
11.

Education Savings Bond Program

What's New

Income limits for exclusion reduction increased. For 2009, the amount of your interest exclusion is phased out (gradually reduced) if your filing status is married filing jointly or qualifying widow(er) and your modified adjusted gross income (MAGI) is between \$104,900 and \$134,900. You cannot exclude any of the interest if your MAGI is \$134,900 or more. For 2008, the limits that applied to you were \$100,650 and \$130,650.

For all other filing statuses, your interest exclusion is phased out if your MAGI is between \$69,950 and \$84,950. You cannot exclude any of the interest if your MAGI is \$84,950 or more. For 2008, the limits that applied to you were \$67,100 and \$82,100. See [Effect of the Amount of Your Income on the Amount of Your Exclusion](#), later.

Introduction

Generally, you must pay tax on the interest earned on U.S. savings bonds. If you do not include the interest in income in the years it is earned, you must include it in your income in the year in which you cash in the bonds.

However, when you cash in certain savings bonds under an education savings bond program, you may be able to exclude the interest from income.

Who Can Cash In Bonds Tax Free

You may be able to cash in qualified U.S. savings bonds without having to include in your income some or all of the interest earned on the bonds if you meet the following conditions.

- You pay qualified education expenses for yourself, your spouse, or a dependent for whom you claim an exemption on your return.
- Your modified adjusted gross income (MAGI) is less than \$84,950 (\$134,900 if married filing jointly or qualifying widow(er)).
- Your filing status is not married filing separately.

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 the name of both you and your spouse (as co-owners).

The owner must be at least 24 years old before the bond's issue date. The issue date is printed on the front of the savings bond.



The issue date is not necessarily the date of purchase—it will be the first day of the month in which the bond is purchased (or posted, if bought electronically).

Qualified education expenses. These 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. Qualified education expenses do not include expenses for room and board or for courses involving sports, games, or hobbies that are not part of a degree or certificate granting program.
2. Contributions to a qualified tuition program (QTP) (see [chapter 9](#)).
3. Contributions to a Coverdell education savings account (ESA) (see [chapter 8](#)).

Adjusted qualified education expenses. You must reduce your qualified education expenses by all of the following tax-free benefits.

1. Tax-free part of scholarships and fellowships (see [chapter 1](#)).
2. Expenses used to figure the tax-free portion of distributions from a Coverdell ESA (see [chapter 8](#)).
3. Expenses used to figure the tax-free portion of distributions from a QTP (see [chapter 9](#)).
4. Any tax-free payments (other than gifts or inheritances) received as educational assistance, such as:
 - a. Veterans' educational assistance benefits (see [chapter 1](#)),
 - b. Qualified tuition reductions (see [chapter 1](#)), or
 - c. Employer-provided educational assistance (see [chapter 12](#)).
5. Any expenses used in figuring the American opportunity, Hope, and lifetime learning credits (see [chapters 2, 3, and 4](#)).

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 U.S. 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.

Certain educational institutions located outside the United States also participate in the U.S. Department of Education's Federal Student Aid (FSA) programs.

Dependent for whom you claim an exemption. You claim an exemption for a person if you list his or her name and other required information on Form 1040 (or Form 1040A), line 6c.

Modified adjusted gross income (MAGI). For most taxpayers, MAGI is adjusted gross income (AGI) as figured on their federal income tax return without taking into account this interest exclusion. However, as discussed below, there may be other modifications.

MAGI when using Form 1040A. If you file Form 1040A, your MAGI is the AGI on line 22 of that form figured without taking into account any savings bond interest exclusion and modified by adding back any amount on line 18 (Student loan interest deduction) and line 19 (Tuition and fees deduction).

MAGI when using Form 1040. If you file Form 1040, your MAGI is the AGI on line 38 of that form figured without taking into account any savings bond interest exclusion and modified by adding back any:

1. Foreign earned income exclusion,
2. Foreign housing exclusion,
3. Foreign housing deduction,
4. Exclusion of income by bona fide residents of American Samoa,
5. Exclusion of income by bona fide residents of Puerto Rico,
6. Exclusion for adoption benefits received under an employer's adoption assistance program,
7. Deduction for student loan interest,
8. Deduction for tuition and fees, and
9. Deduction for domestic production activities.

Use the worksheet in the instructions for line 9 of Form 8815 to figure your MAGI. 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. Do not add in the deduction for (7) student loan interest, (8) tuition and fees, or (9) domestic production activities because line 4 of the worksheet already includes these amounts. Enter the total on Form 8815, line 9, as your modified adjusted gross income (MAGI).



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), Supplemental Income and Loss, you must make a special computation of your deductible interest without regard to this exclusion to figure the net royalty income included in your MAGI. See Royalties included in MAGI under Education Savings Bond Program in Publication 550, chapter 1.

Figuring the Tax-Free Amount

If the total you receive when you cash in the bonds is not more than the adjusted qualified education expenses for the year, all of the interest on the bonds may be tax free. However, if the total you receive when you cash in the

bonds is more than the adjusted expenses, only part of the interest may be tax free.

To determine the tax-free amount, multiply the interest part of the proceeds by a fraction. The numerator (top part) of the fraction is the adjusted qualified education expenses (AQEE) you paid during the year. The denominator (bottom part) of the fraction is the total proceeds you received during the year.

