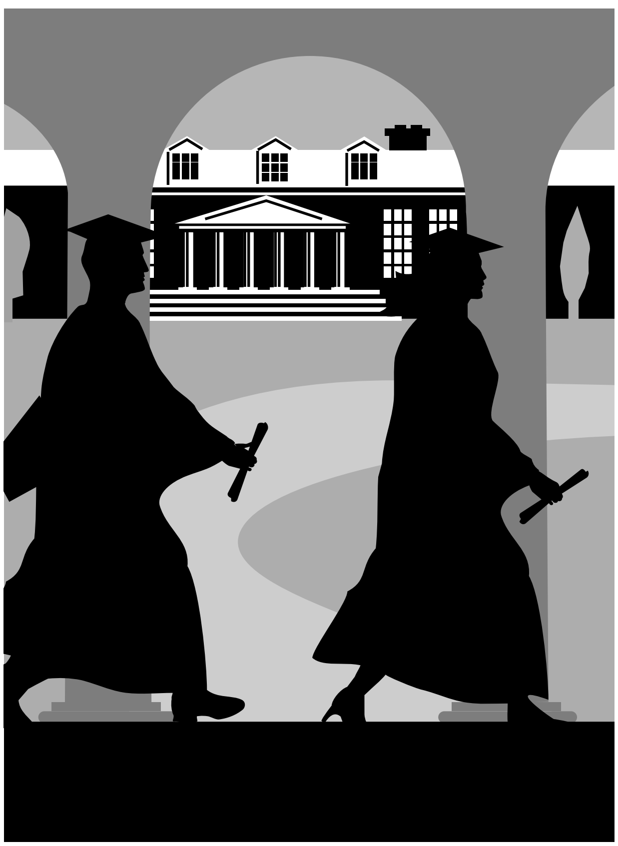
Department of the Treasury
Internal Revenue Service

Publication 970
Cat. No. 25221V

Tax Benefits for Higher Education

For use in preparing
1999 Returns



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See *How To Get More Information* in this publication.

Contents

Important Changes

Tax from recapture of education credits. You may owe this tax if you claimed an education credit on your 1998 tax return and, in 1999, you, your spouse if filing jointly, or your dependent received a refund of qualified tuition and related expenses, or tax-free educational assistance. See *Recapture of credit* under *No double benefit allowed*.

Photographs of missing children. The Internal Revenue Service is a proud partner with the National Center for Missing and Exploited Children. Photographs of missing children selected by the Center may appear in this publication on pages that would otherwise be blank. You can help bring these children home by looking at the photographs and calling **1–800–THE–LOST (1–800–843–5678)** if you recognize a child.

Introduction

This publication explains the tax benefits for persons who are saving for or paying higher education costs for themselves and members of their families. It covers the following topics.

- The Hope credit and the lifetime learning credit.
- Education individual retirement accounts (education IRAs).

- Withdrawals from traditional or Roth IRAs for the costs of higher education.
- Interest paid on certain student loans.
- The cancellation of certain student loans.
- Qualified state tuition programs.
- Savings bond interest used to pay the costs of higher education.
- Employer-provided educational assistance benefits.

Table 1 gives you a general comparison of some features of the different benefits. You may find it helpful in determining the benefits for which you are eligible.

This publication does not cover the itemized deduction you may be able to claim for work-related educational expenses. Information on that deduction can be found in Publication 508, *Tax Benefits for Work-Related Education.* This publication also does not cover scholarships that you may be able to exclude from your income. Information on scholarships can be found in Publication 520, *Scholarships and Fellowships.*

TIP *You may be able to reduce the amount of your federal income tax withholding throughout the year based on your estimated tax benefits for higher education. After you figure the amount of your estimated 2000 income, exclusions, deductions, and credit(s), see Publication 919,* How Do I Adjust My Tax Withholding?

Caution. *You should check your withholding again during the year if there are changes to your personal or financial situation that would affect your expected 2000 tax liability, including your allowable higher education tax benefits.*

Useful Items

You may want to see:

Publication

- ☐ **508** Tax Benefits for Work-Related Education
- ☐ **520** Scholarships and Fellowships
- ☐ **525** Taxable and Nontaxable Income
- ☐ **550** Investment Income and Expenses
- ☐ **590** Individual Retirement Arrangements (IRAs) (Including Roth IRAs and Education IRAs)

Form (and Instructions)

- ☐ **8815** Exclusion of Interest From Series EE and I U.S. Savings Bonds Issued After 1989
- ☐ **8863** Education Credits (Hope and Lifetime Learning Credits)

See *How To Get More Information,* near the end of this publication, for information about getting these publications and forms.

Education Tax Credits

The following two tax credits are available to persons who pay higher education costs.

- The Hope credit.
- The lifetime learning credit.

Rules that apply to both credits are explained first, followed by explanations of rules that apply to each credit, choosing which credit to claim, and how to claim your credits. The last section includes an illustrated Form 8863.

CAUTION *If a student receives a tax-free withdrawal from an education IRA in a particular tax year, none of that student's expenses can be used as the basis of a higher education credit for that tax year. However, the student can waive the tax-free treatment. See* Education IRA*, later.*

Rules That Apply to Both Credits

The amount of each credit is determined by the amount you pay for qualified tuition and related expenses for students and the amount of your modified adjusted gross income. Education credits are subtracted from your tax but they are nonrefundable. This means if the credits are more than your tax, the excess is not refunded to you.

CAUTION *If you are married filing separately, you cannot claim the higher education credits.*

What expenses qualify. The credits are based on qualified tuition and related expenses you pay for yourself, your spouse, or a dependent for whom you claim an exemption on your tax return. The credits are allowed for qualified tuition and related expenses paid for an academic period beginning in the same year as the year the payment is made (but see *Prepaid expenses*, later).

In general, qualified tuition and related expenses are tuition and fees required for enrollment or attendance at an eligible educational institution. Student-activity fees and fees for course-related books, supplies, and equipment are included in qualified tuition and related expenses ***only if*** the fees must be paid ***to the institution*** as a condition of enrollment or attendance.

Prepaid expenses. If you pay qualified tuition and related expenses for an academic period that begins in the first three months of the following year, you can use the prepaid amount in figuring your credit.

For example, if you paid $2,000 in December 1999 for qualified tuition for the winter 2000 semester beginning in January 2000, you can use that $2,000 in figuring your 1999 credit.

Payments with borrowed funds. You claim an education credit for the qualified tuition and related expenses paid with the proceeds of a loan. The credit is claimed in the year in which the expenses are paid, not in the year in which the loan is repaid.

Table 1. **Highlights of Tax Benefits for Higher Education**

Do not rely on this chart alone. It provides only general highlights of some of the differences among the benefits covered in this publication. See the text for definitions of terms and for more complete explanations.

Caution: *No double benefits are allowed. See the footnotes.*

	Hope credit (Education credit)	**Lifetime learning credit** (Education credit)	**Education IRA**[1]	**Traditional and Roth IRAs**[1]	**Interest Paid on Student Loans**	**Qualified State Tuition Programs**	**Qualified U.S. Savings Bonds**[1]	**Employer's Educational Assistance Program**[1]
What is your benefit?[2]	Tax credit (nonrefundable)		Withdrawals are tax free	No 10% additional tax on early withdrawal	Deduction to arrive at adjusted gross income	Prepay future tuition expenses	Interest is excludable from income	Employer benefits are excludable from income
What is the annual limit?	Up to $1,500 per student	Up to $1,000 per family	$500 contribution per child under 18	Amount of qualifying expenses	1999: $1,500 2000: $2,000 2001: $2,500	None	Amount of qualifying expenses	$5,250
What expenses qualify besides tuition and required enrollment fees?[2]	N/A		Books, supplies, & equipment; Room and board if at least half-time attendance; Payments to qualified state tuition program	Books, supplies, & equipment; Room & board if at least half-time attendance	Books, supplies, & equipment; Room & board; Transportation; Other necessary expenses	Books, supplies, & equipment; Room & board if at least half-time attendance	Payments to qualified state tuition programs; Payments to education IRAs	Books, supplies, & equipment
What education qualifies?	1st 2 years of undergraduate	All undergraduate and graduate levels						Undergraduate level
What other conditions apply?	Can be claimed only for 2 years; Must be enrolled at least half-time in a degree program	Applies to expenses ***paid*** and ***for school attendance*** after June 30, 1998	Contributions not deductible; Cannot also contribute to qualified state tuition program ***or*** claim an education credit; Must withdraw assets at age 30	Must receive entire balance or begin receiving withdrawals by April 1 of year following year in which age 70½ is reached	Applies to the 1st 60 months' interest; Must be enrolled at least half-time in a degree program	Tax-deferred earnings are taxed to beneficiary when withdrawn	Applies only to qualified series EE bonds issued after 1989 or series I bonds	Cannot also claim an education credit; Expires for courses beginning after December 31, 2001
At what income range do benefits phase out?	$40,000–$50,000 $80,000–$100,000 for joint returns		$95,000–$110,000; $150,000–$160,000 for joint returns	N/A	$40,000–$55,000; $60,000–$75,000 for joint returns	N/A	1999: $53,100–$68,100; $79,650–$109,650 for joint returns	N/A

[1] Any nontaxable withdrawal is limited to the amount that does not exceed qualifying educational expenses.

