Education – IRA's

~~Andy has~~ signed off on this —

EDUC — EDUCATION

VRA's

Brooke B. Livingston 02/23/2000 04:47:53 PM

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Subject: URGENT FOR CLEARANCE -- S. 1143, the Affordable Education Act -- COMMENTS DUE BY 6PM

Attached for your review is the SAP on S. 1143, the Affordable Education Act. **JACK AND SYLVIA HAVE NOT CLEARED THIS SAP, BUT HAVE ASKED THAT I CIRCULATE IT TO THE WEST WING BECAUSE THE LEGISLATION IS CURRENTLY BEING CONSIDERED ON THE SENATE FLOOR.**

COMMENTS DUE BY 6:00PM.

POSITION
Education and Treasury veto threat.

This position is consistent with the Rubin/Riley letter on this bill sent to the Senate Finance Committee in May 1999 and the SAP on an almost identical bill, HR 2646, which the President vetoed in 1998 (no override attempt).

BACKGROUND
Purpose: Authorizes increased contributions to an education savings account that could be used for K -12 education. Withdrawals from the account, which would be tax-free, would be permitted for private school tuition, a church school, tutoring, or home schooling. Also authorizes increased tax exemption for bonds issued for school construction.

Objections: Disproportionately benefits the most affluent families and provides little to lower- and middle-income families; would create significant tax compliance problems; and would not generate additional savings but only reward some families for what they already do.

CLEARANCE
Lew, Mathews, Chow, Minarik, Deich, Zegers (OMB); WHLA; NEC; DPC; CEA; CoS.

TIMING
THIS BILL IS ALREADY ON THE SENATE FLOOR. I WOULD APPRECIATE YOUR COMMENTS BY 6PM. THANK YOU FOR THE QUICK TURN-AROUND.

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DRAFT -- NOT FOR RELEASE

February 23, 2000
(Senate)

S. 1134 - Affordable Education Act
(Sen. Roth (R) Delaware)

The Administration strongly opposes S. 1134. In 1998, the President vetoed legislation -- H.R. 2646, the "Education Savings and School Excellence Act of 1998" -- that included provisions similar to those contained in S. 1134. At that time, the President described the bill's modifications to Education IRAs as bad education policy and bad tax policy. S. 1134 is equally flawed, and, as the Secretaries of Education and the Treasury stated in their May 18, 1999, letter to the Senate Finance Committee, if it were presented to the President they would recommend that he veto the bill.

Every American child deserves a high-quality elementary and secondary education. The President's FY 2001 Budget contains a series of education tax initiatives, including expanded tax benefits for lower- and middle-income families to defray the cost of higher education, and tax-credit bonds to assist State and local governments in meeting the cost of financing construction, rehabilitation, or repair of public schools. S. 1134 fails to advance education reform and distracts from the need to invest in public schools, where the vast majority of our students learn. It does nothing to reduce class size, improve teacher quality, or help students meet high academic standards. In addition, the provisions to repair or modernize schools are woefully inadequate. Targeting limited Federal resources toward building stronger public schools will help ensure that all our Nation's children receive the education they need to become productive citizens. S. 1134 would divert needed resources away from public schools.

S. 1134 would disproportionately benefit the most affluent families and provide little benefit to lower- and middle-income families. Moreover, given the expansion of tax-preferred savings vehicles in the Taxpayer Relief Act of 1997, which the Administration supported, further increasing the contribution limits for Education IRAs is unlikely to provide significant additional incentives for families to increase their savings for educational purposes. Instead, S. 1134 would reward many families, particularly those with substantial incomes, for what they may already do.

S. 1134 would also create significant compliance problems. The bill permits tax-free withdrawals from Education IRAs for, among other things, tuition, fees, academic tutoring, special needs services, books, room and board, and supplies and equipment expenses incurred in connection with enrollment or attendance in public or private elementary or secondary schools. Distinguishing between withdrawals that should not be subject to tax and those that should will add significant record-keeping requirements for families and schools and will lead to frequent disputes about the use of the withdrawals for discretionary purchases.

Pay-As-You-Go Scoring

S. 1134 would affect receipts; therefore, it is subject to the pay-as-you-go requirement of the Omnibus Reconciliation Act of 1990. The Administration has not yet completed its scoring of the bill.

