

# CREDIT UNION COVERDELL ESA TRUST AGREEMENT (rev. 3/2002)

## 1. CONTRIBUTIONS

The Trustee may accept additional cash contributions, provided the Designated Beneficiary has not attained the age of 18 as of the date such contributions are made. Contributions by an individual contributor may be made for the tax year of the Designated Beneficiary by the due date of the beneficiary's tax return for that year (excluding extensions). Total contributions that are not rollover contributions described in section 530(d)(5) are limited to \$2,000 for the tax year. In the case of an individual contributor, the \$2,000 limitation for any year is phased out between modified adjusted gross income (MAGI) of \$95,000 and \$110,000. For married individuals filing jointly, the phase-out occurs between MAGI of \$190,000 and \$220,000. MAGI is defined in section 530(c)(2).

## 2. INVESTMENT LIMITATIONS

No part of the Trust account funds may be invested in life insurance contracts, nor may the assets of the Trust account be commingled with other property, except in a common trust fund or a common investment fund (within the meaning of section 530(b)(1)(D)).

## 3. REQUIRED DISTRIBUTIONS

**3.1 At Age 30.** Any balance to the credit of the Designated Beneficiary on the date on which he or she attains age 30 shall be distributed to him or her within 30 days of such date.

**3.2 Following Death.** Any balance to the credit of the Designated Beneficiary shall be distributed within 30 days of his or her death unless the Death Beneficiary is a family member of the Designated Beneficiary and is under the age of 30 on the date of death. In such case, that family member shall become the Designated Beneficiary as of the date of death.

## 4. INVESTMENT DIRECTIONS

The Grantor shall have the power to direct the Trustee regarding the investment of the initial amount assigned to the Trust (including earnings thereon) in the investment choices offered by the Trustee. The Responsible Individual, however, shall have the power to redirect the Trustee regarding the investment of such amounts, as well as the power to direct the Trustee regarding the investment of all additional contributions (including earnings thereon) to the trust. In the event that the Responsible Individual does not direct the Trustee regarding the investment of additional contributions (including earnings thereon), the initial investment direction of the Grantor also will govern all additional contributions made to the Trust account until such time as the Responsible Individual otherwise directs the Trustee. Unless otherwise provided in this agreement, the Responsible Individual also shall have the power to direct the Trustee regarding the administration, management, and distribution of the account.

## 5. RESPONSIBLE INDIVIDUAL

The "Responsible Individual" named by the Grantor shall be a parent or guardian of the Designated Beneficiary. The Trust shall have only one Responsible Individual at any time. If the Responsible Individual becomes incapacitated or dies while the Designated Beneficiary is a minor under state law, the successor Responsible Individual shall be the person named to succeed in that capacity by the preceding Responsible Individual in a witnessed writing or, if no successor is so named, the successor Responsible Individual shall be the Designated Beneficiary's other parent or successor guardian. If a family member under the age of majority under state law becomes the Designated Beneficiary by reason of being a Death Beneficiary, the Responsible Individual shall be such Designated Beneficiary's parent or guardian.

## 6. CHANGING THE DESIGNATED BENEFICIARY

The Responsible Individual may not change the beneficiary designated under this agreement to another member of the Designated Beneficiary's family described in section 529(e)(2).

## 7. REPORTING

**7.1** The Grantor agrees to provide the Trustee with the information necessary for the Trustee to prepare any reports required under section 530(h).

**7.2** The Trustee agrees to submit to the Internal Revenue Service (IRS) and Responsible Individual the reports prescribed by the IRS.

## 8. CONTROLLING SECTIONS

Notwithstanding any other articles which may be added or incorporated, the provisions of Articles 1 through 3 will be controlling. Any additional articles inconsistent with section 530 and the related regulations will be invalid.

## 9. AMENDMENTS

This agreement will be amended from time to time to comply with the provisions of the Code and related regulations. Other amendments may be made with the consent of the Grantor and Trustee whose signatures appear on the application form.

The Trustee may also amend this agreement at any time by sending the Responsible Individual a copy of the amendment. An amendment will become effective 30 days after it is mailed to the Responsible Individual, unless the Trustee receives an objection to the amendment from the Responsible Individual.

The Grantor may amend the election on whether the Designated Beneficiary becomes the Responsible Individual when reaching the age of majority. An amendment to prevent this from happening must be made before the Designated Beneficiary reaches the age of majority. An amendment to cause this to happen can be made at any time.

