

105TH CONGRESS
1ST SESSION

H. R. 1597

To amend the Internal Revenue Code of 1986 to provide for the establishment of, and the deduction of contributions to, education savings accounts.

IN THE HOUSE OF REPRESENTATIVES

MAY 14, 1997

Mr. GILLMOR (for himself, Mr. SOLOMON, Mr. LIVINGSTON, Mr. ENGLISH of Pennsylvania, Mr. WATTS of Oklahoma, Mr. KING, Mr. CANADY of Florida, Mr. SHAYS, Mr. QUINN, Mr. MCHUGH, Mr. MANZULLO, Mr. DOOLITTLE, Mr. GREENWOOD, Mr. NORWOOD, Mrs. KELLY, Ms. GRANGER, Mr. UNDERWOOD, Ms. NORTON, Mr. EHLERS, Mr. KNOLLENBERG, Mr. FALEOMAVAEGA, Mr. BEREUTER, Mr. KLUG, Mr. SKEEN, Mr. SENSENBRENNER, Mr. GRAHAM, Mr. BOB SCHAFER of Colorado, and Mr. BILIRAKIS) introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to provide for the establishment of, and the deduction of contributions to, education savings accounts.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. EDUCATION SAVINGS ACCOUNTS.**

4 (a) IN GENERAL.—Part VII of subchapter B of chap-
5 ter 1 of the Internal Revenue Code of 1986 (relating to
6 additional itemized deductions for individuals) is amended

1 by redesignating section 221 as section 222 and by insert-
 2 ing after section 220 the following new section:

3 **“SEC. 221. EDUCATION SAVINGS ACCOUNTS.**

4 “(a) DEDUCTION ALLOWED.—In the case of an indi-
 5 vidual, there shall be allowed as a deduction the sum of—

6 “(1) amounts paid in cash, and

7 “(2) the fair market value of stocks, bonds, or
 8 other securities, which are readily tradable on an es-
 9 tablished securities market, transferred,

10 during the calendar year which ends with or within the
 11 taxable year by such individual to an education savings
 12 account established for the purpose of accumulating funds
 13 to pay the educational expenses of an eligible individual.

14 “(b) LIMITATIONS.—

15 “(1) ACCOUNT MAY NOT BE ESTABLISHED FOR
 16 BENEFIT OF MORE THAN 1 INDIVIDUAL.—An edu-
 17 cation savings account may not be established for
 18 the benefit of more than 1 individual.

19 “(2) ELIGIBLE INDIVIDUAL TREATED AS ELIGI-
 20 BLE INDIVIDUAL ONLY WITH RESPECT TO 1 AC-
 21 COUNT.—If, at any time during a calendar year, 2
 22 or more education savings accounts are maintained
 23 for the benefit of an eligible individual, such individ-
 24 ual shall be treated as an eligible individual for the

1 calendar year only with respect to the first of such
2 accounts.

3 “(3) MAXIMUM DEDUCTION PER ACCOUNT.—

4 The amount allowable as a deduction under sub-
5 section (a) to an individual for amounts paid or
6 transferred to an education savings account for any
7 calendar year shall not exceed \$2,000.

8 “(4) NO DEDUCTION AFTER BENEFICIARY AT-

9 TAINS AGE 19.—No deduction shall be allowed for
10 any contribution to an education savings account es-
11 tablished for the benefit of an eligible individual who
12 has attained age 19 before the close of the calendar
13 year in which such contribution is made.

14 “(5) ADJUSTMENT OF DOLLAR AMOUNT LIM-

15 TATIONS FOR INFLATION.—In the case of any cal-
16 endar year after 1997, the \$2,000 contained in
17 paragraph (3) and subsection (c)(2)(A) shall be in-
18 creased by an amount equal to—

19 “(A) \$2,000, multiplied by

20 “(B) the cost-of-living adjustment deter-
21 mined under section 1(f)(3) for such calendar
22 year by substituting ‘calendar year 1996’ for
23 ‘calendar year 1992’ in subparagraph (B)
24 thereof.