[2] You must generally reduce qualifying educational expenses by any tax-free income. You generally cannot use the same educational expense for figuring more than one benefit.

What expenses do not qualify. Qualified tuition and related expenses do not include the cost of insurance, medical expenses (including student health fees), room and board, transportation or similar personal, living or family expenses, even if the fee must be paid to the institution as a condition of enrollment or attendance.

Qualified tuition and related expenses generally do not include expenses that relate to any course of instruction or other education that involves sports, games, or hobbies, or any noncredit course. However, if the course of instruction or other education is part of the student's degree program or, in the case of the lifetime learning credit, is taken by the student to acquire or improve job skills, these expenses can qualify.

Dependent for whom you claim an exemption. You claim an exemption for a dependent if you list that person in the *Exemptions* section of your tax return.

Eligible educational institution. An eligible educational institution is any college, university, vocational school, or other postsecondary educational institution eligible to participate in a student aid program administered by the Department of Education. It includes virtually all accredited, public, nonprofit, and proprietary (privately owned profit-making) postsecondary institutions. The educational institution should be able to tell you if it is an eligible educational institution.

Academic period. An academic period includes a semester, trimester, quarter, or other period of study (such as a summer school session) as reasonably determined by an educational institution.

No double benefit allowed. If you take a deduction for higher education expenses on your tax return, you cannot claim a credit for those same expenses.

Adjustments to qualified expenses. If you pay higher education expenses with certain ***tax-free*** funds, you cannot claim a credit for those amounts. You must reduce the qualified expenses by the amount of any tax-free educational assistance. Tax-free educational assistance could include scholarships, Pell grants, employer-provided educational assistance, veterans' educational assistance, and any other nontaxable payments (other than gifts, bequests, or inheritances) received for educational expenses. Do not reduce the qualified expenses by amounts paid with the student's earnings, loans, gifts, inheritances, and personal savings. Also, do not reduce the qualified expenses by any scholarship reported as income on the student's return or any scholarship which, by its terms, cannot be applied to qualified tuition and related expenses.

Refunds. Qualified tuition and related expenses do not include expenses that are refunded. If you receive a refund in the same year in which you paid the expenses, or in the following year, but before you file your tax return for the year you paid them, simply reduce the amount of the expenses by the amount of the refund received. If you receive the refund after you file your tax return, see *Recapture of credit*, next.

Recapture of credit. If, after you file your tax return, you receive tax-free educational assistance for, or a refund of, an expense you used to figure a higher education credit on that return, you may have to recapture all or part of the credit. You must refigure your education credits as if the assistance or refund was received in the year the expenses were paid. Include the difference, if any, on your return for the year in which the assistance or refund was received. Include it on line 40 of your Form 1040 (line 25 of Form 1040A). Next to the line, enter the amount and "ECR."

Who can claim the credit. If there are higher education costs for your dependent child, either you or your child, but not both of you, can claim a credit for a particular year. If you claim an exemption for your child on your tax return, only you can claim a credit. If you do not claim an exemption for your child on your tax return, only your child can claim a credit.

Expenses paid by others. If someone other than you, your spouse, or your dependent (such as a relative or former spouse) makes a payment directly to an eligible educational institution to pay for a student's qualified tuition and related expenses, the student is treated as receiving the payment from the other person. The student is treated as paying the qualified tuition and related expenses to the institution.

Example. Ms. Allen makes a payment directly to an eligible educational institution in 1999 for her grandson's qualified tuition and related expenses. For purposes of claiming an education credit, the grandson is treated as receiving the money from Ms. Allen and, in turn, paying his qualified tuition and related expenses.

Expenses paid by dependent. If you claim an exemption for your child on your tax return, treat any expenses paid by your child as if you had paid them. Include these expenses when figuring the amount of your Hope or lifetime learning credit.

TIP *Qualified tuition and related expenses paid directly to an eligible educational institution for your dependent under a court-approved divorce decree are treated as paid by your dependent.*

Income Phaseout

Your education credits are phased out (gradually reduced) if your modified adjusted gross income is between $40,000 and $50,000 ($80,000 and $100,000 in the case of a joint return).

CAUTION *You cannot claim* **any** *higher education credits if your modified adjusted gross income is $50,000 or more ($100,000 or more in the case of a joint return).*

Modified adjusted gross income. For most taxpayers, modified adjusted gross income will be their adjusted gross income (AGI) as figured on their federal income tax return. However, you must make adjustments to your AGI if you excluded income earned abroad or from certain U.S. territories or possessions. If this applies to you, increase your AGI by the following amounts you excluded from your income.

1) Foreign earned income of U.S. citizens or residents living abroad.
2) Housing costs of U.S. citizens or residents living abroad.
3) Income from sources within Puerto Rico, Guam, American Samoa, or the Northern Mariana Islands.

How the phaseout works. The phaseout (reduction) works on a sliding scale. The higher your modified adjusted gross income, the more your credits are reduced. You figure the reduction, if any, in Part III of Form 8863.

Hope Credit

You may be able to claim a Hope credit of up to $1,500 for qualified tuition and related expenses paid for ***each*** eligible student. You can take into account expenses paid in 1999 for academic periods beginning after December 31, 1998, and before April 1, 2000. The credit can be claimed for ***only 2 years*** for each eligible student.

Eligible student for the Hope credit. For purposes of the Hope credit, an eligible student is a student who meets all of the following requirements.

1) Has not ***completed the first 2 years*** of postsecondary education (generally, the freshman and sophomore years of college) as of the beginning of the year.
2) Is enrolled in a program that leads to a degree, certificate, or other recognized educational credential for at least one academic period beginning during the year.
3) Is taking at least ***half of the normal full-time work load*** for his or her course of study for at least one academic period beginning during the calendar year.
4) Is free of any federal or state felony conviction for possessing or distributing a controlled substance as of the end of the year.

Completion of first 2 years. A student awarded 2 years of academic credit for postsecondary work completed prior to the beginning of the year has completed the first 2 years of postsecondary education.

Any academic credit awarded solely on the basis of the student's performance on proficiency examinations is disregarded in determining whether the student has completed 2 years of postsecondary education.

Half of normal full-time workload. The standard for what is half of the normal full-time work load is determined by each eligible educational institution. However, the standard may not be lower than standards for half-time established by the Department of Education under the Higher Education Act of 1965.

Amount of credit. The amount of the Hope credit is 100% of the first $1,000 ***plus*** 50% of the next $1,000 of qualified tuition and related expenses you pay for each eligible student. The maximum amount of Hope credit you can claim in 1999 is $1,500 times the number of eligible students. You can claim the full $1,500 for each eligible student for whom you pay at least $2,000 for qualified expenses. However, the credit may be reduced based on your modified adjusted gross income. See *Income Phaseout,* earlier.

Example. Jon and Karen are married and file a joint tax return. For 1999, they claim an exemption for their dependent daughter on their tax return and their modified adjusted gross income is $70,000. Their daughter is in her sophomore (second) year of studies at the local university and Jon and Karen pay $4,300 in 1999 for her tuition costs.

Jon and Karen, their daughter, and the local university meet all of the requirements for the Hope credit. Jon and Karen can claim a $1,500 Hope credit in 1999. This is the maximum amount allowed for 1999.

