COVERDELL EDUCATION SAVINGS ACCOUNT (ESA)

FOR NEW ACCOUNTS ONLY

CURRENT AS OF FEBRUARY 2014

PENFED®

Federally Insured by the NCUA.

EARN FEDERALLY INSURED DIVIDENDS WHILE YOU SAVE FOR A CHILD'S EDUCATION.

To afford an education takes planning. And with a PenFed Coverdell Education Savings Account (ESA), you are investing wisely and securely for your child's future education.

You can choose a 1-, 2-, 3-, 4-, 5-, or 7-year ESA Certificate. Our ESA certificates offer competitive rates and are compounded daily for even higher yields. You need only $500 to purchase a 1-, 2-, 3-, 4-, 5-, or 7-Year ESA Certificate.

Take advantage of higher yields, federal insurance, automatic renewal, and convenient dividend and maturity payment options by investing in an ESA certificate today.

Or get our high yield on the ESA Premier that offers Money Market-like rates for a minimum transfer or rollover of $10,000.

You can also open a PenFed ESA Share account with as little as $25. And you can contribute any time you wish, up to your yearly ESA limit. You can use automatic transfer service to add to your child's ESA.

You may contribute $2,000 annually to the ESA.

OPEN YOUR ESA CONVENIENTLY BY MAIL

You have decided that PenFed has the ESA investment to best meet your needs. Simply follow the steps below to establish this account.

Contact us today if you have any questions by calling 800.247.5626, or visit us online at PenFed.org.

1. Complete and sign the Education Savings Account Application form.
   - Remember to choose an ESA investment option or combination of options.
   - Make sure you indicate on the application if future funding will be by automatic transfer.
2. If you would like to transfer a preexisting ESA to PenFed, complete and return three copies of the ESA Transfer Authorization form.
3. Read and retain for your records the Education Individual Retirement Custodial Account Form.
4. Read and retain for your records the Education Savings Account Disclosure Statement.
5. You must be a PenFed member to open an ESA. (Joint ownership does not constitute membership.) To establish membership, each person opening an ESA must complete a Membership Application and return it with a Regular Share (savings) account share purchase of $5.00 or more. You may open your membership account online at PenFed.org. The named beneficiary/student need not be a PenFed member.
6. Please return the ESA Application, Membership Application (if necessary), initial contributions(s) and share purchase(s) and transfer forms. Your ESA must be established prior to PenFed’s acceptance of contributions or transferred funds to your ESA.

Education Savings Account Application

BENEFICIARY'S / STUDENT'S NAME	PENTAGON FEDERAL MEMBER NUMBER (If not a member, leave blank)	
ADDRESS	DATE OF BIRTH (MM/DD/YYYY)	SOCIAL SECURITY NUMBER
RESPONSIBLE PARTY NAME	DATE OF BIRTH (MM/DD/YYYY)	SOCIAL SECURITY NUMBER
PENTAGON FEDERAL MEMBER NO. (If not yet a member, leave blank.)		GRADE / RANK
ADDRESS	HOME PHONE ( )	WORK PHONE ( )

Total Opening Contribution		**Distribution of Initial Contribution**
(Cash/Check) $	Transfer from another Pentagon Federal Account Acct. No. $	Contribution $
Transfer from another Financial Institution* $	Name of Institution:	**Rollover Amount from another ESA** $

Investment Options: Please invest my initial contribution as follows:

- ❑ 1-Year ESA Certificate ($500 minimum)
  Select one maturity option: ☐ Combine dividend and principal and renew my certificate. ☐ Close certificate and deposit in an ESA Share account. Amount $ ________
- ❑ 2-Year ESA Certificate ($500 minimum)
  Select one maturity option: ☐ Combine dividend and principal and renew my certificate. ☐ Close certificate and deposit in an ESA Share account. Amount $ ________
- ❑ 3-Year ESA Certificate ($500 minimum)
  Select one maturity option: ☐ Combine dividend and principal and renew my certificate. ☐ Close certificate and deposit in an ESA Share account. Amount $ ________
- ❑ 4-Year ESA Certificate ($500 minimum)
  Select one maturity option: ☐ Combine dividend and principal and renew my certificate. ☐ Close certificate and deposit in an ESA Share account. Amount $ ________
- ❑ 5-Year ESA Certificate ($500 minimum)
  Select one maturity option: ☐ Combine dividend and principal and renew my certificate. ☐ Close certificate and deposit in an ESA Share account. Amount $ ________
- ❑ 7-Year ESA Certificate ($500 minimum)
  Select one maturity option: ☐ Combine dividend and principal and renew my certificate. ☐ Close certificate and deposit in an ESA Share account. Amount $ ________
- ❑ ESA Share Account ($25 minimum)—*Necessary for all ESAs* Amount $ ________
- ❑ ESA Premier Account ($10,000 minimum)—*Rollover/Transfer only* Amount $ ________