Example. In February 2009, Mark and Joan Washington, a married couple, cashed a qualified series EE U.S. savings bond. They received proceeds of \$9,000, representing principal of \$6,000 and interest of \$3,000. In 2009, they paid \$7,650 of their daughter's college tuition. They are not claiming an American opportunity, Hope, or lifetime learning credit for those expenses, and their daughter does not have any tax-free educational assistance. Their MAGI for 2009 was \$80,000.

$$\begin{array}{r} \$3,000 \\ \text{interest} \end{array} \times \frac{\begin{array}{r} \$7,650 \\ \text{AQEE} \end{array}}{\begin{array}{r} \$9,000 \\ \text{proceeds} \end{array}} = \begin{array}{r} \$2,550 \\ \text{tax-free} \\ \text{interest} \end{array}$$

They can exclude \$2,550 of interest in 2009. They must pay tax on the remaining \$450 (\$3,000 – \$2,550) interest.

Effect of the Amount of Your Income on the Amount of Your Exclusion

The amount of your interest exclusion is gradually reduced (phased out) if your MAGI is between \$69,950 and \$84,950 (between \$104,900 and \$134,900 if your filing status is married filing jointly or qualifying widow(er)). You cannot exclude any of the interest if your MAGI is equal to or more than the upper limit.

The phaseout, if any, is figured for you when you fill out Form 8815.

Claiming the Exclusion

Use Form 8815 to figure your education savings bond interest exclusion. Enter your exclusion on line 3 of Schedule B (Form 1040A or 1040), Interest and Ordinary Dividends. Attach Form 8815 to your tax return.

Illustrated Example

The information is the same as in the above [example](#) for Mark and Joan Washington, except they have a modified adjusted gross income of \$118,700. In this example, they can exclude \$1,377 (line 14 of [Form 8815](#) shown on the next page) of interest in 2009.

They must pay tax on the remaining \$1,623 interest (\$3,000 total interest – \$1,377 excluded interest).

**Exclusion of Interest From Series EE and I
U.S. Savings Bonds Issued After 1989
(For Filers With Qualified Higher Education Expenses)
▶ Attach to Form 1040 or Form 1040A.**

Mark & Joan Washington

1	(a)	(b)
	Name of person (you, your spouse, or your dependent) who was enrolled at or attended an eligible educational institution	Name and address of eligible educational institution
	Anna Washington	Jamestown University Normal, VA 20100

If you need more space, attach a statement.

2	Enter the total qualified higher education expenses you paid in 2009 for the person(s) listed in column (a) of line 1. See the instructions to find out which expenses qualify	2	7,650
3	Enter the total of any nontaxable educational benefits (such as nontaxable scholarship or fellowship grants) received for 2009 for the person(s) listed in column (a) of line 1 (see instructions)	3	0
4	Subtract line 3 from line 2. If zero or less, stop . You cannot take the exclusion	4	7,650
5	Enter the total proceeds (principal and interest) from all series EE and I U.S. savings bonds issued after 1989 that you cash during 2009	5	9,000
6	Enter the interest included on line 5 (see instructions)	6	3,000
7	If line 4 is equal to or more than line 5, enter "1.000." If line 4 is less than line 5, divide line 4 by line 5. Enter the result as a decimal (rounded to at least three places)	7	X .850
8	Multiply line 6 by line 7	8	2,550
9	Enter your modified adjusted gross income (see instructions)	9	118,700
	Note: If line 9 is \$84,950 or more if single or head of household, or \$134,900 or more if married filing jointly or qualifying widow(er), stop . You cannot take the exclusion.		
10	Enter: \$69,950 if single or head of household; \$104,900 if married filing jointly or qualifying widow(er)	10	104,900
11	Subtract line 10 from line 9. If zero or less, skip line 12, enter -0- on line 13, and go to line 14	11	13,800
12	Divide line 11 by: \$15,000 if single or head of household; \$30,000 if married filing jointly or qualifying widow(er). Enter the result as a decimal (rounded to at least three places)	12	X .460
13	Multiply line 8 by line 12	13	1,173
14	Excludable savings bond interest. Subtract line 13 from line 8. Enter the result here and on Schedule B (Form 1040A or Form 1040), line 3 ▶	14	1,377

General Instructions

Section references are to the Internal Revenue Code.

Purpose of Form

If you cashed series EE or I U.S. savings bonds in 2009 that were issued after 1989, you may be able to exclude from your income part or all of the interest on those bonds. Use this form to figure the amount of any interest you may exclude.

Who Can Take the Exclusion

You can take the exclusion if all four of the following apply.

1. You cashed qualified U.S. savings bonds in 2009 that were issued after 1989.
2. You paid qualified higher education expenses in 2009 for yourself, your spouse, or your dependents.
3. Your filing status is any status except married filing separately.
4. Your modified AGI (adjusted gross income) is less than: \$84,950 if single or head of household; \$134,900 if married filing jointly or qualifying widow(er). See the instructions for line 9 to figure your modified AGI.

U.S. Savings Bonds That Qualify for Exclusion

To qualify for the exclusion, the bonds must be series EE or I U.S. savings bonds issued after 1989 in your name, or, if you are married, they may be issued in your name and your spouse's name. Also, you must have been age 24 or older before the bonds were issued. A bond bought by a parent and issued in the name of his or her child under age 24 does not qualify for the exclusion by the parent or child.

Recordkeeping Requirements

Keep the following records to verify interest you exclude.

- Bills, receipts, canceled checks, or other documents showing you paid qualified higher education expenses in 2009.
- A written record of each post-1989 series EE or I bond that you cash. Your record must include the serial number, issue date, face value, and total redemption proceeds (principal and interest) of each bond. You can use Form 8818, Optional Form To Record Redemption of Series EE and I U.S. Savings Bonds Issued After 1989, as your written record.