the National School Lunch Act.

No provision.

SENATE AMENDMENT
Increase amount of governmental bonds that may be issued to finance the "small governmental unit" arbitrage rebate exception

The additional amount of governmental bonds issued by public schools that small governmental units may issue without being subject to the arbitrage rebate requirements is increased from $5 million to $10 million. Thus, these governmental units may issue up to $15 million of governmental bonds in a calendar year provided that at least $10 million of the bonds are used to finance public school construction expenditures.

Allow issuance of tax-exempt private activity bonds for public school facilities

The private activities for which tax-exempt bonds may be issued are expanded to include elementary and secondary public school facilities which are owned by private, for-profit corporations pursuant to public-private partnership agreements with a State or local educational agency. The term school facility includes building furnishings and functionally related and subordinate land (including stadiums or other athletic facilities primarily used for school events) and depreciable individual property used in the school facility. The school facilities for which these bonds are issued must be operated by a public educational agency as part of a system of public schools.

A public-private partnership agreement is defined as an arrangement pursuant to which the for-profit corporation constructs, owns, and operates a school facility for a public school agency (typically pursuant to a lease arrangement). The agreement must provide that, at the end of the contract term, ownership of the bond-financed property is transferred to the public school agency party to the agreement for no additional consideration.

Issuance of these bonds is subject to a separate annual per-State private activity bond volume limit equal to $10 per resident ($5 million, if greater than $5 million). As with the present-law State private activity bond volume limits, States may exceed their present-law State private activity bond volume limits. As with the present-law State private activity bond volume limits, States can decide how they wish to allocate the authority in the hands of the State or local government agencies. Bond authority that is unused in any year in which it arises may be carried forward for up to three years for public school projects under rules similar to the carryforward rules of the present-law private activity bond volume limits.

Effective date
The provisions are effective for bonds issued after December 31, 2001, and before January 1, 2005.

CONFERENCE AGREEMENT
The conference agreement follows the Senate amendment. H. MODIFY RULES GOVERNING TAX-EXEMPT BONDS FOR SECTION 501(c)(3) ORGANIZATIONS AS APPLIED TO ORGANIZATIONS ENGAGED IN TIMBER CONSERVATION ACTIVITIES (SEC. 423 OF THE SENATE AMENDMENT AND NEW SEC. 222 OF THE CODE)

PRESENT LAW

Interest on State or local government bonds is tax-exempt when the proceeds of the bonds are used to finance activities carried out by or paid for by those governmental units. Interest on bonds issued by State or local governments acting as conduit borrowers for private activities is taxable unless a specific exception is included in the Code. One such exemption allows tax-exempt bonds to be issued to finance activities of non-profit organizations engaged in timber conservation activities. Qualified 501(c)(3) bonds may be issued only if the tax-exempt interest is not subject to the alternative minimum tax. The tax-exempt portion of any interest paid on tax-exempt bonds must be allocable to the acquisition of timber land by organizations that own or control timberland. The net tax-exempt interest may be taxable. An example of such an issue would be qualified 501(c)(3) bonds issued to finance purchase of land and standing timber, when the timber was to be sold.

As is true of other private activities receiving tax-exempt financing, beneficiaries of qualified 501(c)(3) bonds are restricted in the arrangements they may have with private businesses relating to control and use of bond-financed property.

No provision.

SENATE AMENDMENT

The Senate amendment modifies the rules governing issuance of qualified 501(c)(3) bonds for the acquisition of timber land by organizations a principal purpose of which is conservation of timberland. Under these rules, the bonds will not have to be paid (to avoid loss of tax-exemption on interest) when the timber is harvested and sold. In addition, the Senate amendment provision allows these organizations a principal purpose of which is conservation of timberland to enter into certain otherwise prohibited timber management arrangements with private businesses without losing tax-exemption.

Effective date—The provision is effective for bonds issued after December 31, 2001, and before January 1, 2005.

CONFERENCE AGREEMENT

The conference agreement does not include the Senate amendment provision.

H. DEDUCTION FOR QUALIFIED HIGHER EDUCATION EXPENSES (SEC. 431 OF THE SENATE AMENDMENT AND NEW SEC. 222 OF THE CODE)

PRESENT LAW

Deduction for education expenses

Under present law, an individual taxpayer generally may not deduct the education and training expenses of the taxpayer or the taxpayer’s dependents. However, a deduction for education expenses generally is allowed under Internal Revenue Code (‘‘the Code’’) section 117 if the education or training (1) is qualified tuition and related expenses for the acquisition of a degree or similar educational assistance and scholarships (or the gross income of either the student or the taxpayer claiming the credit) during the taxable year.