*Please complete the ESA Transfer Authorization form on the following page to initiate the transfer of your ESA from your present custodian to PenFed. (Refer to Disclosure Statement V.2. for important information.)

Subsequent contributions to your ESA account will be made by automatic transfer (allotments, net pay or other recurring payments) and are treated as current year contributions. Transfer from ________________ Amount $__________

How often: ☐ Weekly ☐ Twice a month ☐ Monthly

Contingent Responsible Individual (if any)	Name and Address	SSN	Relationship	Date of Birth (MM/DD/YYYY)

Education Savings Account Option:

☐ **Yes** ☐ **NO** The responsible individual shall continue to serve as the responsible individual for the custodial account after the designated beneficiary attains the age of majority under state law and until such time as all assets have been distributed from the custodial account and the custodial account terminated. If the responsible individual becomes incapacitated or dies after the designated beneficiary reaches the age of majority under state law, the responsible individual shall be the designated beneficiary.

☐ **Yes** ☐ **NO** The responsible individual may change the beneficiary designated under this agreement to another member of the designated beneficiary's family described in section 529(e)(2) in accordance with PenFed procedures.

If you do not answer the above questions, PenFed will deem the answers to be no.

NOTE: If you are not currently a PenFed member, you must open a Regular Share account with a share purchase of at least $5. Status as a joint owner of another PenFed account does not constitute membership. Please complete a membership application and return it to us along with your deposit to Regular Shares, this form, and your initial ESA contribution.

By signing below I am hereby requesting a PenFed ESA and acknowledge that I have received, read, and agree to abide by the terms and conditions of this ESA Application and the Form 5305-EA PenFed Coverdell Education Savings Custodial Account Agreement and Disclosure Statement.

If I am establishing my account with a Rollover contribution I understand this is an irrevocable election.

✗ ____

Signature–Responsible Party Date

EDUCATION SAVINGS ACCOUNT TRANSFER AUTHORIZATION

Return all 3 copies to PenFed (Pentagon Federal Credit Union)

______________________________ Date ______________________

(NAME OF FINANCIAL INSTITUTION)

______________________________ Member No. ______________________

(ADDRESS, INCLUDING ZIP)

____

Re: Education Savings Account (ESA) No. ______________________

Name ______________________ ______________________

(SOCIAL SECURITY NUMBER)

Attention ESA Administrator:

Please accept this letter as your authorization to transfer (check one alternative below):

- ❑ The balance of my ESA, including accrued interest on ______________, less applicable penalties or fees
  (insert date transfer is to be made)
- ❑ The sum of $______________

from my ESA to: PenFed
Attention: ESA
P.O. Box 1432
Alexandria, VA 22313-2032

Please make your check payable to: “Pentagon Federal Credit Union, as Custodian of ESA for

______________________________, Account No. ______________.”

(Student’s Name)

Sincerely,

____

(Depositor’s Signature)

To Pentagon Federal: Upon receipt, deposit funds into

- ❑ ESA Share ($25 minimum)
- ❑ ESA Premier Account ($10,000 min.)
- ❑ 1-Year ESA Certificate ($500 min.)
- ❑ 2-Year ESA Certificate ($500 min.)
- ❑ 3-Year ESA Certificate ($500 min.)
- ❑ 4-Year ESA Certificate ($500 min.)
- ❑ 5-Year ESA Certificate ($500 min.)
- ❑ 7-Year ESA Certificate ($500 min.)

ACCEPTANCE BY PENFED (PENTAGON FEDERAL CREDIT UNION)

This is to certify that PenFed has accepted the appointment as Successor Custodian of the ESA named above.