How to figure the Hope credit. The Hope credit is figured in Parts I and III of Form 8863. An illustrated example using Form 8863 appears later.

Lifetime Learning Credit

You may be able to claim a lifetime learning credit of up to $1,000 for qualified tuition and related expenses paid for ***all*** students enrolled in eligible educational institutions. You can take into account expenses paid in 1999 for academic periods beginning after December 31, 1998, and before April 1, 2000.

The lifetime learning credit is different than the Hope credit in the following ways.

1) The lifetime learning credit is not based on the student's work load. It is allowed for one or more courses.
2) The lifetime learning credit is not limited to students in the first 2 years of postsecondary education.
3) Expenses for graduate-level degree work are eligible.
4) Expenses related to a course of instruction or other education that involves sports, games, hobbies, or other noncredit courses are eligible ***if*** they are part of a course of instruction to acquire or improve job skills.
5) There is no limit on the number of years for which the lifetime learning credit can be claimed for each student.
6) The amount you can claim as a lifetime learning credit does not vary (increase) based on the number of students for whom you pay qualified expenses.

Amount of credit. The amount of the lifetime learning credit is 20% of the first $5,000 of qualified tuition and related expenses you pay for all students in the family. The maximum amount of lifetime learning credit you can claim for 1999 is $1,000 (20% × $5,000). However, that amount may be reduced based on your modified adjusted gross income. See *Income Phaseout,* earlier.

Example. Bruce and Toni are married and file a joint tax return. For 1999, their modified adjusted gross income is $50,000. Toni is attending the community college (an eligible educational institution) to earn credits towards an associate's degree in nursing; she already has a bachelor's degree in history and wants to become a nurse. In August 1999, Toni paid $2,000 for her fall 1999 semester. Bruce and Toni can claim a $400 (20% × $2,000) lifetime learning credit on their 1999 joint tax return.

How to figure the lifetime learning credit. The lifetime learning credit is figured in Parts II and III of Form 8863. An illustrated example using Form 8863 appears later.

Choosing Which Credit To Claim

For each student, you can elect for any tax year only ***one*** of the credits ***or*** a tax-free withdrawal from an education IRA. (See *Education IRA*, later, for more information.) For example, if you elect to take the Hope credit for a child on your 1999 tax return, you cannot, for that same child, also claim the lifetime learning credit for 1999 or take a tax-free withdrawal from an education IRA for 1999.

Lifetime learning credit after Hope credit. You can claim the Hope credit for the first 2 years of a student's postsecondary education and claim the lifetime learning credit for that same student in later tax years.

More than one student. If you pay qualified expenses for more than one student in the same year, you can choose to take credits on a per-student, per-year basis. This means that, for example, you can claim the Hope credit for one student and the lifetime learning credit for another student in the same tax year.

How To Claim the Credits

You elect to claim education credits and you figure their amount by completing **Form 8863**. Use Part I for the Hope credit and Part II for the lifetime learning credit. In both parts, you enter the student's name and taxpayer identification number (usually a social security number) and the amount of qualified expenses paid in 1999. You then complete Part III to compute the amount to enter on line 44 of Form 1040 or line 29 of Form 1040A. Attach the completed Form 8863 to your return.

An eligible educational institution (such as a college or university) that receives payment of qualified tuition and related expenses generally must issue **Form 1098–T**, *Tuition Payments Statement,* to each student by February 1, 2000. The information on Form 1098–T will help you determine whether you can claim an education tax credit for 1999. The following information should be included on the 1999 form.

1) The name, address, and taxpayer identification number of the educational institution.
2) The name, address, and taxpayer identification number of the student.
3) Whether the student was enrolled for at least half of the full-time academic workload.
4) Whether the student was enrolled exclusively in a graduate-level program.

The eligible educational institution may ask for a completed **Form W–9S**, *Request for Student's or Borrower's Social Security Number and Certification,* or similar statement, to obtain the information needed to complete (2) above.

Illustrated Example

Dave and Valerie are married and file a joint tax return. For 1999, they claim exemptions for their two dependent children on their tax return, and their modified adjusted gross income is $72,000. Their son, Sean, will receive his bachelor's degree in psychology from the state college in May 2000. Their daughter, Corey, enrolled full-time at that same college in August 1998 to begin working on her bachelor's degree in physical education. In December 1998, Dave and Valerie paid $2,000 for each child's tuition for the winter 1999 semester. In July 1999, they paid $2,200 in tuition costs for each of them for the fall 1999 semester.

Dave and Valerie, their children, and the college meet all of the requirements for the higher education credits. Because Sean is beyond the second (sophomore) year of his postsecondary education, his expenses do not qualify for the Hope credit. But, amounts paid for Sean's expenses in 1999 for academic periods beginning after 1998 and before April 1, 2000, qualify for the lifetime learning credit. Corey is in her first two (freshman and sophomore) years of postsecondary education and expenses paid for her in 1999 for academic periods beginning after 1998 and before April 1, 2000, qualify for the Hope credit.

Dave and Valerie figure their total higher education credits for 1999, $1,940, as shown in the completed Form 8863. They can claim the full amount because their modified adjusted gross income is not more than $80,000. They carry the amount from line 18 of Form 8863 to line 44 of Form 1040, and they attach the Form 8863 to their return.

Individual Retirement Arrangement (IRA) Provisions

You may be able to establish an education individual retirement account (education IRA or Ed IRA) to finance a child's qualified higher education expenses. In addition, you may be able to take withdrawals from other IRAs without paying the 10% additional tax on early withdrawals if you pay for qualified higher education expenses. Publication 590 has detailed information on all IRA accounts.

Education IRA

You may be able to contribute up to $500 cash each year to an education IRA for a child under age 18. Contributions to an education IRA are not deductible, but amounts deposited in the account grow tax free until withdrawn.

Any individual (including the child) can contribute to a child's education IRA if his or her income is below a certain amount. There is no limit on the number of education IRAs that can be established designating a child

Form **8863**

Department of the Treasury
Internal Revenue Service

Education Credits (Hope and Lifetime Learning Credits)

► See instructions on pages 3 and 4. ► Attach to Form 1040 or Form 1040A.

OMB No. 1545-1618

1999

Attachment Sequence No. **51**

Name(s) shown on return: Dave and Valerie Jones

Your social security number: 987 00 6543

Part I **Hope Credit**

1	(a) Student's name First, Last	(b) Student's social security number	(c) Qualified expenses (but **do not** enter more than $2,000 for each student). See instructions	(d) Enter the **smaller** of the amount in column (c) or $1,000	(e) Subtract column (d) from column (c)	(f) Enter one-half of the amount in column (e)
	Corey, Jones	137 00 9642	2,000	1,000	1,000	500
2	Add the amounts in columns (d) and (f) **2**			1,000		500
3	Add the amounts on line 2, columns (d) and (f) . . . . ► **3**					1,500

Part II **Lifetime Learning Credit**

4	(a) Student's name First / Last		(b) Student's social security number	(c) Qualified expenses. See instructions
Caution: *You cannot take the Hope credit and the lifetime learning credit for the same student.*	Sean	Jones	246 00 9731	2,200

5	Add the amounts on line 4, column (c), and enter the total	**5**	2,200
6	Enter the **smaller** of line 5 or $5,000	**6**	2,200
7	Multiply line 6 by 20% (.20) . . . . ►	**7**	440

Part III **Allowable Education Credits**

8	Add lines 3 and 7.			**8**	1,940
9	Enter: $100,000 if married filing jointly; $50,000 if single, head of household, or qualifying widow(er)	**9**	100,000		
10	Enter the amount from Form 1040, line 34 (or Form 1040A, line 19)*	**10**	72,000		
11	Subtract line 10 from line 9. If line 10 is greater than or equal to line 9, **stop;** you cannot take any education credits	**11**	28,000		
12	Enter: $20,000 if married filing jointly; $10,000 if single, head of household, or qualifying widow(er)	**12**	20,000		
13	If line 11 is greater than or equal to line 12, enter the amount from line 8 on line 14 and go to line 15. If line 11 is less than line 12, divide line 11 by line 12. Enter the result as a decimal (rounded to at least three places)			**13**	× .
14	Multiply line 8 by line 13 . . . . ►			**14**	1,940
15	Enter your tax from Form 1040, line 40 (or Form 1040A, line 25)			**15**	9,475
16	Enter the total, if any, of your credits from Form 1040, lines 41 and 42 (or from Form 1040A, lines 26 and 27)			**16**	0
17	Subtract line 16 from line 15. If line 16 is greater than or equal to line 15, **stop;** you cannot take any education credits			**17**	9,475
18	**Education credits.** Enter the **smaller** of line 14 or line 17 here and on Form 1040, line 44 (or Form 1040A, line 29) . . . . ►			**18**	1,940

*See Pub. 970 for the amount to enter if you are filing Form 2555, 2555-EZ, or 4563, or you are excluding income from Puerto Rico.

as the beneficiary. However, total contributions for the child during any tax year cannot be more than $500. See *Contributions*, later.

