

Arizona Administrative Register
Notices of Exempt Rulemaking

the proposed rulemaking: Persons directly affected are account owners.

- c. An analysis of the probable costs and benefits from the implementation and enforcement of the proposed rulemaking on the Commission, and on any political subdivision or business directly affected by the proposed rulemaking: The Commission will bear administrative costs in keeping track of the information received from the financial institutions and enforcing the penalties for non-qualified withdrawals. The financial institution's will bear the burden of ensuring that substantiation is provided for withdrawals.
- d. The probable impact of the proposed rulemaking on employment in business, agencies, and political subdivisions of this state affected by the proposed rulemaking: None
- e. A statement of the probable impact of the proposed rulemaking on small business: Some financial institutions are small businesses and will need to bear administrative costs in implementing and maintaining the Program.
- f. A statement of the probable effect on state revenues: No effect is anticipated as this Program is self-supported.
- g. A description of any less intrusive or less costly alternative methods of achieving the purpose of the proposed rulemaking: Due to the nature of the various statutory requirements, less intrusive or less costly alternatives were not available.

9. A description of the changes between the proposed rules, including supplemental notices, and final rules (if applicable):

Not applicable

10. A summary of the principal comments and the agency response to them:

On June 7, 2000, the Commission held a public hearing to consider comments regarding the proposed rules for the Arizona Family College Savings Program. There were not any oral or written comments made by the public. Prior to the June 7th public hearing, the IRS requested that the Commission make the rule changes described below to satisfy the requirements in determining the Program as a Qualified State Tuition Program. The Commission also discussed the proposed rules at its regular meetings on March 29, 2000 and April 4, 2000. The Commission received notification from the Internal Revenue Service on April 28, 2000 that the Arizona Family College Savings Program is a qualified State tuition program, exempt from federal income tax under section 529 of the Internal Revenue Code.

11. Any other matters prescribed by statute that are applicable to the specific agency or to any specific rule or class of rules:

Not applicable

12. Incorporation by reference and their location in the rules:

Not applicable

13. Was this rule previously adopted as an emergency rule?

Not applicable

14. The full text of the rules follows:

TITLE 7. EDUCATION

CHAPTER 3. COMMISSION FOR POSTSECONDARY EDUCATION

ARTICLE 5. ARIZONA FAMILY COLLEGE SAVINGS PROGRAM

R7-3-506. Withdrawals; Reporting of Non-qualified Withdrawals; Penalties

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R7-3-506. Withdrawals; Reporting of Non-qualified Withdrawals; Penalties

A. No change.

B. Withdrawals

1. Qualified Withdrawals

In order to make a qualified withdrawal, the account holder or the account holder's designee must complete a certification, on a form approved by the Commission, declaring that the funds will be used for the purposes set forth in A.R.S. § 15-1871(11). The form shall include a statement advising the designated beneficiary and account owner of

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their obligations to report, in accordance with R7-3-506(B)(3)(c), refunds received from a higher education institution. In addition to the certification, a withdrawal shall be deemed qualified only if:

- a. the financial institution is provided with a copy of an invoice from the higher education institution, and the distribution is made directly to the higher education institution; or
- b. the financial institution is provided with a copy of an invoice from the higher education institution, and the distribution is made in the form of a check payable to both the designated beneficiary and the higher education institution; or
- c. within 30 days following the withdrawal, substantiation that the withdrawal was actually expended for qualified higher education expenses is submitted to the financial institution.

2. **Withdrawal Based on Death, Disability, or Scholarship**

A penalty-free withdrawal may be made as a result of the designated beneficiary's death, disability, or scholarship, if written substantiation thereof is provided. Such written substantiation must come from a party other than the designated beneficiary or the account owner. In the case of a scholarship, the withdrawal may not exceed the amount of the scholarship.