## 10. GENERAL PROVISIONS

**10.1 Notices and Reports.** The Responsible Individual will mail notices to the Trustee or to an agent specified by the Trustee. The Trustee will mail notices and reports to the last known address of the recipient according to its records. If the Trustee does not receive a notice that information in a report appears to be inaccurate within 60 days after mailing the report, it may treat the information contained in the report as accurate for all purposes.

**10.2 Trustee's Liability.** The Trustee will not be liable for any loss or damage unless it is caused by a violation of an express provision of this agreement, or by a lack of good faith in acting in compliance with this agreement.

**10.3 Trustee's Fees.** The Trustee may charge reasonable fees for its services, and deduct such fees from the assets of the ESA.

**10.4 Change of Trustee.** The Trustee can substitute a successor Trustee, and it will do so if it receives notice from the IRS that such substitution is required to protect the tax status of this ESA. If the Trustee resigns without substituting another Trustee or the Trustee is removed by the governmental agency that regulates it, then CUNA Mutual Group, Madison, Wisconsin, will appoint a successor Trustee and notify the Responsible Individual of the change. A successor Trustee will have all of the same duties and rights granted to the original Trustee under this agreement. A successor Trustee will not be liable for any act or omission of a predecessor Trustee.

**10.5 Security Interest Waiver.** The Trustee waives the provisions of any written contract that grants it a security interest in this ESA.

## 11. DEATH BENEFICIARIES

### 11.1 Naming Your Death Beneficiaries.

The Responsible Individual may name a primary and a secondary Death Beneficiary, and may change the Death Beneficiaries at any time. The original selection and any subsequent changes can only be made by completing and signing a death beneficiary selection form that we will provide upon request; and we will not be responsible for following instructions on signature cards or on any other documents. A Death Beneficiary selection remains effective after the amendment of the terms of this agreement.

**11.2 No Named Death Beneficiaries.** If none of the named Death Beneficiaries are alive following the death of the Designated Beneficiary or if the Trustee has not received a death beneficiary selection form, then: (a) The Designated Beneficiary's spouse will be the Death Beneficiary, or (b) If the Designated Beneficiary is not survived by a spouse, then the assets of this ESA will be distributed to the Designated Beneficiary's estate.

## CREDIT UNION COVERDELL ESA DISCLOSURE STATEMENT (rev. 3/2002)

Beginning January 1, 2002, taxpayers may deposit up to \$2,000 per year into a Coverdell Education Savings Account (ESA) for a child under age 18. Parents, grandparents, other family members, friends, and a child him/herself may contribute to the child's Coverdell ESA, provided that the total contributions for the child during the taxable year do not exceed the \$2,000 limit. Amounts deposited in the account grow tax-deferred until distributed, and the child will not owe tax on any withdrawal from the account if the child's qualified education expenses at an eligible educational institution for the year equal or exceed the amount of the withdrawal. If the child does not need the money for education, the account balance can be rolled over to the Coverdell ESA of certain family members who can use it for their education. A portion of amounts withdrawn from a Coverdell ESA that exceed the child's qualified education expenses in a taxable year is subject to income tax and to an additional tax of 10 percent.

### **Q1: What is a Coverdell ESA?**

A1: A Coverdell ESA is a trust or custodial account that is created or organized in the United States exclusively for the purpose of paying the qualified education expenses of the Designated Beneficiary of the account. The account must be designated as a Coverdell ESA when it is created in order to be treated as a Coverdell ESA for tax purposes.

### **Q2: For whom may a Coverdell ESA be established?**

A2: A Coverdell ESA may be established for the benefit of any child under age 18. Contributions to the Coverdell ESA will not be accepted after the Designated Beneficiary reaches his/her 18th birthday. The IRS is authorized to issue regulations allowing contributions after age 18 for special needs beneficiaries.

### **Q3: Where may an individual open a Coverdell ESA?**

A3: An individual may open a Coverdell ESA with any bank, or other entity that has been approved to serve as a nonbank trustee or custodian of an individual retirement account (IRA), and the bank or entity is offering Coverdell ESAs. Other entities that wish to offer Coverdell ESAs but are not approved to serve as IRA trustees or custodians may seek approval by following the same IRS procedures used for approval of other IRA nonbank trustees. See Notice 97-57, 1997-43 I.R.B. (October 27, 1997).

### **Q4: How much may be contributed to a child's Coverdell ESA?**

A4: Up to \$2,000 per year in aggregate contributions may be made for the benefit of any child. The contributions may be placed in a single Coverdell ESA or in multiple Coverdell ESAs. Contributions prior to 2002 were subject to a \$500 per year limit.