1 Any increase determined under the preceding sen-
2 tence shall be rounded to the nearest multiple of
3 \$10.

4 “(c) DEFINITIONS AND SPECIAL RULES.—For pur-
5 poses of this section—

6 “(1) ELIGIBLE INDIVIDUAL.—The term ‘eligible
7 individual’ means an individual who is—

8 “(A) a child (within the meaning of section
9 153(e)(3)) of the taxpayer or of a brother, sis-
10 ter, stepbrother, or stepsister of the taxpayer,

11 “(B) an individual with respect to whom
12 the taxpayer has been appointed guardian by a
13 court of competent jurisdiction, or

14 “(C) a descendant of a child of the tax-
15 payer.

16 “(2) EDUCATION SAVINGS ACCOUNT.—The
17 term ‘education savings account’ means a trust cre-
18 ated or organized in the United States exclusively
19 for the purpose of paying the educational expenses
20 of an eligible individual, but only if the written gov-
21 erning instrument creating the trust meets the fol-
22 lowing requirements:

23 “(A) No contribution will be accepted un-
24 less it is in cash, stocks, bonds, or other securi-
25 ties which are readily tradable on an established

1 securities market, and, except in the case of
2 contributions from another education savings
3 account or an individual retirement plan, con-
4 tributions will not be accepted for the taxable
5 year in excess of \$2,000.

6 “(B) The trustee is a bank (as defined in
7 section 408(n)) or another person who dem-
8 onstrates to the satisfaction of the Secretary
9 that the manner in which that person will ad-
10 minister the trust will be consistent with the re-
11 quirements of this section.

12 “(C) No part of the trust assets will be in-
13 vested in life insurance contracts (other than
14 contracts the beneficiary of which is the trust
15 and the face amount of which does not exceed
16 the amount by which the maximum amount
17 which can be contributed to the account exceeds
18 the sum of the amounts contributed to the ac-
19 count for all taxable years).

20 “(D) The assets of the account may be in-
21 vested in accordance with the direction of the
22 individual contributing to the account, but, if
23 more than one individual has made contribu-
24 tions to the account, the consent of all such in-

1 dividuals shall be required for any such direc-
2 tion.

3 “(E) The assets of the trust shall not be
4 commingled with other property except in a
5 common trust fund or common investment
6 fund.

7 “(F) Any balance in the account on the
8 day after the date on which the individual for
9 whose benefit the trust is established attains
10 age 30 (or, if earlier, the date on which such
11 individual dies) shall be distributed within 30
12 days of such date—

13 “(i) in accordance with paragraph (5)
14 to each of the individuals who have con-
15 tributed to the trust, or

16 “(ii) as directed by such individuals,
17 to another education savings account es-
18 tablished for the benefit of an eligible indi-
19 vidual who has not attained age 30 or to
20 an eligible educational institution.

21 “(3) TIME WHEN CONTRIBUTIONS DEEMED
22 MADE.—A taxpayer shall be deemed to have made a
23 contribution on the last day of the preceding taxable
24 year if the contribution is made on account of such
25 taxable year and is made not later than the time

1 prescribed by law for filing the return for such tax-
2 able year (including extensions thereof).

3 “(4) STOCK, ETC., TO BE VALUED AS OF
4 TRANSFER DATE.—The fair market value of stocks,
5 bonds, and other securities shall be determined as of
6 the date on which they are transferred to the ac-
7 count. If the date of transfer falls on a Saturday,
8 Sunday, or public legal holiday, then the fair market
9 value shall be determined by reference to the last
10 preceding day on which they could have been traded
11 on an established securities market.

12 “(5) DISTRIBUTION OF BALANCE IN ACCOUNT
13 TO CONTRIBUTORS.—The Secretary shall prescribe
14 regulations describing the manner in which any bal-
15 ance in the educational savings account shall be dis-
16 tributed under paragraph (2)(F)(i) among the con-
17 tributors to the account. Any division of the balance
18 in the account shall reflect—

19 “(A) the amount of net income of the ac-
20 count which is attributable to the contributions
21 of each such individual, and

22 “(B) a proper allocation of any amounts
23 previously distributed from the account for edu-
24 cational expenses among the contributions
25 which were made before any such distribution

1 (including the net income of the account which
2 was attributable to such contributions and
3 earned before any such distribution).