3. **Non-Qualified or Unsubstantiated Withdrawals**

Pursuant to A.R.S. §§ 15-1875 (H), (I), and (J), the Commission has authority to assess penalties for non-qualified withdrawals. If an account holder fails to certify that a withdrawal is qualified or penalty-free, as defined in R7-3-506(B)(1) and (2), above, or if a financial institution has reason to believe that a withdrawal is non-qualified, the financial institution shall withhold from such withdrawal an amount equal to 10% of that portion of that withdrawal which constitutes income under section 72 of the Code. If an account holder seeks to make a withdrawal in accordance with R7-3-506(B)(1)(c) and does not provide the required substantiation at the time of the withdrawal, the withdrawal shall be limited so that the balance remaining in the account is sufficient to pay the 10% of earnings penalty. If the financial institution is not provided with the required substantiation within 30 days, the withdrawal shall be treated as a non-qualified withdrawal, the penalty shall be assessed at that time, and the financial institution shall withdraw the penalty from the account.

- a. If the withdrawal has not been declared, by the party making the withdrawal, to be non-qualified, the amount of any penalty shall be remitted to the Commission with the financial institution's first monthly report following the date that the withdrawal is determined to be non-qualified. If the withdrawal *has* been declared to be non-qualified, the amount of said withholding may be remitted to the Commission with the financial institution's required monthly report.
- b. If the withdrawal has not been declared, by the party making the withdrawal, to be non-qualified, the financial institution shall report any such withholding, in writing, to the Commission with the financial institution's first monthly report following the date that the withdrawal is determined to be non-qualified. The report shall include identification of the account holder, beneficiary, date of withdrawal, amount of withdrawal, and a brief description as to why the financial institution believes the withdrawal to be non-qualified. If the withdrawal *has* been declared to be non-qualified, the report may be submitted to the Commission with the financial institution's required monthly report. The financial institution shall notify the account holder and beneficiary, in writing, of any withholding.
- c. If a qualified withdrawal is made from an account in any calendar year, within 60 days after the end of such year and within 60 days after the end of the following year, any designated beneficiary or account owner who received a partial or total refund from the higher education institution attended by the designated beneficiary or the higher education institution that the designated beneficiary had expected to attend shall provide to the financial institution a signed statement identifying the amount of any refunds received. In addition, the designated beneficiary or account owner shall provide an explanation as to what portion, if any, of the refund is allocable to a qualified withdrawal. If all or a portion of a refund is allocable to a qualified withdrawal, the designated beneficiary (or the account owner) may provide the financial institution with substantiation of qualified higher education expenses for which the refund was used or substantiation that the refund was made by reason of scholarship, or the death, or disability of the designated beneficiary. To the extent that a refund allocable to a qualified withdrawal was not used to pay qualified higher education expenses or made on account of death, disability, or scholarship of the designated beneficiary, it shall be considered a non-qualified withdrawal subject to the penalty described in R7-3-506(B)(3). The financial institution shall withdraw the penalty from the account from which the original qualified withdrawal was made, if sufficient funds are available in the account, or attempt to collect the penalty by billing bill the designated beneficiary or account owner for the penalty, if sufficient funds are not available in the account.

4. **Substantiation Procedures**

Before treating any withdrawal as qualified or penalty-free based on substantiation provided, the financial institution shall review the substantiation to confirm that substantiation is provided for the amount of a withdrawal that the account owner or designated beneficiary asserts is qualified or penalty-free, that the substantiation complies with the program rules, and, in the case of a withdrawal to pay qualified higher education expenses, that the substantiated expenditures

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are of a nature and in amounts that can be treated as qualified higher education expenses. The financial institution may seek additional information from the account owner, the designated beneficiary, or the higher education institution before approving or rejecting substantiation, and the financial institution may seek guidance from staff of the Commission. If the financial institution determines that substantiation is inadequate, it shall promptly notify the account owner and defer making any distribution with respect to any inadequately substantiated request until proper substantiation is provided or the account owner instructs the financial institution to make the requested distribution and either withhold the penalty from the distribution or from other funds in the account.

C. No change.