Pentagon Federal Credit Union

by ______________________________

(Authorized Signature) (Date)

PenFed Form L-736 (3/13)

First Copy: Current Custodian Second Copy: Return to PenFed Third Copy: PenFed

Form **5305-EA**
(Rev. October 2010)
Department of the Treasury
Internal Revenue Service

PENFED®

Coverdell Education Savings Custodial Account
(Under Section 530 of the Internal Revenue Code)

Do not file with the Internal Revenue Service

Name of depositor	**Depositor's identification number**	Check if amendment . . . ► ☐
Name of designated beneficiary	**Designated beneficiary's identification number**	
Address of designated beneficiary	Date of birth of designated beneficiary	
Name of responsible individual (generally the parent or guardian of the designated beneficiary)		
Address of responsible individual		
Name of custodian	Address or principal place of business of custodian	

The depositor named above is establishing a Coverdell education savings account under section 530 for the benefit of the designated beneficiary exclusively to pay for the qualified elementary, secondary, and higher education expenses, within the meaning of section 530(b)(2), of such designated beneficiary.

The depositor assigned the custodial account ______________________ dollars ($ ____________) in cash.

The depositor and the custodian make the following agreement:

Article I

The custodian 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 (AGI) of $95,000 and $110,000. For married individuals filing jointly, the phase-out occurs between modified AGI of $190,000 and $220,000. Modified AGI is defined in section 530(c)(2).

Article II

No part of the custodial account funds may be invested in life insurance contracts, nor may the assets of the custodial 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)).

Article III

1. 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.

2. Any balance to the credit of the designated beneficiary shall be distributed within 30 days of his or her death **unless** the designated 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.

Article IV

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

Article V

The "responsible individual" named by the depositor shall be a parent or guardian of the designated beneficiary. The custodial account 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. Unless otherwise directed by checking the option below, at the time that the designated beneficiary attains the age of majority under state law, the designated beneficiary becomes the responsible individual. If a family member under the age of majority under state law becomes the designated beneficiary by reason of being a named death beneficiary, the responsible individual shall be such designated beneficiary's parent or guardian.

☐ **Option** *(This provision is effective only if checked):* The responsible individual shall continue to serve as the responsible individual for the custodial account after the designated beneficiary attains the age of majority under state law and until such time as all assets have been distributed from the custodial account and the custodial account terminates. If the responsible individual becomes incapacitated or dies after the designated beneficiary reaches the age of majority under state law, the responsible individual shall be the designated beneficiary.

Article VI

The responsible individual ☐ may or ☐ **may not** change the beneficiary designated under this agreement to another member of the designated beneficiary's family described in section 529(e)(2) in accordance with the custodian's procedures.

Article VII

1. The depositor agrees to provide the custodian with all information necessary to prepare any reports required by section 530(h).
2. The custodian agrees to submit to the Internal Revenue Service (IRS) and responsible individual the reports prescribed by the IRS.

Article VIII

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

Article IX

This agreement will be amended as necessary to comply with the provisions of the Code and the related regulations. Other amendments may be made with the consent of the depositor and the custodian whose signatures appear below.

Article X

Article X may be used for any additional provisions. If no other provisions will be added, draw a line through this space. If provisions are added, they must comply with applicable requirements of state law and the Internal Revenue Code.

Depositor's signature ______________________ Date ______________

Custodian's signature **Pentagon Federal Credit Union** Date ______________

Witness' signature ______________________ Date ______________

(Use only if signature of the depositor or the custodian is required to be witnessed.)

General Instructions

Section references are to the Internal Revenue Code unless otherwise noted.

What's New

Military death gratuity. Families of soldiers who receive military death benefits may contribute, subject to certain limitations, up to 100 percent of such benefits into an educational savings account. Publication 970, Tax Benefits for Education, explains the rules for rolling over the military death gratuity and lists eligible family members.

Purpose of Form

Form 5305-EA is a model custodial account agreement that meets the requirements of section 530(b)(1) and has been pre-approved by the IRS. A Coverdell education savings account (ESA) is established after the form is fully executed by both the depositor and the custodian. This account must be created in the United States for the exclusive purpose of paying the qualified elementary, secondary, and higher education expenses of the designated beneficiary.