4 “(6) EDUCATIONAL EXPENSES.—The term
5 ‘educational expenses’ means—

6 “(A) tuition and fees required for the en-
7 rollment or attendance of a student at an eligi-
8 ble educational institution,

9 “(B) fees, books, supplies, and equipment
10 required for courses of instruction at an eligible
11 educational institution, and

12 “(C) a reasonable allowance for meals and
13 lodging while attending an eligible educational
14 institution.

15 “(7) ELIGIBLE EDUCATIONAL INSTITUTION.—
16 The term ‘eligible educational institution’ means—

17 “(A) an institution of higher education, or

18 “(B) a vocational school.

19 “(8) INSTITUTION OF HIGHER EDUCATION.—

20 The term ‘institution of higher education’ means the
21 institutions described in section 1201(a) or 481(a)
22 of the Higher Education Act of 1965.

23 “(9) VOCATIONAL SCHOOL.—The term ‘voca-
24 tional school’ means an area vocational education
25 school as defined in subparagraph (C) or (D) of sec-

1 tion 521(4) of the Carl D. Perkins Vocational and
2 Applied Technology Education Act to the extent
3 such school is located within any State (as defined
4 in section 521(33) of such Act).

5 “(d) TAX TREATMENT OF DISTRIBUTIONS.—

6 “(1) IN GENERAL.—Except as otherwise pro-
7 vided in this subsection, any amount paid or distrib-
8 uted out of an education savings account shall be in-
9 cluded in gross income of the payee or distributee
10 for the taxable year in which the payment or dis-
11 tribution is received to the extent such amount is
12 not the return of a contribution for which no deduc-
13 tion was allowed under subsection (a).

14 “(2) DISTRIBUTION USED TO PAY EDU-
15 CATIONAL EXPENSES.—Paragraph (1) shall not
16 apply to any payment or distribution out of an edu-
17 cation savings account to the extent such payment
18 or distribution is used exclusively to pay the edu-
19 cational expenses incurred by the individual for
20 whose benefit the account is established.

21 “(3) DISTRIBUTIONS TO ANOTHER ACCOUNT OR
22 TO ELIGIBLE EDUCATIONAL INSTITUTION.—Para-
23 graph (1) shall not apply to any distribution under
24 subsection (c)(2)(F)(ii).

1 “(4) EXCESS CONTRIBUTIONS RETURNED BE-
2 FORE DUE DATE OF RETURN.—Paragraph (1) does
3 not apply to the distribution of any contribution paid
4 during a taxable year to an education savings ac-
5 count to the extent that such contribution exceeds
6 the amount allowable as a deduction under sub-
7 section (a) if—

8 “(A) such distribution is received on or be-
9 fore the day prescribed by law (including exten-
10 sions of time) for filing such individual’s return
11 for such taxable year,

12 “(B) no deduction is allowed under sub-
13 section (a) with respect to such excess contribu-
14 tion, and

15 “(C) such distribution is accompanied by
16 the amount of net income attributable to such
17 excess contribution.

18 Any net income described in subparagraph (C) shall
19 be included in the gross income of the individual for
20 the taxable year in which such excess contribution
21 was made.

22 “(5) DISTRIBUTIONS TO INDIVIDUAL RETIRE-
23 MENT PLANS.—Paragraph (1) shall not apply to any
24 payment or distribution out of an education savings
25 account if—

1 “(A) before the close of the 60th day after
2 the day on which the payment or distribution is
3 received, the payment or distribution is contrib-
4 uted into an individual retirement plan of an in-
5 dividual who contributed to the education sav-
6 ings account, and

7 “(B) the amount of such payment or dis-
8 tribution (when added to all prior payments or
9 distributions excluded from the gross income of
10 such individual by reason of this paragraph)
11 does not exceed the aggregate amount contrib-
12 uted to the education savings account by the in-
13 dividual from amounts paid or distributed out
14 of an individual retirement plan in accordance
15 with section 408(d)(8).