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(Do Not Distribute Outside the Executive Office of the President)

This Statement of Administration Policy (SAP) was developed by the Legislative Reference Division (Jones) in consultation with the Departments of the Treasury (Comstock, Fant, and Dorsey) and Education (Riddle); the Council of Economic Advisers (Williams); and within OMB by EIMLD (Rasetti) and BASD (Barth).

The Domestic Policy Council, the National Economic Council, and OMB Economic Policy did not respond to our request for comments on the draft SAP.

OMB/LA Clearance:

S. 1134 was reported by the Senate Finance Committee by a vote of 12-8.

Administration Position to Date

On May 8, 1999 Treasury Secretary Summers and Education Secretary Riley, in a letter to the Senate Finance Committee, expressed the Administration's strong opposition to S. 1134 and stated that they would recommend that the President veto the bill.

Summary of S. 1134

Education IRAs. Education IRAs, which were created by the "Taxpayer Relief Act of 1997", are trusts or custodial accounts created exclusively to pay higher education expenses of a named beneficiary. Contributions to Education IRAs are not tax deductible but earnings on the account generally are not taxed until they are distributed to the beneficiary. Contributions into those accounts can be made by any person or corporation, but the contribution amount is phased out for higher income taxpayers.

S. 1134 would modify Education IRAs by:

- increasing the current limit on the annual contributions to an Education IRA from $500 to $2,000 for tax years beginning after December 31, 1999, and ending before January 1, 2004;

- permitting withdrawals from Education IRAs to be used for qualified expenses at a public, private, or religious elementary or secondary school (with "school" being determined by State law);

- allowing Education IRAs to be used for home schooling expenses if State and local home schooling requirements are met;

- permitting contributions to an Education IRA to continue beyond the age of 18 in the case of a "special needs beneficiary" (as defined by Treasury Department regulations);

- clarifying that corporations, tax exempt organizations, and other entities are permitted to make contributions to Education IRAs, regardless of the corporation's income;

- allowing taxpayers to claim a HOPE or Lifetime Learning credit and to exclude amounts distributed from gross income through December 31, 2003; and

repealing the excise tax on contributions made during any taxable year in which contributions are also made to a qualified state tuition program on behalf of the same beneficiary.

Qualified Tuition Programs

The bill would modify qualified tuition programs to:

- expand the definition of a "qualified tuition program" to allow private institutions to provide prepaid tuition plans;

- exclude from gross income distributions made after December 31, 1999, from qualified state tuition programs and after December 31, 2003, distributions made by any qualified tuition program; and

- allow distributions from qualified tuition programs to be made on behalf of a student if a HOPE or Lifetime Learning Credit is claimed for that student.

Other Education-related Tax Provisions

The bill also contains other education-related tax provisions that would:

- extend the tax exclusion of employer-provided assistance for undergraduate courses through June 30, 2004, and allow the exclusion for graduate courses beginning on January 1, 2000, through June 30, 2004;

- eliminate the 60-month limit on the deductibility of interest paid on qualified education loans, effective December 31, 1999;

- eliminate the tax on awards under the National Health Corps Scholarship Program and the F. Edward Herbert Armed Forces Health Professions Scholarship Program;

- increase the arbitrage rebate exemption for small government units from $10 million to $15 million on bonds used to finance qualified school construction;

- allow the issuance of tax-exempt private activity bonds for public school facilities; and

- allow the Federal Housing Board to guarantee up to $500 million annually in school construction bonds through the Federal Home Loan Banks.

Revenue Offset Provisions

Among the revenue offsets contained in S. 1134 are provisions that would:

- reduce the carryback period for foreign tax credits from two years to one year and extend the foreign tax credit carryforward from five years to seven years;

- limit the use of the non-accrual experience method of accounting;

- extend certain IRS user fees through September 30, 2009;

- impose a limitation on prefunding of certain employee benefits;

- repeal the installment method for most accrual basis taxpayers; and

- include the streptococcus pneumonia vaccine in the list of taxable vaccines.

Pay-As-You-Go Scoring

According to BASD (Barth), S. 1134 would affect receipts and, therefore, is subject to the pay-as-you-go requirement of the Omnibus Budget Reconciliation Act. OMB and Treasury scoring is under development.

LEGISLATIVE REFERENCE DIVISION
February 23, 2000 -- 12:27 PM