If the model account is a trust account, see **Form 5305-E,** Coverdell Education Savings Trust Account.

Do not file Form 5305-EA with the IRS. Instead, the depositor must keep the completed form in its records.

Definitions

Custodian. The custodian must be a bank or savings and loan association, as defined in section 408(n), or any person who has the approval of the IRS to act as custodian. Any person who may serve as a custodian of a traditional IRA may serve as the custodian of a Coverdell ESA.

Depositor. The depositor is the person who establishes the custodial account.

Designated beneficiary. The designated beneficiary is the individual on whose behalf the custodial account has been established.

Family member. Family members of the designated beneficiary include his or her spouse, child, grandchild, sibling, parent, niece or nephew, son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, or sister-in-law, and the spouse of any such individual. A first cousin, but not his or her spouse, is also a "family member."

Responsible individual. The responsible individual, generally, is a parent or guardian of the designated beneficiary. However, under certain circumstances, the responsible individual may be the designated beneficiary.

Identification Numbers

The depositor's and designated beneficiary's social security numbers will serve as their identification numbers. If the depositor is a nonresident alien and does not have an identification number, write "Foreign" in the block where the number is requested. The designated beneficiary's social security number is the identification number of his or her Coverdell ESA. If the designated beneficiary is a nonresident alien, the designated beneficiary's individual taxpayer identification number is the identification number of his or her Coverdell ESA. An employer identification number (EIN) is required only for a Coverdell ESA for which a return is filed to report unrelated business income. An EIN is required for a common fund created for Coverdell ESAs.

Specific Instructions

Note: *The age limitation restricting contributions, distributions, rollover contributions, and change of beneficiary are waived for a designated beneficiary with special needs.*

Article X. Article X and any that follow may incorporate additional provisions that are agreed to by the depositor and custodian to complete the agreement. They may include, for example, provisions relating to: definitions, investment powers, voting rights, exculpatory provisions, amendment and termination, removal of the custodian, custodian's fees, state law requirements, treatment of excess contributions, and prohibited transactions with the depositor, designated beneficiary, or responsible individual, etc. Attach additional pages as necessary.

Optional provisions in Article V and Article VI. Form 5305-EA may be reproduced in a manner that provides only those optional provisions offered by the custodian.

PENFED®

EDUCATION SAVINGS ACCOUNT
DISCLOSURE STATEMENT

GENERAL

The Internal Revenue Service (IRS) has not published final regulations for the Education Savings Account. PenFed is providing the following reprint of IRS Notice 97-60 addressing Education Savings Accounts. Until regulations are published the following are the disclosures applicable to your Education Savings Account.

Please note: The contribution limit for an Education Savings Account were increased by the "Economic Growth and Tax Relief Reconciliation Act of 2001." The current limit is $2,000 per year.

I. Questions and Answers

You may decide for any reason to revoke your Pentagon Federal ESA within 30 days of the date of establishment. Your request to revoke your account must be made in writing and should be sent to: PenFed, P.O. Box 1432, Attention: ESA Specialist, Alexandria, Virginia 22313-2032. Upon receipt of your letter, PenFed will refund your contribution in full, neither crediting your account with earnings nor charging it with any administrative fees. Revocation of your ESA is subject to reporting to the IRS. If you have any questions concerning your right to revoke your account, please contact us at 800.247.5626.

Beginning January 1, 2002, taxpayers may deposit up to $2000 per year into an Education Savings Account for a child under age 18. Parents, grandparents, other family members, friends, and a child him/herself may contribute to the child's Education Savings Account, provided that the total contributions for the child during the taxable year do not exceed the $2000 limit. Amounts deposited in the account grow tax-free until distributed, and the child will not owe tax on any withdrawal from the account if the child's qualified higher education expenses at a qualified higher educational institution for the year equal or exceed the amount of the withdrawal. If the child does not need the money for postsecondary education, the account balance can be rolled over to the Education Savings Account of certain family members who can use it for their higher education. Amounts withdrawn from an Education Savings Account that exceed the child's qualified higher education expenses in a taxable year are generally subject to income tax and to an additional tax of 10 percent. The Hope Scholarship Credit and Lifetime Learning Credit may not be claimed for a student's expenses in a taxable year in which the student takes a tax-free withdrawal from an Education Savings Account.

