NOTICES OF EXEMPT RULEMAKING

The Administrative Procedure Act requires the *Register* publication of the rules adopted by the state's agencies under an exemption from all or part of the Administrative Procedure Act. Some of these rules are exempted by A.R.S. §§ 41-1005 or 41-1057; other rules are exempted by other statutes; rules of the Corporation Commission are exempt from Attorney General review pursuant to a court decision as determined by the Corporation Commission.

NOTICE OF EXEMPT RULEMAKING

TITLE 7. EDUCATION

CHAPTER 3. COMMISSION FOR POSTSECONDARY EDUCATION

PREAMBLE

1. Sections Affected — **Rulemaking Action**

Sections Affected	Rulemaking Action
R7-3-501	Amend
R7-3-502	Amend
R7-3-505	Amend
R7-3-506	Amend
R7-3-507	Amend

2. The specific authority for the rulemaking, including both the authorizing statute (general) and the statutes the rules are implementing (specific):

Authorizing statute: A.R.S. § 15-1852(C)

Implementing statutes: A.R.S. §§ 15-1873 *et seq.*

3. The effective date of the rules:

August 14, 2003

4. A list of all previous notices appearing in the Register addressing the exempt rules:

Notice of Rulemaking Docket Opening: 9 A.A.R. 1562, May 23, 2003

Notice of Proposed Rulemaking: 9 A.A.R. 2158, July 3, 2003

5. The name and address of agency personnel with whom persons may communicate regarding the rulemaking:

Name: Verna L. Allen, Executive Director

Address: 2020 N. Central Avenue, Suite 550
Phoenix, AZ 85004

Telephone: (602) 258-2435

Fax: (602) 258-2483

6. An explanation of the rules, including the agency's reasons for initiating the rules:

The Commission for Postsecondary Education's purpose in promulgating the proposed rule amendments is to make some necessary technical changes to the Arizona Family College Savings Program rules to bring them into conformity with § 529 of the Internal Revenue Code (Code) and IRS Notices promulgated pursuant to § 529 of the Code. Additionally, the formula for contribution or account balance limitations is amended to increase this cap.

7. A reference to any study relevant to the rules that the agency reviewed and either relied on or did not rely on in its evaluation of or justification for the rules, where the public may obtain or review each study, all data underlying each study, and any analysis of each study and other supporting material:

None

8. A showing of good cause why the rules are necessary to promote a statewide interest if the rules will diminish a previous grant of authority of a political subdivision of this state:

Not applicable

9. The summary of the economic, small business, and consumer impact:

a. An identification of the proposed rulemaking: Arizona Family College Savings Plan, R7-3-501(G), R7-3-502(B), R7-3-505(1), R7-3-506(B)(a) and (b), R7-3-506(3)(b) and (c), R7-3-506(4), and R7-3-507(C)(1) through (3).

b. An identification of the persons who will be directly affected by, bear the costs of, or directly benefit from 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 any administrative costs as a consequence of the proposed rulemaking.

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: None

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 are not available.

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

Not applicable

11. A summary of the comments made regarding the rules and the agency response to them:

On April 30, 2003, the Commission had discussions and approved the Notice of Rulemaking Docket Opening for the AFCSP Program Rules amendments for technical changes and amended change to the account balance limitations formula. On June 11, 2003, the Commission held a public meeting for review and approval of the proposed rulemaking amendment regarding technical changes and amended change to the account balance limitations formula. Also, on August 13, 2003, the Commission held another meeting for public comments and approved the final amendment language for R7-3-501, R7-3-502, R7-3-505, R7-3-506, and R7-3-507.

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

Not applicable

13. Incorporations by reference and their location in the rules:

Not applicable

14. Were these rules previously adopted as emergency rules?

No

15. The full text of the rules follows:

TITLE 7. EDUCATION

CHAPTER 3. COMMISSION FOR POSTSECONDARY EDUCATION

ARTICLE 5. ARIZONA FAMILY COLLEGE SAVINGS PROGRAM

ARTICLE 5. ARIZONA FAMILY COLLEGE SAVINGS PROGRAM

R7-3-501. Definitions

A. "Account Year" means the period beginning on October 1 and ending on September 30 of each year.
B. "A.R.S." means Arizona Revised Statutes.
C. "Cash" means currency, bills and coin in circulation, or converting a negotiable instrument to cash by endorsing and presenting to a financial institution for deposit. An automatic transfer, cashier's check, certified check, money order, payroll deposit, traveler's check, personal check, and wire transfer will be treated as cash. Deposits will also be accepted by credit card.
D. "Code" means the Internal Revenue ~~Service~~ Code of 1986, as amended, or the corresponding provision of any future United States Internal Revenue law.
E. "Commission" means the Commission for Postsecondary Education as defined in A.R.S. § 15-1871.
F. "Committee" means the Family College Savings Program Oversight Committee as defined in A.R.S. § 15-1871.