16 “(e) TAX TREATMENT OF ACCOUNTS.—

17 “(1) EXEMPTION FROM TAX.—An education
18 savings account is exempt from taxation under this
19 subtitle unless such account has ceased to be an
20 education savings account by reason of paragraph
21 (2) or (3). Notwithstanding the preceding sentence,
22 any such account is subject to the taxes imposed by
23 section 511 (relating to imposition of tax on unre-
24 lated business income of charitable, etc. organiza-
25 tions).

1 “(2) LOSS OF EXEMPTION OF ACCOUNT WHERE
2 INDIVIDUAL ENGAGES IN PROHIBITED TRANS-
3 ACTION.—

4 “(A) IN GENERAL.—If the individual for
5 whose benefit an education savings account is
6 established or any individual who contributes to
7 such account engages in any transaction prohib-
8 ited by section 4975 with respect to the ac-
9 count, the account shall cease to be an edu-
10 cation savings account as of the first day of the
11 taxable year (of the individual so engaging in
12 such transaction) during which such transaction
13 occurs.

14 “(B) ACCOUNT TREATED AS DISTRIBUTING
15 ALL ITS ASSETS.—In any case in which any ac-
16 count ceases to be an education savings account
17 by reason of subparagraph (A) as of the first
18 day of any taxable year, paragraph (1) of sub-
19 section (d) shall apply as if there was a dis-
20 tribution on such first day in an amount equal
21 to the fair market value (on such first day) of
22 all assets in the account (on such first day).

23 “(3) EFFECT OF PLEDGING ACCOUNT AS SECU-
24 RITY.—If, during any taxable year, the individual for
25 whose benefit an education savings account is estab-

1 lished, or any individual who contributes to such ac-
 2 count, uses the account or any portion thereof as se-
 3 curity for a loan, the portion so used shall be treated
 4 as distributed to the individual so using such por-
 5 tion.

6 “(f) ADDITIONAL TAX ON CERTAIN AMOUNTS IN-
 7 CLUDED IN GROSS INCOME.—

8 “(1) DISTRIBUTION NOT USED FOR EDU-
 9 CATIONAL EXPENSES.—In the case of any payment
 10 or distribution to which subsection (d)(1) applies,
 11 the tax liability of each payee or distributee under
 12 this chapter for the taxable year in which the pay-
 13 ment or distribution is received shall be increased by
 14 an amount equal to 10 percent of the amount of the
 15 distribution which is includible in the gross income
 16 of such payee or distributee for such taxable year.

17 “(2) DISQUALIFICATION CASES.—If an amount
 18 is includible in the gross income of an individual for
 19 a taxable year because such amount is required to
 20 be treated as a distribution under paragraph (2) or
 21 (3) of subsection (e), such individual’s tax liability
 22 under this chapter for such taxable year shall be in-
 23 creased by an amount equal to 10 percent of such
 24 amount required to be treated as a distribution and
 25 included in his gross income.

1 “(3) DISABILITY OR DEATH CASES.—Para-
2 graphs (1) and (2) shall not apply if the payment
3 or distribution is made after the individual for whose
4 benefit the education savings account becomes dis-
5 abled within the meaning of section 72(m)(7) or
6 dies.

7 “(g) COMMUNITY PROPERTY LAWS.—This section
8 shall be applied without regard to any community property
9 laws.

10 “(h) CUSTODIAL ACCOUNTS.—For purposes of this
11 section, a custodial account shall be treated as a trust if
12 the assets of such account are held by a bank (as defined
13 in section 408(n)) or another person who demonstrates,
14 to the satisfaction of the Secretary, that the manner in
15 which he will administer the account will be consistent
16 with the requirements of this section, and if the custodial
17 account would, except for the fact that it is not a trust,
18 constitute an education savings account described in sub-
19 section (c)(2). For purposes of this title, in the case of
20 a custodial account treated as a trust by reason of the
21 preceding sentence, the custodian of such account shall be
22 treated as the trustee thereof.

