

Coverdell Education Savings Accounts

Notice 2003-53

This notice provides guidance regarding certain reporting requirements and transition rules applicable to Coverdell Education Savings Accounts ("CESAs") described in section 530 of the Internal Revenue Code.

Section 530(h) provides that the trustee or custodian of a CESA shall make reports to the Secretary and to the beneficiary of the CESA with respect to contributions, distributions, and such other matters as the Secretary may require in the time and manner required by the Secretary.

For calendar years before 2003, CESA trustees and custodians were required to report on Form 1099-R (*Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*) gross distributions from CESAs during the calendar year, together with other information including the name, address and TIN of the beneficiary. For calendar years after 2002, CESA trustees and custodians are required to report on Form 1099-Q (*Payments from Qualified Education Programs (Under Sections 529 and 530)*) not only gross distributions from CESAs during the calendar year (as they did on Form 1099-R), but also the earnings and basis portions of the distributions, and certain other information. Gross distributions reportable on Form 1099-Q include transfers from the CESA trustee to a section 529 qualified tuition program (QTP) or to another CESA (trustee-to-trustee transfers).

The Internal Revenue Service (IRS) has received comments concerning changes to the reporting requirements for distributions from CESAs. Commentators have stated that a financial institution that acts as trustee or custodian of CESAs may not have

collected historical account information that would enable the financial institution to determine the basis and earnings portions of gross distributions for a taxable year. Further, even if a financial institution has collected its own historical basis and earnings information for the CESAs it holds, the financial institution may not have the basis and earnings information for amounts that were transferred to the financial institution from CESAs managed by other financial institutions. Commentators also asked whether gross distributions required to be reported on Form 1099-Q include trustee-to-trustee transfers. Commentators indicated that the records of a financial institution that acts as trustee or custodian of CESAs may not establish whether a CESA distribution was sent to a CESA or QTP at another financial institution or directly to the beneficiary. Commentators requested additional time to allow financial institutions to implement appropriate recordkeeping and reporting procedures.

Modifications to reporting for 2003

The IRS is modifying the reporting requirements relating to CESAs. If a trustee or custodian is unable to calculate the earnings and basis portions of a gross distribution from a CESA made in 2003, the trustee or custodian will satisfy the reporting requirements of section 530(h) if the trustee or custodian provides in a timely manner a Form 1099-Q that includes:

- Gross distributions, including the amount of any excess contributions and earnings thereon distributed to a participant during the calendar year, in box 1;

- All other required information except for earnings and basis information in boxes 2 and 3, which should be left blank unless the gross distribution includes a distribution of earnings on excess contributions;
- The amount of any earnings on excess contributions in box 2, computed using the method for calculating the net income attributable to IRA contributions that are distributed as a returned contribution pursuant to section 408(d)(4) of the Code under Notice 2000-39, 2000-2 CB 132, and Proposed section 1.408-11, Income Tax Regulations;
- If earnings on excess contributions are reported in box 2, an indication in the empty box below boxes 5 and 6 that the amount in box 2 includes earnings on excess contributions;
- The fair market value of the CESA (appropriately labeled) as of December 31, 2003, in the empty box below boxes 5 and 6; and
- A cross reference in the empty box below boxes 5 and 6 to Publication 970 (*Tax Benefits for Education*), as provided in the instructions to Form 1099-Q, so that recipients will know how to calculate the earnings portion of the gross distribution.

If the trustee or custodian does not have records indicating whether a gross distribution from a CESA made in 2003 was a trustee-to-trustee transfer, the trustee or custodian may leave box 4 of Form 1099-Q blank.

These modifications allow additional time for CESA trustees or custodians to implement recordkeeping procedures to enable them to report basis and earnings information, and to identify trustee-to-trustee transfers. The IRS expects to publish

further guidance about required reporting for CESA distributions made in 2004 and future years. These modifications remain in effect until further guidance is issued. These modifications do not apply to QTPs, which are required to report distributions, including trustee-to-trustee transfers, in accordance with Notice 2001-81, 2001-2 C.B. 617.

Request for Comments

The IRS recognizes that to report basis and earnings information for 2004 and future years, trustees and custodians that have not previously collected this information with respect to existing CESAs will need to use information from various sources to establish basis and earnings. The IRS invites comments on sources of information that should be considered satisfactory for this purpose, including Forms 5498 (IRA and Coverdell ESA Contribution Information) filed by other trustees or custodians, account statements from financial institutions, and other forms of documentation. The IRS invites comments on an appropriate rule for determining basis and earnings if documentation is not available. The IRS also invites comments on other CESA reporting matters that may be appropriate for additional guidance.

Comments should reference Notice 2003-53. Please send written comments by October 17, 2003, to: CC:PA:RU (Notice 2003-53), room 5226, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington DC 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:RU (Notice 2003-53), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW, Washington DC. Comments may also be sent via e-mail to

notice.comments@irs.counsel.treas.gov. Comments will be available for public inspection.

DRAFTING INFORMATION

The principal author of this notice is Monice Rosenbaum of the Office of Division Counsel/Associate Chief Counsel (Tax Exempt and Government Entities). For further information regarding this notice contact Ms. Rosenbaum at (202) 622-6070 (not a toll-free number).