If, for a year, withdrawals from an account are not more than a child's qualified higher education expenses at an eligible educational institution, the child will not owe tax on the withdrawals. See *Withdrawals,* later.

Education IRAs At a Glance

Do not rely on this chart alone. It provides only general highlights. See the text for definitions of terms in bold type and for more complete explanations.

Question	Answer
What is an **education IRA?**	An IRA that is set up to pay the **qualified higher education expenses** of a designated beneficiary.
Where can it be established?	It can be opened in the United States at any bank or other IRS-approved entity that offers education IRAs.
Who can an education IRA be set up for?	Any child who is under age 18.
Who can contribute to an education IRA?	Generally, any individual (including the beneficiary) whose **modified adjusted gross income** for the year is less than $110,000 ($160,000 in the case of a joint return).

What Is an Education IRA?

An education IRA is a trust or custodial account created only for the purpose of paying the qualified higher education expenses (defined later) of the designated beneficiary of the account. When the account is established, the designated beneficiary must be a child under age 18. To be treated as an education IRA, the account must be designated as an education IRA when it is created.

Account requirements. The document creating and governing the account must be in writing and must satisfy the following requirements.

1) The account must be created or organized in the United States.
2) The trustee or custodian must be a bank or an entity approved by the IRS.
3) The document must provide that the trustee or custodian can only accept a contribution that meets all of the following conditions.
   a) Is in cash.
   b) Is made before the beneficiary reaches age 18.
   c) Would not result in total contributions for the tax year (not including rollover contributions) being more than $500.
4) Money in the account cannot be invested in life insurance contracts.
5) Money in the account cannot be combined with other property except in a common trust fund or common investment fund.
6) The balance in the account generally must be withdrawn within 30 days after the earlier of the following events.
   a) The beneficiary reaches age 30.
   b) The beneficiary's death.

   See *When assets must be withdrawn*, later.

Designated beneficiary. The individual named in the document creating the trust or custodial account to receive the benefit of the funds in the account is the designated beneficiary.

Qualified higher education expenses. These are expenses required for the enrollment or attendance of the designated beneficiary at an eligible educational institution. They include the following items.

1) Tuition and fees.
2) The cost of books, supplies, and equipment.
3) Amounts contributed to a qualified state tuition program. (See *State Tuition Programs,* later.)
4) The cost of room and board if the designated beneficiary is at least a half-time student at an eligible educational institution.

The term ***eligible educational institution*** was defined earlier under *Rules That Apply to Both Credits* for the education credits. A student is enrolled “at least half-time” if he or she is enrolled for at least half the full-time academic work load for the course of study the student is pursuing as determined under the standards of the school where the student is enrolled.

For purposes of item (4) above, the expense for room and board is limited to one of the following two amounts.

1) The school's posted room and board charge for students living on campus.
2) $2,500 each year for students living off campus and not at home.

Contributions

Any individual (including the child for whose benefit the account is established) can contribute to a child's education IRA if the individual's ***modified adjusted gross income*** (defined earlier under *Income Phaseout* for the education credits) for the tax year is less than $110,000 ($160,000 in the case of a joint return). Contributions must be in cash, and you cannot contribute to an education IRA after the beneficiary reaches age 18.

Contributions can be made to one or several education IRAs for the same child provided that the total contributions are not more than the contribution limit (defined later) for a tax year.

Education IRA Contributions At a Glance

Do not rely on this chart alone. It provides only general highlights. See the text for definitions of terms in bold type and for more complete explanations.

Question	Answer
Are contributions deductible?	No.
Why should someone contribute to an education IRA?	Earnings on the account grow tax free until withdrawn.
What is the **contribution limit** per child?	$500 each year for each child.
What if more than one education IRA has been opened for the same child?	The annual contribution limit is $500 for each child, no matter how many education IRAs are set up for that child.
What if more than one individual makes contributions for the same child?	The contribution limit is $500 per child, no matter how many individuals contribute.
Can contributions other than cash be made to an education IRA?	No.
When must contributions stop?	No contributions can be made to a child's education IRA after he or she reaches age 18.

No contributions can be made to an education IRA on behalf of a child if any amount is contributed during the tax year to a **qualified state tuition program** *on behalf of the same child.*

Contribution limits. There are two yearly limits, one on the total amount that can be contributed for each designated beneficiary (child) and one on the amount that any individual can contribute for any one child for a year.

Limit for each child. The total of all contributions to all education IRAs set up for the benefit of any one designated beneficiary (child) cannot be more than $500 for a year. This includes contributions (other than rollovers) to all the child's education IRAs from all sources. Rollovers are discussed under *Rollovers and Other Tranfers*, later.

Limit for each contributor. You can contribute up to $500 for each child for any year. This is the most you can contribute for the benefit of any one child for any year, regardless of the number of education IRAs set up for the child. However, this limit may be reduced as explained next.

If your ***modified adjusted gross income*** (defined earlier) is between $95,000 and $110,000 (between $150,000 and $160,000 if filing a joint return), the $500 limit for each child is gradually reduced (see *Figuring the limit*, next). If your modified adjusted gross income is $110,000 or more ($160,000 or more if filing a joint return), you cannot contribute to anyone's education IRA.

Figuring the limit. To figure the limit on the amount you can contribute for each child, multiply $500 by a fraction. The numerator (top number) is your modified adjusted gross income minus $95,000 ($150,000 if filing a joint return). The denominator (bottom number) is $15,000 ($10,000 if filing a joint return). Subtract the result from $500. This is the amount you can contribute for each child.

Example. Paul, a single individual, had modified adjusted gross income of $96,500 for the year. For Paul, the maximum contribution for each child is reduced to $450, figured as follows.

1) $96,500 – $95,000 = $1,500

2) $1,500 ÷ $15,000 = 10%

3) 10% × $500 = $50

4) $500 – $50 = $450

Additional tax on excess contributions. A 6% excise tax applies each year to excess contributions that are in an education IRA at the end of the year. Excess contributions are the ***total*** of the following three amounts.

1) Contributions to any child's education IRA for the year that are more than $500 (or, if less, the total of each contributor's limit for the year, as discussed earlier).

2) All contributions to a child's education IRA for the year if any amount is also contributed during the year to a qualified state tuition program on behalf of the same child. However, amounts withdrawn from the education IRA to be contributed to the qualified state tuition program are not excess contributions.

3) Excess contributions for the preceding year, reduced by the total of the following two amounts:

   a) Withdrawals (other than those rolled over as discussed later) made during the year, and

   b) The contribution limit for the current year minus the amount contributed for the current year.

Exceptions. The excise tax does not apply if the excess contributions (and any earnings on them) are withdrawn before the due date of the beneficiary's tax return (including extensions). If the beneficiary does not have to file a return, the tax does not apply if the excess contributions (and the earnings) are withdrawn by April 15 of the year following the year the contributions are made. The withdrawn earnings must be included in the beneficiary's income for the year in which the excess contribution is made.

The excise tax also does not apply to any rollover contribution.

Rollovers and Other Transfers

Assets can be rolled over from one education IRA to another. The designated beneficiary can be changed and the beneficiary's interest can be transferred to a spouse or former spouse because of divorce.

Rollovers. Any amount withdrawn from an education IRA and rolled over to another education IRA for the benefit of the same beneficiary or a member of the beneficiary's family is not taxable. A rollover to an education IRA of a family member is not taxable only if that family member is under age 30. An amount is rolled over if it is paid to another education IRA within 60 days after the date of the withdrawal.