23 “(i) REPORTS.—The trustee of an education savings
24 account shall make such reports regarding such account
25 to the Secretary and to the individual for whose benefit

1 the account is maintained with respect to contributions,
 2 distributions, and such other matters as the Secretary
 3 may require under regulations. The reports required by
 4 this subsection shall be filed at such time and in such
 5 manner and furnished to such individuals at such time and
 6 in such manner as may be required by those regulations.”

7 (b) DEDUCTION ALLOWED IN ARRIVING AT AD-
 8 JUSTED GROSS INCOME.—Paragraph (7) of section 62(a)
 9 of such Code (relating to retirement savings) is
 10 amended—

11 (1) by inserting “OR EDUCATION” after “RE-
 12 TIREMENT” in the heading of such paragraph, and

13 (2) by inserting before the period at the end the
 14 following: “and the deduction allowed by section 221
 15 (relating to education savings accounts)”.

16 (c) TAX ON EXCESS CONTRIBUTIONS.—

17 (1) Subsection (a) of section 4973 of such Code
 18 (relating to tax on certain excess contributions) is
 19 amended by striking “or” at the end of paragraph
 20 (2), by inserting “or” at the end of paragraph (3),
 21 and by inserting after paragraph (3) the following
 22 new paragraph:

23 “(4) an education savings account (within the
 24 meaning of section 221(c)(2)),”.

1 (2) Section 4973 of such Code is amended by
2 adding at the end the following new subsection:

3 “(e) **EXCESS CONTRIBUTIONS TO EDUCATION SAV-**
4 **INGS ACCOUNTS.**—For purposes of this section, in the
5 case of an education savings account, the term ‘excess con-
6 tributions’ means the amount by which the amount con-
7 tributed for the taxable year to the account exceeds the
8 amount allowable as a deduction under section 221 for
9 such taxable year. For purposes of this subsection, any
10 contribution which is distributed out of the education sav-
11 ings account in a distribution to which section 221(d)(4)
12 applies shall be treated as an amount not contributed.”

13 (3) The section heading for section 4973 of
14 such Code is amended to read as follows:

15 **“SEC. 4973. EXCESS CONTRIBUTIONS TO CERTAIN TAX-FA-**
16 **VORED ACCOUNTS, ANNUITIES, ETC.”**

17 (4) The table of sections for chapter 43 of such
18 Code is amended by striking the item relating to sec-
19 tion 4973 and inserting the following new item:

“Sec. 4973. Excess contributions to certain tax-favored accounts,
annuities, etc.”

20 (d) **CONTRIBUTION NOT SUBJECT TO GIFT TAX.**—
21 Section 2503 of such Code (relating to taxable gifts) is
22 amended by adding at the end the following new sub-
23 section:

1 “(h) EDUCATION SAVINGS ACCOUNTS.—Any con-
 2 tribution made by an individual to an education savings
 3 account described in section 221(c)(2) which is allowable
 4 as a deduction under section 221 shall not be treated as
 5 a transfer of property by gift for purposes of this
 6 chapter.”

7 (e) TAX ON PROHIBITED TRANSACTIONS.—

8 (1) Section 4975 of such Code (relating to pro-
 9 hibited transactions) is amended by adding at the
 10 end of subsection (c) the following new paragraph:

11 “(5) SPECIAL RULE FOR EDUCATION SAVINGS
 12 ACCOUNTS.—An individual for whose benefit an edu-
 13 cation savings account is established and any con-
 14 tributor to such account shall be exempt from the
 15 tax imposed by this section with respect to any
 16 transaction concerning such account (which would
 17 otherwise be taxable under this section) if, with re-
 18 spect to such transaction, the account ceases to be
 19 an education savings account by reason of the appli-
 20 cation of section 221(e)(2)(A) to such account.”