~~**G.** "Higher education institution" means a higher education institution as defined in A.R.S. § 15-1871(7), provided that, solely for the purposes of determining whether a withdrawal or distribution is subject to a penalty under R7-3-506, the term shall not include any institution that is not also an "eligible educational institution" as defined in Code § 529(e)(5).~~

G. "Distributee" means the designated beneficiary or the account owner who receives or is treated as receiving a distribution from an account. If a distribution is made directly to the designated beneficiary or to an eligible educational institution for the benefit of the designated beneficiary, the designated beneficiary is the distributee. In all other circumstances, the account owner is the distributee.

H. "Eligible educational institution" means an institution of higher education that qualifies under § 529 of the Code as an eligible educational institution.

~~**H.**~~**I.** "Negotiable instrument" means negotiable instrument as defined in A.R.S. § 47-3104.

~~**I.**~~**J.** "Qualified Tuition Program" means a qualified tuition program as defined in § 529 of the Code.

R7-3-502. Fees

A. Application fee. The application fee is $10. Application fees shall be forwarded to the Commission at the end of the month in which the account is opened. A financial institution may waive the application fee but will nevertheless be responsible for tendering to the Commission $10 for each new account opened; said tender to be made at the end of the month in which the account is opened. The Committee shall review the application fee every 24 months and recommend to the Commission whether the application fee should be adjusted.

B. Administrative fee. For each account opened, the financial institution shall pay to the Commission a one-time fee of $3 at the end of the month in which the account was opened. The Committee shall review the administrative fee every 24 months and recommend to the Commission whether the administrative fee should be adjusted. The financial institution shall not charge the account ~~holder~~ owner the administrative fee.

C. Marketing fee. The financial institution shall pay to the Commission an annual marketing fee. The marketing fee shall be paid at the beginning of each calendar year as a $200 flat fee. If a financial institution begins participating in the Arizona Family College Savings Program after the beginning of a calendar year, the financial institution shall pay a pro-rated marketing fee based upon the month in which it begins participation in the Program regardless of the day in the month. The Committee shall review the marketing fee every 12 months and recommend to the Commission whether the marketing fee should be adjusted. The Commission may review the marketing fee prior to the committee's required 12-month review. The financial institution shall not charge the account ~~holder~~ owner the marketing fee.

R7-3-505. Account Balance Limitations

A. For each designated beneficiary, the balance in all qualified tuition programs, as defined in § 529 of the Code, shall not exceed the lesser of:
1. The product (rounded down to the nearest multiple of $1000) of 7 and the average one year's undergraduate tuition, fees, room and board at the ten independent four year ~~higher education institutions~~ eligible educational institutions as measured and last published by the College Board's Independent College 500 Index that have the largest total direct charges. For purposes of this subsection, "total direct charges" means the charges determined for each eligible educational institution by multiplying the eligible educational institution's undergraduate enrollment by the reported tuition, fees, room and board for an on-campus student at the eligible educational institution; or
2. The cost in current dollars of qualified higher education expenses the account ~~holder~~ owner reasonably anticipates the designated beneficiary will incur.

B. No person shall make any contribution to a qualified tuition program during an account year that would cause the sum of the account balances in all qualified tuition programs of the designated beneficiary as of the first day of the account year plus contributions made during the account year less withdrawals during the account year to or from any such account to exceed the maximum allowable balance set forth in subsection (A). Any excess contributions with respect to a designated beneficiary shall be promptly withdrawn as a non-qualified withdrawal or transferred to another account in accordance with A.R.S. § 15-1875(F).

C. No financial institution shall accept for deposit in any account a contribution if the contribution would cause the sum of the values (as of the beginning of an account year) of all qualified tuition programs of the designated beneficiary that are managed by the financial institution and contributions to such accounts less withdrawals from such accounts during the account year to exceed the maximum allowable balance set forth in subsection (A).

D. Each year, the Commission shall review the amounts set forth in subsection (A).

E. Persons making a contribution to an account shall certify that as to the account's designated beneficiary, and to the best of the contributor's knowledge, the contribution shall not cause the balances in all qualified tuition programs to exceed the account balance limitations described in subsection (A).

F. If the Commission determines that contributions have been made to program accounts in violation of subsection (B) or (C), it shall notify the designated beneficiary and the account owners of all accounts of such designated beneficiary. The account owners shall have 60 days after receipt of such notice to reduce the balances of the qualified tuition programs through distributions and/or changes in beneficiaries to a level less than or equal to the maximum account balance described in subsection (A). If the balances are not appropriately reduced, the Commission will disqualify such accounts in reverse order of their date of opening until the sum of the balances in the accounts does not exceed the maximum allowable balance set forth in subsection (A). This subsection shall not apply to any contribution made at a time when such contributions did not cause the account balance limits to be exceeded.