Lifetime Learning credit

Individual taxpayers are allowed to claim a nonrefundable credit, the ‘‘HOPE’’ credit, against Federal income taxes up to $1,500 per year for qualified tuition and related expenses paid for the first two years of the student’s post secondary education in a degree or certificate program. The credit is 10 percent on the first $1,000 of qualified tuition and related expenses, and 50 percent on the next $1,000 of qualified tuition and related expenses. The qualified tuition and related expenses must be incurred on behalf of the taxpayer, the taxpayer’s spouse, or a dependent or other individual for whom the taxpayer claims an exemption.

The HOPE credit is available for ‘‘qualified tuition and related expenses,’’ which include tuition and fees required to be paid to an eligible educational institution in connection with enrollment or attendance of an eligible student. Charges and fees for equipment, books, transportation, and similar personal, living, or family expenses are not eligible for the credit.

The expenses of education involving sports, games, or hobbies are not qualified tuition and related expenses unless this education is part of the student’s degree program.

Qualified tuition and related expenses generally include only out-of-pocket expenses. Qualified tuition and related expenses do not include expenses covered by employer-provided educational assistance and scholarships that are not required to be included in gross income of the individual taxpayer and that do not reduce the individual taxpayer’s gross income.

Qualified tuition and related expenses incurred during the taxable year on behalf of the taxpayer, the taxpayer’s spouse, or any dependents. For expenses paid after June 30, 1998, and prior to January 1, 2003, up to $5,000 of qualified tuition and related expenses per taxpayer return are eligible for the Lifetime Learning credit (i.e., the maximum credit per taxpayer return is $1,000 paid after December 31, 2002, up to $10,000 of qualified tuition and related expenses per taxpayer return will be eligible for the Lifetime Learning credit (i.e., the maximum credit per taxpayer return will be $2,000).

In contrast to the HOPE credit, a taxpayer may claim the Lifetime Learning credit for

38 Thus, an eligible student who incurs $1,000 of qualified tuition and related expenses is eligible for a $200 HOPE credit. If the student incurs $2,000 of qualified tuition and related expenses, then he or she is eligible for a $1,000 HOPE credit

39 The HOPE credit may not be claimed against a taxpayer’s alternative minimum tax liability.
An unlimited number of taxable years. Also in contrast to the HOPE credit, the maximum amount of the Lifetime Learning credit that may be claimed on a taxpayer’s return will be determined on the number of students in the taxpayer’s family—that is, the HOPE credit is computed on a per student basis, while the Lifetime Learning credit is computed on a family-wide basis. A diligent student’s Lifetime Learning credit amount that a taxpayer may otherwise claim is phased-out ratably for taxpayers with modified AGI between $40,000 and $50,000 ($80,000 and $100,000 for joint returns).

HOUSE BILL
No provision.

SENATE AMENDMENT
The Senate amendment permits taxpayers an above-the-line deduction for qualified higher education expenses paid by the taxpayer during a taxable year. Qualified higher education expenses are defined in the same manner as for purposes of the HOPE credit.

In 2002 and 2003, taxpayers with adjusted gross income that does not exceed $65,000 ($130,000 in the case of married couples filing joint returns) are entitled to a maximum deduction of $3,000 per year. Taxpayers with adjusted gross income above those thresholds would not be entitled to a deduction. In 2004 and 2005, taxpayers with adjusted gross income that does not exceed $65,000 ($130,000 in the case of married taxpayers filing joint returns) are entitled to a maximum deduction of $5,000 and taxpayers with adjusted gross income that does not exceed $80,000 ($160,000 in the case of married taxpayers filing joint returns) are entitled to a maximum deduction of $2,000.

Taxpayers are not eligible to claim the deduction and a HOPE or Lifetime Learning Credit in the same year with respect to the same student. A taxpayer may not claim a deduction in the year for interest paid after December 31, 2001, and before January 1, 2007.

Effective date.—The Senate amendment applies to taxable years beginning after December 31, 2001, and before January 1, 2007.

CONFERENCE AGREEMENT
The conference agreement does not include the Senate amendment provision.

