Module H

IRC § 144(b) – Qualified Student Loan Bonds

IRC § 150(d) – Qualified Scholarship Funding Bonds

Overview

Introduction

Module H continues the text's discussion of qualified private activity bonds by focusing on qualified student loan and scholarship funding bonds.

Objectives

At the end of this lesson you will be able to:

- Define a qualified student loan bond.
- Explain the special arbitrage rules governing issues financing student loans.
- Define qualified scholarship funding bonds.

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Qualified Student Loan Bonds

Use of Proceeds

IRC § 144(b)(1) provides that a qualified student loan bond means any bond if:

- 90 percent or more of the net proceeds of the issue are to be used directly or indirectly to make or finance student loans under the Guaranteed Student Loan program or Parents Loans for Undergraduate Students program under the *Higher Education Act of 1965* (See IRC § 144(b)(1)(A).)

OR

- 95 percent or more of the net proceeds of the issue of which are to be used directly or indirectly to make or finance student loans under a program of general application approved by the state, as long as, the loan does not exceed the difference between the total cost of attendance and other forms of student assistance for which the student may be eligible.

(See IRC § 144(b)(1)(B).)

State Residency

According to IRC § 144(b)(3), for the loan to be qualified under IRC § 144(b)(1), either:

- the student must be a resident of the state from which the volume cap allocation for the related qualified student loan bonds was derived, OR

- the student must be enrolled at an educational institution located in such state.

Non-discrimination

Proceeds of bonds issued under IRC § 144(b)(1)(A) may not be used to finance loans under a program which discriminates on the basis of the location of the educational institution in which the student is enrolled.

Arbitrage Rules

Temporary Period

- IRC § 148(c)(2)(A) provides that proceeds of an issue that are to be used to finance student loans under IRC § 144(b)(1)(A) may be invested without regard to yield restriction for an initial temporary period equal to 6 months. (See also Treas. Reg. § 1.148-2(e)(4)(i).)

- For bonds issued prior to January 1, 1989, this temporary period was 18 months.

Any proceeds received as a result of a repayment of a loan may be invested without regard to yield restriction for a temporary period equal to 3 months. (See IRC § 148(c)(2)(B) and Treas. Reg. § 1.148-2(e)(4)(ii).)

Yield on the Student Loan

The yield on the student loans that are considered program investments may not exceed 2 percentage points over the yield on the related issue of bonds. (See Treas. Reg. § 1.148-2(d)(2)(iv).)

For definition of program investment, see Module M and Treas. Reg. § 1.148-1(b).

Note

There are other arbitrage and rebate rules applicable to qualified student loan bonds that are described in Module M.

Qualified Scholarship Funding Bonds

Definition

IRC § 150(d) provides that a qualified scholarship funding bond is a bond issued by a corporation which:

(i) is a not-for-profit corporation established and operated exclusively for purpose of acquiring student loans incurred under the *Higher Education Act of 1965*, and

(ii) is organized at the request of a state or political subdivision of the state.

The corporation should be required by its organizational documents or by state law to devote any income to the purchase of additional student loans or to pay over its income to the United States.

Treated as State or Local Bond

A bond issued by a corporation described above is treated as a state or local bond.

Loan Origination Services

The corporation described above must be operated exclusively for acquiring student loans.

- In PLR 9407016, a corporation which provided *loan origination* services and loan servicing services in its operations, was not described in IRC § 150(d) because it performed loan origination services.
- However, in PLR 9126019, a corporation was permitted to provide *loan-servicing* services.

Summary of Module H

Review of Module H

Module H discussed qualified student loan bonds and qualified scholarship funding bonds.

Generally, qualified student loan bonds are bonds where:

- 90 percent or more of the net proceeds are used to finance student loans under one of two programs provided by the *Higher Education Act of 1965*, OR
- 95 percent or more of the net proceeds are used to finance student loans under a program approved by the state.

In addition to the generally applicable arbitrage and rebate rules, special rules also apply to these bonds.

A qualified scholarship funding bond is a bond issued by a corporation which:

- is a not-for-profit corporation established and operated exclusively for the purpose of acquiring student loans incurred under the *Higher Education Act of 1965*, AND
- is organized at the request of a state or political subdivision of the state.

A qualified scholarship fund bond is a private activity bond which must be <u>qualified</u> for interest to be paid on the bond to be excludable from gross income. Therefore, these bonds must also be analyzed under the rules for qualified student loan bonds contained in IRC § 144(b).

Preview of Module I

Module I continues the text's discussion of qualified private activity bonds by discussing qualified 501(c)(3) bonds. Although these bonds are subject to the rules of qualified private activity bonds, in many ways they receive favored status, being treated like governmental bonds.

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