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

A. An account owner may withdraw funds from an account at any time. The designated beneficiary of an account shall not have any authority to withdraw funds from an account unless the account is structured to give the designated beneficiary such right of withdrawal upon matriculation or upon incurring qualified higher education expenses.

B. Withdrawals

1. Qualified Withdrawals.
   In order to make a qualified withdrawal, the account ~~holder~~ owner or the account ~~holder's~~ owner'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 their obligations to report, in accordance with R7-3-506(B)(3)(c), refunds received from ~~a higher education~~ ~~institution~~ an eligible educational 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~~ eligible educational institution, and the distribution is made directly to the ~~higher education institution~~ eligible educational institution; or
   b. The financial institution is provided with a copy of an invoice from the ~~higher education~~ ~~institution~~ eligible educational institution, and the distribution is made in the form of a check payable to both the designated beneficiary and the ~~higher education~~ ~~institution~~ eligible educational 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~~ owner 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 § 72 of the Code. If an account ~~holder~~ owner 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 institutions'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~~ owner, 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~~ owner 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~~ eligible educational institution attended by the designated beneficiary or the ~~higher education institution~~ eligible educational 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 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 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~~ <u>eligible educational institution</u> 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.

5. Distributions Made after December 31, 2001

   R7-3-506(B)(1) through (4) shall not apply to any withdrawals made after December 31, 2001, except to the extent that any provision contained therein is required for the Family College Savings Program to qualify as a qualified tuition program under § 529 of the Code. A financial institution shall not be required to collect a penalty on any withdrawal made after December 31, 2001. Withdrawals may be made pursuant to forms prepared or used by the financial institution and meeting the requirements of R7-3-501 through R7-3-507, if any, and any requirements for the Family College Savings Program to qualify as a qualified tuition program under § 529 of the Code. To the extent that A.R.S. § 15-1875 requires provisions that will generally enable the Commission to determine whether withdrawals are qualified or nonqualified withdrawals, a financial institution shall require an account owner to state whether the account owner expects that the withdrawal will be a qualified or nonqualified withdrawal.

C. The account ~~holder~~ <u>owner</u> may dispute any withholding made by a financial institution under subsection (B) by submitting written notice, to the Commission, within 30 days from the date of such withholding. The Commission shall make a written determination regarding the dispute within 30 days of the receipt of its notice from the account ~~holder~~ <u>owner</u>. If the account ~~holder~~ <u>owner</u> disagrees with the Commission's determination, the matter shall be adjudicated in accordance with A.R.S. § 41-1092 et seq.

R7-3-507. Oversight of Financial Institutions

A. Disclaimer of state liability. Every document pertaining to the Family College Savings Program shall clearly indicate that "The account is not insured by the state of Arizona and neither the principal deposited nor the investment return is guaranteed by the state of Arizona." A rubber stamp may be used to imprint this language on deposit slips, account statements, payroll stubs, or other documents pertaining to the Family College Savings Program. This language may also be handwritten or typed or provided by any other method to facilitate compliance.

B. No Investment Direction. A financial institution shall not permit an account ~~holder~~ <u>owner</u> to move funds, once deposited, that in any way would result in investment direction under § 529~~(b)(5)~~ of the Code.

C. Reporting Requirements

~~1. To account holders~~

~~a.~~<u>1.</u> At least quarterly, every financial institution shall provide each account ~~holder~~ <u>owner</u> with a statement. The statement shall list a beginning balance, all activity during the quarter, including any interest paid or dividends earned and any penalties charged, and an ending balance. Additionally, the statement for the 4th quarter shall include the following information: an annual beginning balance, an annual total of the interest earned or dividends paid, an annual total of any penalties charged, and a year-end balance.

~~b.~~<u>2.</u> Within the time-frames established by the Code, financial institutions<u>, at the request of the Commission,</u> shall provide Form 1099~~G~~<u>Q</u> to ~~account holders~~ <u>all distributees</u>.

~~2.~~<u>3.</u> ~~To Commission.~~ A copy of the statement described in (C)(1)~~(a)~~ and ~~(b)~~ <u>(2)</u> shall be sent to the Commission. Additionally, each financial institution shall provide the Commission with the information required by A.R.S. § 15-1874(F).

D. Access to books and records. No contractor shall have access to the books and records of a financial institution or Program Manager unless the Commission or its designee ~~1st~~ first approves, with or without modification, such request for access.

E. Non-renewal. The Commission's failure to renew a contract with a financial institution shall not be construed as "good cause" as referred to in A.R.S. § 15-1874(I).

F. Marketing programs

1. Any financial institution or group of financial institutions that wishes to engage in its own marketing program may do so provided that any proposed marketing program is ~~1st~~ first submitted to the Commission for review. If, within 30 days, the Commission does not notify the financial institution or group of financial institutions, in writing, that the proposed marketing program is rejected or requires modifications, the proposed marketing program shall be deemed approved.
2. Any financial institution or group of financial institutions that chooses to engage in its own marketing program may petition the Commission for a credit against future marketing fees.