K. ENHANCED DEDUCTION FOR CHARITABLE CONTRIBUTION OF BOOK INVENTORY FOR EDUCATIONAL PURPOSES (SEC. 434 OF THE SENATE AMENDMENT AND SEC. 170 OF THE CODE)

PRESENT LAW
In the case of a charitable contribution of inventory or other ordinary-income or short-term capital gain property, the amount of the deduction is limited to the basis of the property in the year the contribution was made. In the case of a charitable contribution of tangible personal property, the deduction is limited to the taxpayer’s basis in such property if the use by the recipient charitable organization is unrelated to the organization’s tax-exempt purposes or if the property is contributed to a private operating foundation.

Under present law, a taxpayer’s deduction for charitable contributions of book inventory generally is limited to the taxpayer’s basis (typically, cost) in the inventory. However, certain corporations may claim a deduction in excess of basis for certain charitable contributions to charitable organizations other than private non-operating foundations. This enhanced deduction is equal to the lesser of (1) basis plus one-half of the item’s appreciated value (i.e., basis plus one-half of fair market value minus basis) or (2) two times basis. To be eligible for an enhanced deduction, (1) the use of the property by the donee must be related to the donee’s exempt purpose and be used by the donee solely for the care of the ill, the needy, or infants; (2) the property must not be transferred by the donee in exchange for money, other property, or services; and (3) the taxpayer must establish that the fair market value of the donated item exceeds basis.

HOUSE BILL
No provision.

PROVISION
An above-the-line deduction for interest paid on qualified education loans is permitted during the first 60 months in which interest payments are required. Required payments of interest generally do not include voluntary payments, such as interest payments made after the due date of loan forbearance. Months during which interest payments are not required because the qualified education loan is in deferral or forbearance do not count toward the 60-month period. No deduction is allowed to an individual if that individual is claimed as a dependent on another taxpayer’s return for the taxable year. The maximum allowable annual deduction is $2,500. The deduction is phased-out ratably for single taxpayers with modified adjusted gross income between $40,000 and $55,000 and for married taxpayers filing joint returns with modified adjusted gross income between $90,000 and $75,000. The income ranges will be adjusted for inflation after 2009. A taxpayer taking the credit in a taxable year may not claim a HOPE or Lifetime Learning credit in the same year with respect to the same student. A taxpayer may not claim a deduction and a HOPE or Lifetime Learning credit with respect to the amount taken into account in computing a health care facility conducting postgraduate training.

Effective date.—The provision is effective for taxable years beginning after December 31, 2008.

CONFERENCE AGREEMENT
The conference agreement does not include the Senate amendment provision.

J. DEDUCTION FOR QUALIFIED EMERGENCY RESPONSE EXPENSES OF ELIGIBLE EMERGENCY RESPONSE PROFESSIONALS (SEC. 433 OF THE SENATE AMENDMENT AND NEW SEC. 224 OF THE CODE)

PRESENT LAW
Employee business expenses are deductible only as an itemized deduction and only to the extent that the expenses, along with the taxpayer’s other itemized deductions, exceed two percent of the taxpayer’s adjusted gross income. Itemized deductions are reduced by the overall limitation on itemized deductions, which generally applies to taxpayers with adjusted gross income in excess of $132,950 (for 2001).

Another section of the Senate amendment makes certain modifications to present law.

HOUSE BILL
No provision.
The Senate amendment provides that contributions of book inventory to certain educational organizations are entitled to the present-law deduction. Eligible educational organizations are (1) educational organizations that normally maintain a regular faculty and curriculum and normally have a regularly enrolled body of students in attendance at the place where its educational activities are regularly carried on; (2) charities organized primarily for purposes of supporting elementary and secondary education; and (3) charities organized primarily to make books available to the general public at no cost or to operate a library or reading room and regularly carry on activities associated with meals, lodging, insurance, transportation, and similar personal, living, or family expenses are not eligible for the credit. The expenses of providing instruction, sports, games, or hobbies are not qualified tuition and related expenses unless this education is part of the student’s degree program.

Qualified tuition and related expenses generally include only out-of-pocket expenses.42 The qualified tuition and related expenses do not include expenses covered by employer-provided educational assistance and scholarships that are not required to be included in the gross income of the individual claiming the credit. Thus, total qualified tuition and related expenses are reduced by any scholarship or fellowship grants included from gross income under section 117 and any other tax-free educational benefits received by the student (or the taxpayer claiming the credit) during the taxable year.