### **Q5: When can Coverdell ESA contributions be made for a child?**

A5: Regular contributions can be made to a Coverdell ESA for a year up until the time prescribed by law for filing the tax return for that year (excluding extensions). If a calendar tax year is used, the deadline for making a regular Coverdell ESA contribution is April 15 of the following year. If April 15 is a weekend or a legal holiday, then the deadline is the next business day. A contribution can be made on or before this deadline, even if the tax return has already been filed for the tax year. In such a situation, an amended return should be filed on IRS Form 1040X to reflect the contribution.

There is no special time during this period for making a contribution. Contributions may be made periodically throughout the year, or in a single contribution for the year.

### **Q6: What happens if more than \$2,000 is contributed to a Coverdell ESA on behalf of a child in a calendar year?**

A6: Aggregate contributions for the benefit of a particular child in excess of \$2,000 for a calendar year are treated as excess contributions. If the excess contributions (and any earnings attributable to them) are not withdrawn from the child's account (or accounts) by May 31 of the year after the year for which the contributions were made, the excess contributions are subject to a 6 percent excise tax for each year the excess amount remains in the account. The May 31 deadline is extended to October 15 if the Designated Beneficiary timely filed an income tax return for the year and correctly reports the contributions and the withdrawal.

### **Q7: May contributions other than cash be made to a child's Coverdell ESA?**

A7: No. Coverdell ESAs are permitted to accept contributions made in cash only.

### **Q8: May contributors take a deduction for contributions made to a Coverdell ESA?**

A8: No.

### **Q9: Are there any restrictions on who can contribute to a Coverdell ESA?**

A9: Any individual may contribute up to \$2,000 to a child's Coverdell ESA if the individual's modified adjusted gross income for the taxable year is no more than \$95,000 (\$190,000 for married taxpayers filing jointly). The \$2,000 maximum contribution per child is gradually reduced for individuals with modified adjusted gross income between \$95,000 and \$110,000 (between \$190,000 and \$220,000 for married taxpayers filing jointly). For example, an unmarried taxpayer with modified adjusted gross income of \$96,500 in a taxable year could make a maximum contribution per child of \$1,800 for that year. Taxpayers with modified adjusted gross income above \$110,000 (\$220,000 for married taxpayers filing jointly) cannot make contributions to anyone's Coverdell ESA.

### **Q10: May a child contribute to his/her own Coverdell ESA?**

A10: Yes.

### **Q11: Does a taxpayer have to be related to the Designated Beneficiary in order to contribute to the Designated Beneficiary's Coverdell ESA?**

A11: No.

### **Q12: How many Coverdell ESAs may a child have?**

A12: There is no limit on the number of Coverdell ESAs that may be established designating a particular child as beneficiary. However, in any given taxable year the total aggregate contributions to all the accounts designating a particular child as beneficiary may not exceed \$2,000.

### **Q13: May a Designated Beneficiary take a tax-free withdrawal from a Coverdell ESA to pay qualified education expenses if the Designated Beneficiary is enrolled less than full-time at an eligible educational institution?**

A13: Yes. Whether the Designated Beneficiary is enrolled full-time, half-time, or less than half-time, he/she may take a tax-free withdrawal to pay qualified education expenses.

### **Q14: What happens when a Designated Beneficiary withdraws assets from a Coverdell ESA to pay for college?**

A14: Generally, the withdrawal is tax-free to the Designated Beneficiary to the extent the amount of the withdrawal does not exceed the Designated Beneficiary's qualified education expenses.

## CREDIT UNION COVERDELL ESA DISCLOSURE STATEMENT (continued)

### Q15: What are “qualified education expenses”?

A15: “Qualified education expenses” mean qualified elementary and secondary education expenses (Q&A16) and qualified higher education expenses (Q&A17).

### Q16: What are “qualified elementary and secondary education expenses”?

A16: Qualified elementary and secondary education expenses are the total of:

- (1) expenses for tuition, fees, academic tutoring, books, supplies, equipment and special needs services (for a special needs beneficiary) incurred in connection with enrollment or attendance of the Designated Beneficiary as an elementary or secondary school student at a public, private, or religious school as determined under state law;
- (2) expenses for room and board, uniforms, transportation, and supplementary items and services (e.g., extended day programs) required or provided by a school in connection with enrollment or attendance; and
- (3) purchase of computer technology or equipment or Internet access to be used by the beneficiary and his or her family while the beneficiary is in elementary or secondary school, except this does not include software for sports, games or hobbies unless the software is predominantly educational.