21 (2) Paragraph (1) of section 4975(e) of such
 22 Code is amended by striking “or” at the end of sub-
 23 paragraph (D), by redesignating subparagraph (E)
 24 as subparagraph (F), and by inserting after sub-
 25 paragraph (D) the following new subparagraph:

1 “(E) an education savings account de-
 2 scribed in section 221(c)(2), or”.

3 (f) FAILURE TO PROVIDE REPORTS ON EDUCATION
 4 SAVINGS ACCOUNTS.—

5 (1) Paragraph (2) of section 6693(a) of such
 6 Code (relating to failure to provide reports on indi-
 7 vidual retirement accounts or annuities) is amended
 8 by striking “and” at the end of subparagraph (A),
 9 by striking the period at the end of subparagraph
 10 (B) and inserting “, and”, and by adding at the end
 11 the following new subparagraph:

12 “(C) section 221(i) (relating to education
 13 savings accounts).”

14 (2) The section heading for section 6693 of
 15 such Code is amended to read as follows:

16 **“SEC. 6693. FAILURE TO PROVIDE REPORTS ON CERTAIN**
 17 **TAX-FAVORED ACCOUNTS, ETC.”**

18 (3) The table of sections for part I of sub-
 19 chapter B of chapter 68 of such Code is amended
 20 by striking the item relating to section 6693 and in-
 21 serting the following new item:

“Sec. 6693. Failure to provide reports on certain tax-favored ac-
 counts, etc.”

22 (g) SPECIAL RULE FOR DETERMINING AMOUNTS OF
 23 SUPPORT FOR DEPENDENT.—Subsection (b) of section
 24 152 of such Code (relating to definition of dependent) is

1 amended by adding at the end the following new para-
 2 graph:

3 “(6) A distribution from an education savings
 4 account described in section 221(c)(2) to the individ-
 5 ual for whose benefit such account has been estab-
 6 lished shall not be taken into account in determining
 7 support for purposes of this section to the extent
 8 such distribution is excluded from gross income of
 9 such individual under section 221(d)(2).”

10 (h) CLERICAL AMENDMENT.—The table of sections
 11 for part VII of subchapter B of chapter 1 of such Code
 12 is amended by striking the item relating to section 221
 13 and inserting the following new items:

“Sec. 221. Education savings accounts.
 “Sec. 222. Cross reference.”

14 **SEC. 2. TRANSFERS BETWEEN INDIVIDUAL RETIREMENT**
 15 **PLANS AND EDUCATION SAVINGS ACCOUNTS.**

16 (a) EXEMPTION FROM ANNUAL CONTRIBUTION LIM-
 17 ITATION FOR DISTRIBUTIONS FROM EDUCATION SAVINGS
 18 ACCOUNTS INTO IRA’S.—Paragraph (1) of section 408(a)
 19 of the Internal Revenue Code of 1986 (relating to defini-
 20 tion of individual retirement account) is amended by in-
 21 serting after “403(b)(8),” the following: “or in the case
 22 of a contribution from an education savings account in ac-
 23 cordance with section 221(d)(5),”.

1 (b) EXCLUSION FROM GROSS INCOME FOR DIS-
 2 TRIBUTIONS FROM IRA'S INTO EDUCATION SAVINGS AC-
 3 COUNTS.—Subsection (d) of section 408 of such Code (re-
 4 lating to tax treatment of distributions from individual re-
 5 irement plans) is amended by adding at the end the fol-
 6 lowing new paragraph:

7 “(8) DISTRIBUTIONS USED TO MAKE CON-
 8 TRIBUTION TO EDUCATION SAVINGS ACCOUNT.—
 9 Paragraph (1) shall not apply to any amount paid
 10 or distributed out of an individual retirement plan if,
 11 before the close of the 60th day after the day on
 12 which the payment or distribution is received, the
 13 payment or distribution is contributed into an edu-
 14 cation savings account (as defined in section
 15 221(c)(2)).

16 **SEC. 3. EFFECTIVE DATE.**

17 The amendments made by this Act shall apply to tax-
 18 able years beginning after December 31, 1996.

○