LIFETIME LEARNING CREDIT

Under present law, individual taxpayers may claim a nonrefundable credit, the Lifetime Learning credit, against Federal income taxes equal to 20 percent of qualified tuition and related expenses paid for educational activities that are (1) tied to (a) challenging State performance standards or (b) strategies and programs designed to improve student performance, or substantially increasing student academic achievement and student performance, or substantially increasing the knowledge and teaching skills of the individual; and (2) is provided in a program or setting in which students can learn; (2) is tied to (a) challenging State or local content standards and student performance standards or (b) strategies and programs designed to improve student performance, or substantially increasing student academic achievement and student performance, or substantially increasing the knowledge and teaching skills of the individual; and (3) is designed to provide instruction directly related to the curriculum and academic subjects in which the individual provides instruction.43 The credit is available for one course per semester,63 after which the maximum credit amount and the AGI phase-out ranges are indexed for inflation.

The HOPE credit is available for “qualified tuition and related expenses,” which includes tuition and fees required to be paid to an eligible educational institution as a condition of enrollment or attendance of an eligible student. The credit is supposed to enhance the ability of the individual to understand and use State standards for the academic subjects in which the individual provides instruction. The law does not specify how to teach children with different learning styles, particularly children with disabilities and children with special learning needs (including children who are gifted and talented), or designed to provide instruction in how to best discipline children in the classroom and identify early and appropriate interventions to help children described in (c) learn; (2) is tied to (a) challenging State or local content standards and student performance standards or (b) strategies and programs designed to improve student performance, or substantially increasing student academic achievement and student performance, or substantially increasing the knowledge and teaching skills of the individual; and (3) is of sufficient intensity and duration to have a positive and lasting impact on the performance of the individual in the classroom (which does not include one day or short-term workshops and conferences); and (3) is part of a program of professional development approved and certified by the appropriate local educational agency as furthering the goals described in (1) and (2).

No other deduction or credit is allowed with respect to the amount taken into account under this provision. A deduction is allowed for qualified professional development expenses under the provision only to the extent that the amount of such expenses exceeds the amount includable under the provisions relating to education savings bonds, education IRAs, and qualified tuition plans.

May 25, 2001

Conference Agreement

The conference agreement does not include the Senate amendment provision. The conference agreement does not include

PRESENT LAW

Deduction for education expenses

Under present law, an individual taxpayer generally may not deduct the education and training expenses of the taxpayer or the taxpayer’s dependents. However, a deduction for education expenses generally is allowed under section 112 of the Code (the Code) to the extent that such expenses are allowable with respect to an individual student in attendance at a school described in section 117 and are allowed for qualified professional development expenses paid for taxable years beginning after 2001, the HOPE credit is computed on a per student basis.

The conference agreement does not include

CREDIT FOR CLASSROOM MATERIALS

The conference agreement does not include the Senate amendment provision.

PRESENT LAW

Unreimbursed employee business expenses are deductible only as a miscellaneous deduction and only to the extent that the individual’s total miscellaneous itemized deductions (including employee business expenses) exceed two percent of adjusted gross income.64

Taxpayers who itemize deductions may claim a deduction for contributions to qualified professional development organizations. The law does not specify how such contributions may exceed 50 percent of adjusted gross income. Other limits apply.

H2770

CONGRESSIONAL RECORD—HOUSE

May 25, 2001

SENATE AMENDMENT

The Senate amendment provides that contributions of book inventory to certain educational organizations are entitled to the present-law deduction. Eligible educational organizations are (1) educational organizations that normally maintain a regular faculty and curriculum and normally have a regularly enrolled body of students in attendance at the place where its educational activities are regularly carried on; (2) charities organized primarily for purposes of supporting elementary and secondary education; and (3) charities organized primarily to make books available to the general public at no cost or to operate a library or reading room and regularly carry on activities associated with meals, lodging, insurance, transportation, and similar personal, living, or family expenses are not eligible for the credit. The expenses of providing instruction, sports, games, or hobbies are not qualified tuition and related expenses unless this education is part of the student’s degree program.

Qualified tuition and related expenses generally include only out-of-pocket expenses. The qualified tuition and related expenses do not include expenses covered by employer-provided educational assistance and scholarships that are not required to be included in the gross income of the individual claiming the credit. Thus, total qualified tuition and related expenses are reduced by any scholarship or fellowship grants included from gross income under section 117 and any other tax-free educational benefits received by the student (or the taxpayer claiming the credit) during the taxable year.