### Q17: What are “qualified higher education expenses”?

A17: Qualified higher education expenses are the expenses for tuition, fees, books, supplies, and equipment required for the enrollment or attendance of the Designated Beneficiary at an eligible higher educational institution.

Qualified higher education expenses also include amounts contributed to a qualified state tuition program.

Qualified higher education expenses also include room and board (generally the school's posted room and board charge, or \$2,500 per year for students living off-campus and not at home) if:

- (1) for at least one academic period (e.g., semester, trimester, quarter) beginning during the calendar year, the student is enrolled at least half-time in a program leading to a degree, certificate, or other recognized educational credential, and

- (2) the student is free of any conviction for a Federal or State felony offense consisting of the possession or distribution of a controlled substance.

A student will be considered to be enrolled at least half-time if the student is enrolled for at least half the full-time academic workload for the course of study the student is pursuing as determined under the standards of the institution where the student is enrolled. The institution's standard for a full-time workload must equal or exceed the standards established by the Department of Education under the Higher Education Act and set forth in 34 C.F.R. section 674.2(b).

An eligible educational institution is any college, university, vocational school, or other postsecondary educational institution that is described in section 481 of the Higher Education Act of 1965 (20 U.S.C. 1088) and, therefore, eligible to participate in the student aid programs administered by the Department of Education. This category includes virtually all accredited public, nonprofit, and proprietary postsecondary institutions. (The same eligibility requirements for institutions apply for the Hope Scholarship Credit, the Lifetime Learning Credit, and early withdrawals from IRAs for qualified education expenses.)

### Q18: What happens if a Designated Beneficiary withdraws an amount from a Coverdell ESA but does not have any qualified education expenses to pay in the taxable year he/she makes the withdrawal?

A18: Generally, if a Designated Beneficiary withdraws an amount from a Coverdell ESA and does not have any qualified education expenses during the taxable year, a portion of the distribution is taxable. The taxable portion is the portion that represents earnings that have accumulated tax-deferred in the account. The taxable portion of the distribution is also subject to a 10 percent additional tax unless an exception applies.

### Q19: Is a distribution from a Coverdell ESA taxable if the distribution is contributed to another Coverdell ESA?

A19: Any amount distributed from a Coverdell ESA and rolled over to another Coverdell ESA for the benefit of the same Designated Beneficiary or certain members of the Designated Beneficiary's family is not taxable. An amount is rolled over if it is paid to another Coverdell ESA on a date within 60 days after the date of

the distribution. Members of the Designated Beneficiary's family include the Designated Beneficiary's children and their descendants, stepchildren and their descendants, siblings and their children, parents and grandparents, stepparents, and spouses of all the foregoing. The \$2,000 annual contribution limit to Coverdell ESAs does not apply to these rollover contributions. For example, an older brother who has \$5,000 left in his Coverdell ESA after he graduates from college can roll over the full \$5,000 balance to a Coverdell ESA for his younger sister who is still in high school without paying any tax on the transfer.

### Q20: What happens to the assets remaining in a Coverdell ESA after the Designated Beneficiary finishes his/her postsecondary education?

A20: There are two options. The amount remaining in the account may be withdrawn for the Designated Beneficiary. The Designated Beneficiary will be subject to both income tax and the additional 10 percent tax on the portion of the amount withdrawn that represents earnings if the Designated Beneficiary does not have any qualified education expenses in the same taxable year he/she makes the withdrawal. Alternatively, if the amount in the Designated Beneficiary's Coverdell ESA is withdrawn and rolled over (as described in Q&A19 of this section) to another Coverdell ESA for the benefit of a member of the Designated Beneficiary's family, the amount rolled over will not be taxable.

### Q21: Rather than rolling over money from one Coverdell ESA to another, may the Designated Beneficiary of the account be changed from one child to another without triggering a tax?

A21: No, not under the Credit Union Coverdell ESA Trust Agreement.

### Q22: May a student or the student's parents claim the Hope Scholarship Credit or Lifetime Learning Credit for the student's expenses in a taxable year in which the student receives money from a Coverdell ESA on a tax-free basis?

A22: Yes, but expenses used to claim the Hope Scholarship Credit and Lifetime Learning Credit may not also be used to take a tax-free withdrawal from a Coverdell ESA.

### Q23: May contributions be made to both a qualified tuition program and a Coverdell ESA on behalf of the same Designated Beneficiary in the same taxable year?

A23: Yes.