Members of the beneficiary's family. The beneficiary's spouse and the following individuals (and their spouses) are members of the beneficiary's family.

- The beneficiary's child, grandchild, or stepchild.
- A brother, sister, half brother, half sister, stepbrother, or stepsister of the beneficiary.
- The father, mother, grandfather, grandmother, stepfather, or stepmother of the beneficiary.
- A brother or sister of the beneficiary's father or mother.
- A son or daughter of the beneficiary's brother or sister.
- The beneficiary's son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, or sister-in-law.

CAUTION *Only one rollover per education IRA is allowed during the 12-month period ending on the date of the payment or withdrawal.*

Changing the designated beneficiary. The designated beneficiary can be changed to a member of the beneficiary's family (defined earlier). There are no tax consequences if, at the time of the change, the new beneficiary is under age 30.

Transfer because of divorce. If a spouse or former spouse receives an education IRA under a divorce or separation instrument, it is not a taxable transfer. After the transfer, the spouse or former spouse treats the education IRA as his or her own.

Withdrawals

The designated beneficiary of an education IRA can take withdrawals at any time. Whether the withdrawals are tax free depends, in part, on whether the withdrawals are more than the amount of qualified higher education expenses (defined earlier) that the beneficiary has in the tax year.

Education IRA Withdrawals At a Glance

Do not rely on this chart alone. It provides only general highlights. See the text for definitions of terms in bold type and for more complete explanations.

Question	Answer
Is a withdrawal from an education IRA to pay for a designated beneficiary’s qualified higher education expenses tax free?	Generally, yes, to the extent the amount of the withdrawal is not more than the designated beneficiary’s qualified higher education expenses.
After the designated beneficiary completes his or her education at an **eligible educational institution,** may amounts remaining in the education IRA be withdrawn?	Yes. Amounts ***must*** be withdrawn when the designated beneficiary reaches age 30. Also, certain transfers to **members of the designated beneficiary’s family** are permitted.
Does the designated beneficiary need to be enrolled for a minimum number of courses to take a tax-free withdrawal?	No.

Withdrawals not more than expenses. Generally, withdrawals are tax free if they are not more than the beneficiary's qualified higher education expenses for the tax year.

Withdrawals more than expenses. Generally, a portion of the withdrawals is taxable to the beneficiary if the withdrawals are more than the beneficiary's qualified higher education expenses for the tax year.

The taxable portion is the amount of the withdrawal that represents earnings that have accumulated tax free in the account. Figure the taxable portion as shown in the following steps.

1) Multiply the amount withdrawn by a fraction. The numerator is the total contributions in the account and the denominator is the total balance in the account before the withdrawal(s).
2) Subtract the amount figured in (1) from the total amount withdrawn during the year. This is the amount of earnings included in the withdrawal(s).
3) Multiply the amount of earnings figured in (2) by a fraction. The numerator is the qualified higher education expenses paid during the year and the denominator is the total amount withdrawn during the year.

4) Subtract the amount figured in (3) from the amount figured in (2). This is the amount the beneficiary must include in income.

Example. You receive a $600 withdrawal from an education IRA to which $1,000 has been contributed. The balance in the IRA before the withdrawal was $1,200. You had $450 of qualified higher education expenses for the year. Using the steps above, you figure the taxable portion of your withdrawal as follows.

1) $600 × ($1,000 ÷ $1,200) = $500

2) $600 − $500 = $100

3) $100 × ($450 ÷ $600) = $75

4) $100 − $75 = $25

You must include $25 in income as withdrawn earnings not used for the expenses of higher education.

You cannot take a deduction or credit for any educational expenses that you use as the basis for a tax-free withdrawal from an education IRA. But see Waiver of tax-free treatment, *next.*

Waiver of tax-free treatment. The designated beneficiary can waive the tax-free treatment of the withdrawal and elect to pay any tax that would otherwise be owed on the withdrawal. The beneficiary or the beneficiary's parents may then be eligible to claim a Hope credit or lifetime learning credit for qualified higher education expenses paid in that tax year. (See *Education Tax Credits,* earlier, to determine if all of the requirements for those credits are met.)

Additional tax. Generally, if the beneficiary receives a taxable withdrawal, he or she also must pay a 10% additional tax on the amount included in income.

Exceptions. The 10% additional tax does not apply to withdrawals described in the following list.

1) Paid to a beneficiary (or to the estate of the designated beneficiary) on or after the death of the designated beneficiary.

2) Made because the designated beneficiary is disabled. A person is considered to be disabled if he or she shows proof that he or she cannot do any substantial gainful activity because of his or her physical or mental condition. A physician must determine that his or her condition can be expected to result in death or to be of long-continued and indefinite duration.

3) Made because the designated beneficiary received:

   a) A qualified scholarship excludable from gross income,

   b) An educational assistance allowance, or

   c) Payment for the designated beneficiary's educational expenses that is excludable from gross income under any law of the United States.

   The exception applies only to the extent the withdrawal is not more than the scholarship, allowance, or payment.

4) Included in income only because the beneficiary waived the tax-free treatment of the withdrawal (as explained earlier).

5) A return of an excess contribution (and any earnings on it) made before the due date of the beneficiary's tax return (including extensions). If the beneficiary does not have to file a return, the excess (and any earnings) must be withdrawn by April 15 of the year following the year of the contribution. The beneficiary must include in gross income for the year the contribution is made any income earned on the excess contribution.

When assets must be withdrawn. Any assets remaining in an education IRA must be withdrawn when either one of the following two events occurs.

1) The designated beneficiary reaches age 30. In this case, the designated beneficiary must withdraw the remaining assets within 30 days after he or she reaches age 30.

2) The designated beneficiary dies before reaching age 30. In this case, the remaining assets must generally be withdrawn within 30 days after the date of death.

The earnings that accumulated tax free in the account must be included in taxable income. You determine these earnings as shown in the following two steps.

1) Multiply the amount withdrawn by a fraction. The numerator is the total contributions in the account and the denominator is the total balance in the account before the withdrawal(s).

2) Subtract the amount figured in (1) from the total amount withdrawn during the year. The result is the amount of earnings included in the withdrawal. The beneficiary must include this amount in income.

Exception for transfer to surviving spouse or family member. If an education IRA is transferred to a surviving spouse or other family member as the result of the death of the designated beneficiary, the education IRA retains its status. (For this purpose, family member was defined earlier under *Rollovers.)* This means the spouse or other family member can treat the education IRA as his or her own. There are no tax consequences as a result of the transfer.

Withdrawals From Traditional or Roth IRAs

You can make withdrawals from your traditional or Roth IRA for qualified higher education expenses. A traditional IRA is an IRA that is not a Roth IRA, SIMPLE IRA, or education IRA. You will owe income tax on at least part of the amount withdrawn, but you will not have to pay the 10% additional tax on early withdrawals. (Generally, if you make withdrawals from your traditional or Roth IRA before you reach age 59½, you must pay a 10% additional tax on the early withdrawal.)

Withdrawals for higher education expenses. Part (or all) of any withdrawal may not be subject to the 10% additional tax on early withdrawals. The part not subject to the tax is generally the amount that is not more than the qualified higher education expenses (defined later) for the year for education furnished at an eligible educational institution (defined earlier under *Rules That Apply to Both Credits* for the education credits). The education must be for you, your spouse, or the children or grandchildren of you or your spouse.

When determining the amount of the withdrawal that is not subject to the 10% additional tax, ***include*** qualified higher education expenses paid with any of the following funds.

1) An individual's earnings.
2) A loan.
3) A gift.
4) An inheritance given to either the student or the individual making the withdrawal.
5) Personal savings (including savings from a qualified state tuition program).

Do ***not include*** expenses paid with any of the following funds.

1) Tax-free withdrawals from an education IRA.
2) Tax-free scholarships, such as a Pell grant.
3) Tax-free employer-provided educational assistance.
4) Any tax-free payment (other than a gift, bequest, or devise) due to enrollment at an eligible educational institution.

Qualified higher education expenses. Qualified higher education expenses are tuition, fees, books, supplies, and equipment required for the enrollment or attendance of a student at an eligible educational institution. In addition, if the individual is at least a half-time student, room and board are qualified higher education expenses.