LIFETIME LEARNING CREDIT

Under present law, individual taxpayers are allowed to claim a nonrefundable credit, the “HOPE” credit, against Federal income taxes of up to $1,500 per student per year for qualified tuition and related expenses paid for the education of an eligible student in attendance at a qualified elementary or secondary school in a degree or certificate program. The HOPE credit rate is 100 percent of the first $1,000 of qualified tuition and related expenses and 50 percent of the next $1,000 of qualified tuition and related expenses.42

The qualified tuition and related expenses must be incurred on behalf of the taxpayer’s spouse, or a dependent of the taxpayer.46 The HOPE credit is available with respect to an individual student in attendance at the place where its educational activities are regularly carried on; (2) meets the express require-

SECONDARY SCHOOL TEACHERS (SEC. 442 AND SECTION 223 OF THE CODE)

The conference agreement does not include the Senate amendment provision.

PRESENT LAW

Deduction for education expenses

Under present law, an individual taxpayer generally may not deduct the education and training expenses of the taxpayer or the taxpayer’s dependents. However, a deduction for education expenses generally is allowed under section 112 of the Code (the Code) to the extent that such expenses are allowable with respect to an individual student in attendance at a school described in section 117 and are allowed for qualified professional development expenses paid for taxable years beginning after 2001, the HOPE credit is computed on a per student basis.

The conference agreement does not include

CREDIT FOR CLASSROOM MATERIALS (SEC. 443 OF THE SENATE AMENDMENT AND NEW SEC. 308 OF THE CODE)

PRESENT LAW

Unreimbursed employee business expenses are deductible only as a miscellaneous deduction and only to the extent that the individual’s total miscellaneous itemized deductions (including employee business expenses) exceed two percent of adjusted gross income.

Taxpayers who itemize deductions may claim a deduction for contributions to qualified professional development organizations. The law does not specify how such contributions may exceed 50 percent of adjusted gross income. Other limits apply.

64Thus, an eligible student who incurs $1,000 of qualified tuition and related expenses is eligible (subject to the AGI phase-out) for a $1,000 HOPE credit. If an eligible student incurs $2,000 of qualified tuition and related expenses, then he or she is eligible for a $1,500 HOPE credit.

63The HOPE credit may not be claimed against a taxpayer’s alternative minimum tax liability.

46Local education agency is as defined in section 14101 of the Elementary and Secondary Education Act of 1965.

65One-day or short-term workshops and conferences do not satisfy this requirement. This requirement does not apply to an activity that is one component described in a long-term comprehensive professional development plan established by the individual and his or her supervisor based on an assessment of the needs of the individual, the individual’s related expenses, and the knowledge and skills involved.

42Thus, an eligible student who incurs $1,000 of qualified tuition and related expenses is eligible (subject to the AGI phase-out) for a $1,000 HOPE credit. If an eligible student incurs $2,000 of qualified tuition and related expenses, then he or she is eligible for a $1,500 HOPE credit.
in the case of contributions to certain organizations and certain property.

An individual’s otherwise allowable itemized deductions may be further limited by the overall limitation on itemized deductions, which reduces itemized deductions for taxpayers with adjusted gross income in excess of $132,950 (for 2001).

Depending on the particular facts and circumstances, a contribution by a teacher to the school and which he or she is employed may be deductible as an unreimbursed employee business expense or as a charitable contribution.

**HOUSE BILL**

No provision.

**SENATE AMENDMENT**

The Senate amendment provides a non-refundable personal credit equal to 50 percent of the qualified elementary and secondary education expenses paid or incurred by an eligible educator during the taxable year. The maximum credit cannot exceed $250 in any year. An eligible educators are kindergarten through 12th grade teachers, instructors, counselors, principals, or aides who work in an elementary or secondary school for at least 900 hours during the school year. Qualified elementary and secondary education expenses are expenses for books, supplies (other than nonathletic supplies for courses of instruction in health or physical education), computer equipment (including related software and services) and other equipment, and supplementary materials used by an eligible educator in the classroom.

The credit may not exceed the excess (if any) of (1) the taxpayer’s regular tax for the taxable year, reduced by the sum of certain other allowable credits over (2) the taxpayer’s tentative minimum tax for the taxable year.

No deduction is allowed for any expense for which a credit is allowed under the provision.

A taxpayer may elect not to have the credit apply.

**Effective date.**—The provision is effective for taxable years beginning after December 31, 2001, and expires on December 31, 2005.

**CONFERENCE AGREEMENT**

The conference agreement does not include the Senate amendment provision.

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47 Elementary and secondary schools are defined by reference to section 14101 of the Elementary and Secondary Education Act of 1965.