Student Loans

You may be able to deduct interest you pay on a qualified student loan. This applies to loan interest payments due and paid after 1997. And, if a student loan is canceled, you may not have to include any amount in income.

Interest Deduction

You may be able to deduct interest you pay on a qualified student loan even if you took out the loan before 1999. Regardless of when you took out the loan, you can deduct only interest paid during the ***first 60 months*** that interest payments are required.

Example. You took out a qualified student loan in 1992. You made a payment on the loan every month, as required, beginning October 1, 1994. You can deduct the interest on your first nine payments for 1999. You cannot deduct the interest on any later payments because they are after the 60-month period (October 1, 1994 – September 30, 1999).

Your interest deduction for 1999 cannot be more than $1,500 and is subject to the limit described later.

Include as interest. Loan origination fees (other than fees for services) and capitalized interest are deductible as student loan interest if all other requirements are met.

Capitalized interest is accrued and unpaid interest on a qualified student loan that is capitalized by the lender and added to the outstanding principal balance of the loan.

Claiming the deduction. This deduction is an adjustment to income, so you can claim it even if you do not itemize deductions on Schedule A (Form 1040). Complete the worksheet in your form instructions and enter the allowable amount on line 24 of Form 1040 or line 16 of Form 1040A.

TIP *If you pay more than $600 in interest during the year to a single lender, you should receive a statement at the end of the year from the lender showing the amount of interest. That information will help you complete your tax forms.*

Persons not eligible. You cannot claim the deduction in any tax year in which:

1) Your filing status is married filing a separate return, or
2) You are a dependent for whom an exemption is claimed on the tax return of another taxpayer.

Qualified student loan. This is a loan you took out solely to pay qualified higher education expenses. The expenses must have been:

1) For you, your spouse, or a person who was your dependent when you took out the loan,
2) Paid or incurred within a reasonable time before or after you took out the loan, and
3) For education furnished during a period when the recipient of the education was an eligible student.

Qualified higher education expenses. These expenses are the costs of attending an eligible educational institution, including graduate school. Generally, these costs include tuition, fees, room and board, books, equipment, and other necessary expenses, such as transportation. But you must reduce these costs by the following items.

1) Nontaxable employer-provided educational assistance benefits.
2) Nontaxable withdrawals from an education IRA.
3) U.S. savings bond interest that is nontaxable because you paid qualified higher education expenses.
4) Qualified scholarships that are nontaxable.

5) Veterans' educational assistance benefits.

6) Any other nontaxable payments (other than gifts, bequests, or inheritances) received for educational expenses.

Eligible educational institution. The term eligible educational institution generally has the same meaning as defined earlier under *Rules That Apply to Both Credits* for the education credits. For purposes of the student loan interest deduction, the term also includes an institution conducting an internship or residency program leading to a degree or certificate from an institution of higher education, a hospital, or a health care facility that offers postgraduate training.

Eligible student. An eligible student is one who:

1) Is enrolled in a degree, certificate, or other program (including a program of study abroad that is approved for credit by the institution at which the student is enrolled) leading to a recognized educational credential at an eligible educational institution, and

2) Is carrying at least one-half the normal full-time work load for the course of study the student is pursuing.

Loan from related person. You cannot deduct interest on a loan you get from a related person. Related persons include your brothers and sisters, half brothers and half sisters, spouse, ancestors (parents, grandparents, etc.), and lineal descendants (children, grandchildren, etc.). Related persons also include certain corporations, partnerships, trusts, and exempt organizations.

Loan from employer plan. You cannot deduct interest on a loan made under a qualified employer plan or under a contract purchased under such a plan.

Refinanced loan. If you refinance a qualified student loan, the new loan can also be a qualified student loan. But refinancing a loan does not extend the 60-month period described earlier. The 60-month period is based on the original loan.

Maximum deduction. Your deduction for 1999 cannot be more than $1,500. This limit increases to $2,000 for 2000, and $2,500 for 2001 and later years.

Limit on deduction. Your deduction may be limited, depending on the amount of your modified adjusted gross income. This limit applies if your modified adjusted gross income is more than $40,000 ($60,000 in the case of a joint return).

If your modified adjusted gross income is $55,000 or more ($75,000 or more in the case of a joint return), you cannot claim a deduction.

Modified adjusted gross income. For purposes of this deduction, modified adjusted gross income means AGI figured on your income tax return before this deduction for student loan interest and modified by adding back any of the following items you excluded or deducted from your income.

1) Foreign earned income of U.S. citizens or residents living abroad.

2) Housing costs of U.S. citizens or residents living abroad.

3) Income from sources within Puerto Rico, American Samoa, Guam, or the Northern Mariana Islands.

Figuring the limit. To figure the limit, multiply your deduction (before the limit) by a fraction. The numerator is your modified adjusted gross income minus $40,000 ($60,000 in the case of a joint return). The denominator is $15,000. Subtract the result from your deduction (before the limit). This result is the amount you can deduct.

Example 1. During 1999 you paid $900 interest on a qualified student loan. Your 1999 modified adjusted gross income is $70,000 and you are filing a joint return. You must reduce your deduction (before the limit) by $600, figured as follows.

$$\$900 \times \frac{\$70{,}000 - \$60{,}000}{\$15{,}000} = \$600$$

You can deduct $300 ($900 – $600).

Example 2. The facts are the same as in *Example 1* except that you paid $1,600 interest. Your maximum deduction for 1999 is $1,500. You must reduce your maximum deduction by $1,000, figured as follows.

$$\$1{,}500 \times \frac{\$70{,}000 - \$60{,}000}{\$15{,}000} = \$1000$$

You can deduct $500 ($1,500 – $1,000).

CAUTION

You cannot deduct as interest on a student loan any amount you can deduct under any other provision of the tax law (for example, as home mortgage interest).

Cancellation of Loan

Forgiveness of a student loan in return for certain community service is tax free.

Qualifying loans. To qualify for tax-free treatment, your student loan must contain a provision that all or part of the debt will be canceled if you work for a certain period of time in certain professions for any of a broad class of employers. You do not have income if your student loan is later canceled because you agreed to this provision and performed the services required.

The loan must have been made by one of the following.

1) The government — federal, state, or local, or an instrumentality, agency, or subdivision thereof.

2) A tax-exempt public benefit corporation that has assumed control of a state, county, or municipal hospital, and whose employees are considered public employees under state law.

3) An educational institution if the loan is made:

   a) Under an agreement with an entity described in (1) or (2) that provided the funds to the educational institution to make the loan, or

b) Under a program of the educational institution that is designed to encourage students to serve in occupations or areas with unmet needs, and where the services required of the students are for or under the direction of a governmental unit or a tax-exempt section 501(c)(3) organization.

CAUTION *In satisfying the community service requirement in (3)(b), the student must not provide services for the lender organization.*

An ***educational institution*** is an organization with a regular faculty and curriculum and a regularly enrolled body of students in attendance at the place where the educational activities are carried on.

A ***section 501(c)(3) organization*** is any corporation, community chest, fund, or foundation organized and operated exclusively for one or more of the following purposes.

- Charitable.
- Religious.
- Educational.
- Scientific.
- Literary.
- Testing for public safety.
- Fostering national or international amateur sports competition (but only if none of its activities involve providing athletic facilities or equipment).
- The prevention of cruelty to children or animals.

Refinanced loan. If you refinanced a student loan with another loan from an educational institution or certain tax-exempt organizations, that loan can also qualify for tax-free treatment of canceled debt. This is true if the new loan was made:

1) To assist you in attending the educational institution, and

2) Under a program of the new lender that meets the conditions under (3)(b).

State Tuition Programs

Certain states and agencies maintain programs that allow people to purchase credits or certificates or make contributions to an account to pay for future education. Contributions to a qualified state tuition program are not deductible, and withdrawals are taxable only to the extent they are more than the amount contributed to the program. (See *Withdrawals more than expenses* for the education IRA.)

A qualified state tuition program is one that is established and maintained by a state or agency and that:

1) Allows a person to:

a) Buy tuition credits or certificates for a designated beneficiary who would then be entitled to a waiver or payment of qualified higher educational expenses, or

b) Make contributions to an account that is set up to meet the qualified higher educational expenses of a designated beneficiary of the account,

2) Requires all purchases or contributions to be made only in cash,

3) Prohibits the contributor and the beneficiary from directing the amount invested,

4) Allows a rollover or a change of beneficiary to be made only between members of the same family (defined earlier under *Rollovers* for the education IRA), and

5) Imposes a penalty on any refund of earnings that does not meet at least one of the following conditions.

a) The amount is used for qualified higher educational expenses of the beneficiary.

b) The refund is made because of the death or disability of the beneficiary.

c) The refund is made because the beneficiary received (and the refund is not more than) a scholarship, a veterans educational assistance allowance, or another nontaxable payment (other than a gift, bequest, or inheritance) received for educational expenses.

For more information on a specific state tuition program, contact the state or agency that established and maintains it.

Education Savings Bonds

You may be able to exclude from your gross income all or part of the interest you receive during the year on the redemption of qualified U.S. savings bonds if you pay qualified higher educational expenses during the same year.

CAUTION *If you are married, you can qualify for this exclusion only if you file a joint return with your spouse.*

Qualified U.S. savings bonds. A qualified U.S. savings bond is a series EE bond ***issued after 1989*** or a series I bond. The bond must be issued either in your name (as the sole owner) or in your and your spouse's names (as co-owners). You must be at least 24 years old before the bond's issue date.

Qualified expenses. Qualified higher education expenses include the following items you pay for either yourself, your spouse, or a dependent for whom you claim an exemption.

1) Tuition and fees required to enroll at or attend an eligible educational institution (defined earlier under *Rules That Apply to Both Credits* for the education credits). Qualified expenses do ***not*** include ex-

penses for room and board or for courses involving sports, games, or hobbies that are not part of a degree program.

2) Contributions to a qualified state tuition program.

3) Contributions to an education IRA.

Expenses reduced by certain benefits. You must reduce your qualified higher educational expenses by the amount of any of the following benefits received by the student.

1) Tax-free scholarships (see Publication 520).

2) Tax-free withdrawals from an education IRA.

3) Any nontaxable payments (other than gifts, bequests, or inheritances) received for educational expenses or for attending an eligible educational institution, such as:

   a) Veterans' educational assistance benefits,

   b) Benefits under a qualified state tuition program, or

   c) Tax-free employer-provided educational assistance.

4) Any expenses used in figuring the Hope and lifetime learning credits.

Amount excludable. If the total proceeds (interest and principal) from the qualified U.S. savings bonds you redeem during the year are not more than the qualified higher educational expenses for the year, you can exclude all of the interest. If the proceeds are more than the expenses, you can exclude only part of the interest.

To determine the excludable amount, multiply the interest part of the proceeds by a fraction. The numerator (top part) of the fraction is the qualified higher educational expenses you paid during the year. The denominator (bottom part) of the fraction is the total proceeds you received during the year.

Modified adjusted gross income limit. The interest exclusion is phased out if your modified adjusted gross income is between $53,100 and $68,100 (between $79,650 and $109,650 for joint returns). You do not qualify for the interest exclusion if your modified adjusted gross income is equal to or more than the upper limit.

Modified adjusted gross income, for purposes of this exclusion, is adjusted gross income (AGI) (line 18 of Form 1040A or line 33 of Form 1040) figured before the interest exclusion, and modified by adding back any:

1) Foreign earned income exclusion,

2) Foreign housing exclusion or deduction,

3) Exclusion of income for bona fide residents of American Samoa,

4) Exclusion for income from Puerto Rico,

5) Exclusion for adoption benefits received under an employer's adoption assistance program, and

6) Deduction for student loan interest.

Use the worksheet in the instructions for line 9, Form 8815, to figure your modified AGI. If you claim any of the exclusion or deduction items (1) – (6) listed above, add the amount of the exclusion or deduction to the amount on line 5 of the worksheet, and enter the total on Form 8815, line 9, as your modified AGI.

CAUTION *Because the deduction for interest expenses attributable to royalties and other investments is limited to your net investment income, you cannot figure the deduction until you have figured this interest exclusion. Therefore, if you had interest expenses attributable to royalties and deductible on Schedule E (Form 1040), you must make a special computation of your deductible interest without regard to this exclusion to figure the net royalty income included in your modified AGI. See* Royalties included in modified AGI *under* Education Savings Bond Program *in chapter 1 of Publication 550.*

Claiming the exclusion. Use Form 8815 to figure your exclusion. Attach the form to your Form 1040 or 1040A.

Employer-Provided Educational Assistance

Educational assistance benefits you receive from your employer under an educational assistance program are tax free, up to $5,250 each year. This means your employer should not include the benefits with your wages, tips, and other compensation shown in box 1 of your Form W–2.

CAUTION *You must reduce your* **deductible educational expenses** *by the amount of any tax-free educational assistance benefits you received for those expenses.*

Educational assistance program. To qualify as an educational assistance program, the plan must be written and meet certain other requirements. Your employer can tell you whether there is a qualified program where you work.

Educational assistance. Tax-free educational assistance benefits include payments by your employer for tuition, fees and similar expenses, books, supplies, and equipment. The payments must be for undergraduate-level courses that begin before January 1, 2002. The payments do not have to be for work-related courses.

Educational assistance benefits do ***not*** include payments for the following items.

1) Meals, lodging, transportation, or tools or supplies (other than textbooks) that you can keep after completing the course of instruction.

2) Education involving sports, games, or hobbies unless the education has a reasonable relationship to the business of your employer, or is required as part of a degree program.

3) Graduate-level courses normally taken under a program leading to a law, business, medical, or other advanced academic or professional degree.

Benefit over $5,250. If your employer gives you more than $5,250 of educational assistance benefits during the year, the amount over $5,250 is generally taxable. Your employer should include the taxable amount in your wages (box 1 of your Form W–2).

However, if the payments also qualify as a working condition fringe benefit, your employer can exclude all of the payments from your wages. A working condition fringe benefit is a benefit which, had you paid for it, you could deduct as an employee business expense. For more information on fringe benefits, see chapter 4 of Publication 535, *Business Expenses.*

Expenses paid with benefits. If you received tax-free benefits under your employer's qualified educational assistance program, you cannot take a deduction for qualified educational expenses.

CAUTION *If you had educational expenses that you excluded from gross income under your employer's educational assistance program, you cannot take the Hope credit or the lifetime learning credit for these same expenses.*

How To Get More Information

You can order free publications and forms, ask tax questions, and get more information from the IRS in several ways. By selecting the method that is best for you, you will have quick and easy access to tax help.

Free tax services. To find out what services are available, get Publication 910, *Guide to Free Tax Services.* It contains a list of free tax publications and an index of tax topics. It also describes other free tax information services, including tax education and assistance programs and a list of TeleTax topics.

Personal computer. With your personal computer and modem, you can access the IRS on the Internet at **www.irs.gov**. While visiting our web site, you can select:

- *Frequently Asked Tax Questions* (located under *Taxpayer Help & Ed)* to find answers to questions you may have.
- *Forms & Pubs* to download forms and publications or search for forms and publications by topic or keyword.
- *Fill-in Forms* (located under *Forms & Pubs)* to enter information while the form is displayed and then print the completed form.
- *Tax Info For You* to view Internal Revenue Bulletins published in the last few years.
- *Tax Regs in English* to search regulations and the Internal Revenue Code (under *United States Code (USC)).*
- *Comments & Help* to e-mail us with comments about the site or with tax questions.
- *Digital Dispatch* and *IRS Local News Net* (both located under *Tax Info For Business)* to receive our electronic newsletters on hot tax issues and news.
- *Small Business Corner* (located under *Tax Info For Business)* to get information on starting and operating a small business.

You can also reach us with your computer using File Transfer Protocol at **ftp.irs.gov.**

TaxFax Service. Using the phone attached to your fax machine, you can receive forms and instructions by calling **703–368–9694.** Follow the directions from the prompts. When you order forms, enter the catalog number for the form you need. The items you request will be faxed to you.

Phone. Many services are available by phone.

- *Ordering forms, instructions, and publications.* Call **1–800–829–3676** to order current and prior year forms, instructions, and publications.
- *Asking tax questions.* Call the IRS with your tax questions at **1–800–829–1040**.
- *TTY/TDD equipment.* If you have access to TTY/TDD equipment, call **1–800–829–4059** to ask tax questions or to order forms and publications.
- *TeleTax topics.* Call **1–800–829–4477** to listen to pre-recorded messages covering various tax topics.

Evaluating the quality of our telephone services. To ensure that IRS representatives give accurate, courteous, and professional answers, we evaluate the quality of our telephone services in several ways.

- A second IRS representative sometimes monitors live telephone calls. That person only evaluates the IRS assistor and does not keep a record of any taxpayer's name or tax identification number.
- We sometimes record telephone calls to evaluate IRS assistors objectively. We hold these recordings no longer than one week and use them only to measure the quality of assistance.
- We value our customers' opinions. Throughout this year, we will be surveying our customers for their opinions on our service.

Walk-in. You can walk in to many post offices, libraries, and IRS offices to pick up certain forms, instructions, and publications. Also, some libraries and IRS offices have:

- An extensive collection of products available to print from a CD-ROM or photocopy from reproducible proofs.
- The Internal Revenue Code, regulations, Internal Revenue Bulletins, and Cumulative Bulletins available for research purposes.

Mail. You can send your order for forms, instructions, and publications to the Distribution Center nearest to you and receive a response within 10 workdays after your request is received. Find the address that applies to your part of the country.

- **Western part of U.S.:**
  Western Area Distribution Center
  Rancho Cordova, CA 95743–0001
- **Central part of U.S.:**
  Central Area Distribution Center
  P.O. Box 8903
  Bloomington, IL 61702–8903
- **Eastern part of U.S. and foreign addresses:**
  Eastern Area Distribution Center
  P.O. Box 85074
  Richmond, VA 23261–5074

CD-ROM. You can order IRS Publication 1796, *Federal Tax Products on CD-ROM,* and obtain:

- Current tax forms, instructions, and publications.
- Prior-year tax forms, instructions, and publications.
- Popular tax forms which may be filled in electronically, printed out for submission, and saved for recordkeeping.
- Internal Revenue Bulletins.

The CD-ROM can be purchased from National Technical Information Service (NTIS) by calling **1–877–233–6767** or on the Internet at **www.irs.gov/cdorders.** The first release is available in mid-December and the final release is available in late January.

IRS Publication 3207, *Small Business Resource Guide,* is an interactive CD-ROM that contains information important to small businesses. It is available in mid-February. You can get one free copy by calling **1–800–829–3676.**

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Tax Publications for Individual Taxpayers

See *How To Get More Information* for a variety of ways to get publications, including by computer, phone, and mail.

General Guides

- **1** Your Rights as a Taxpayer
- **17** Your Federal Income Tax (For Individuals)
- **225** Farmer's Tax Guide
- **334** Tax Guide for Small Business
- **509** Tax Calendars for 2000
- **553** Highlights of 1999 Tax Changes
- **595** Tax Highlights for Commercial Fishermen
- **910** Guide to Free Tax Services

Specialized Publications

- **3** Armed Forces' Tax Guide
- **378** Fuel Tax Credits and Refunds
- **463** Travel, Entertainment, Gift, and Car Expenses
- **501** Exemptions, Standard Deduction, and Filing Information
- **502** Medical and Dental Expenses
- **503** Child and Dependent Care Expenses
- **504** Divorced or Separated Individuals
- **505** Tax Withholding and Estimated Tax
- **508** Tax Benefits for Work-Related Education
- **514** Foreign Tax Credit for Individuals
- **516** U.S. Government Civilian Employees Stationed Abroad
- **517** Social Security and Other Information for Members of the Clergy and Religious Workers
- **519** U.S. Tax Guide for Aliens
- **520** Scholarships and Fellowships
- **521** Moving Expenses
- **523** Selling Your Home
- **524** Credit for the Elderly or the Disabled
- **525** Taxable and Nontaxable Income
- **526** Charitable Contributions
- **527** Residential Rental Property
- **529** Miscellaneous Deductions
- **530** Tax Information for First-Time Homeowners
- **531** Reporting Tip Income
- **533** Self-Employment Tax
- **534** Depreciating Property Placed in Service Before 1987
- **537** Installment Sales
- **541** Partnerships
- **544** Sales and Other Dispositions of Assets
- **547** Casualties, Disasters, and Thefts (Business and Nonbusiness)
- **550** Investment Income and Expenses
- **551** Basis of Assets
- **552** Recordkeeping for Individuals
- **554** Older Americans' Tax Guide
- **555** Community Property
- **556** Examination of Returns, Appeal Rights, and Claims for Refund
- **559** Survivors, Executors, and Administrators
- **561** Determining the Value of Donated Property
- **564** Mutual Fund Distributions
- **570** Tax Guide for Individuals With Income From U.S. Possessions
- **575** Pension and Annuity Income
- **584** Casualty, Disaster, and Theft Loss Workbook (Personal-Use Property)
- **587** Business Use of Your Home (Including Use by Day-Care Providers)
- **590** Individual Retirement Arrangements (IRAs) (Including Roth IRAs and Education IRAs)
- **593** Tax Highlights for U.S. Citizens and Residents Going Abroad
- **594** Understanding the Collection Process
- **596** Earned Income Credit (EIC)
- **721** Tax Guide to U.S. Civil Service Retirement Benefits
- **901** U.S. Tax Treaties
- **907** Tax Highlights for Persons with Disabilities
- **908** Bankruptcy Tax Guide
- **911** Direct Sellers
- **915** Social Security and Equivalent Railroad Retirement Benefits
- **919** How Do I Adjust My Tax Withholding?
- **925** Passive Activity and At-Risk Rules
- **926** Household Employer's Tax Guide
- **929** Tax Rules for Children and Dependents
- **936** Home Mortgage Interest Deduction
- **946** How To Depreciate Property
- **947** Practice Before the IRS and Power of Attorney
- **950** Introduction to Estate and Gift Taxes
- **967** IRS Will Figure Your Tax
- **968** Tax Benefits for Adoption
- **970** Tax Benefits for Higher Education
- **971** Innocent Spouse Relief
- **972** Child Tax Credit
- **1542** Per Diem Rates
- **1544** Reporting Cash Payments of Over $10,000
- **1546** The Taxpayer Advocate Service of the IRS

Spanish Language Publications

- **1SP** Derechos del Contribuyente
- **579SP** Cómo Preparar la Declaración de Impuesto Federal
- **594SP** Comprendiendo el Proceso de Cobro
- **596SP** Crédito por Ingreso del Trabajo
- **850** English-Spanish Glossary of Words and Phrases Used in Publications Issued by the Internal Revenue Service
- **1544SP** Informe de Pagos en Efectivo en Exceso de $10,000 (Recibidos en una Ocupación o Negocio)

Commonly Used Tax Forms

See *How To Get More Information* for a variety of ways to get forms, including by computer, fax, phone, and mail. For fax orders only, use the catalog numbers when ordering.

Form Number and Title	Catalog Number
1040 U.S. Individual Income Tax Return	11320
Sch A & B Itemized Deductions & Interest and Ordinary Dividends	11330
Sch C Profit or Loss From Business	11334
Sch C-EZ Net Profit From Business	14374
Sch D Capital Gains and Losses	11338
Sch D-1 Continuation Sheet for Schedule D	10424
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Sch EIC Earned Income Credit	13339
Sch F Profit or Loss From Farming	11346
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Sch R Credit for the Elderly or the Disabled	11359
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Sch 2 Child and Dependent Care Expenses for Form 1040A Filers	10749
Sch 3 Credit for the Elderly or the Disabled for Form 1040A Filers	12064
1040EZ Income Tax Return for Single and Joint Filers With No Dependents	11329
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2210 Underpayment of Estimated Tax by Individuals, Estates, and Trusts	11744
2441 Child and Dependent Care Expenses	11862
2848 Power of Attorney and Declaration of Representative	11980
3903 Moving Expenses	12490
4562 Depreciation and Amortization	12906
4868 Application for Automatic Extension of Time To File U.S. Individual Income Tax Return	13141
4952 Investment Interest Expense Deduction	13177
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8582 Passive Activity Loss Limitations	63704
8606 Nondeductible IRAs	63966
8812 Additional Child Tax Credit	10644
8822 Change of Address	12081
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8863 Education Credits	25379