Q1: What is an Education Savings Account (ESA)?

A1: An Education Savings Account is a trust or custodial account that is created or organized in the United States exclusively for the purpose of paying the qualified higher education expenses of the designated beneficiary of the account. The account must be designated as an Education Savings Account when it is created in order to be treated as an Education Savings Account for tax purposes.

Q2: For whom may an ESA be established?

A2: An Education Savings Account may be established for the benefit of any child under age 18. Contributions to the Education Savings Account will not be accepted after the designated beneficiary reaches his/her 18th birthday.

Q3: Where may an individual open an ESA?

A3: An individual may open an Education Savings Account with any bank, or other entity that has been approved to serve as a nonbank trustee or custodian of an individual retirement arrangement (IRA), and the bank or entity is offering Education Savings Accounts. Other entities that wish to offer Education Savings Accounts 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. 19 (October 27, 1997).

Q4: When may a taxpayer start contributing to an Education Savings Account for a child?

A4: A taxpayer may start making contributions on January 1, 1998, or at any time thereafter.

Q5: How much may be contributed to a child's Education Savings Account?

A5: Up to $2000 per year in aggregate contributions may be made for the benefit of any child. The contributions may be placed in a single Education Savings Account or in multiple Education Savings Accounts.

Q6: What happens if more than $2000 is contributed to an Education Savings Account on behalf of a child in a calendar year?

A6: Aggregate contributions for the benefit of a particular child in excess of $2000 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) before the tax return for the year is due, the excess contributions are subject to a 6 percent excise tax for each year the excess amount remains in the account.

Q7: May contributions other than cash be made to a child's Education Savings Account?

A7: No. Education Savings Accounts are permitted to accept contributions made in cash only.

Q8: May contributors take a deduction for contributions made to an Education Savings Account?

A8: No.

Q9: Are there any restrictions on who can contribute to an Education Savings Account?

A9: Any individual may contribute up to $2000 to a child's Education Savings Account if the individual's modified adjusted gross income for the taxable year is no more than $110,000 ($220,000 for married taxpayers filing jointly). (See IRS Notice 97-60 Sec. 1, Q&A6 for a description of modified adjusted gross income.) The $2000 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). Taxpayers with modified adjusted gross income of $110,000 ($220,000 for married taxpayers filing jointly) cannot make contributions to anyone's Education Savings Account.

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

A10: Yes.

Q11: Does a taxpayer have to be related to the designated beneficiary in order to contribute to the designated beneficiary's Education Savings Account?

A11: No.

Q12: How many Education Savings Accounts may a child have?

A12: There is no limit on the number of Education Savings Accounts 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 $2000.

Q13: May a designated beneficiary take a tax-free withdrawal from an Education Savings Account to pay qualified higher 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 higher education expenses.

Q14: What happens when a designated beneficiary withdraws assets from an Education Savings Account 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 higher education expenses.

Q15: What are "qualified higher education expenses"?

A15: "Qualified higher education expenses" mean expenses for tuition, fees, books supplies, and equipment required for the enrollment or attendance of the designated beneficiary at an eligible 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 the designated beneficiary is at least a half-time student at an eligible educational institution. The standards for determining whether a student is enrolled at least half-time are the same as those used for the Hope Scholarship Credit. (See IRS Notice 97-60 Sec. 1, Q&A3.)

Q16: What is an eligible educational institution?

A16: 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, and early withdrawals from IRAs for qualified higher education expenses. (See IRS Notice 97-60 Sec. 1, Q&A4, Sec. 2, Q&A3, and Sec. 4, Q&A2.))

Q17: What happens if a designated beneficiary withdraws an amount from an Education Savings Account but does not have any qualified higher education expenses to pay in the taxable year he/she makes the withdrawal?

A17: Generally, if a designated beneficiary withdraws an amount from an Education Savings Account and does not have any qualified higher 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-free in the account. The taxable portion of the distribution is also subject to a 10 percent additional tax unless an exception applies.

Q18: Is a distribution from an Education Savings Account taxable if the distribution is contributed to another Education Savings Account?

A18: Any amount distributed from an Education Savings Account and rolled over to another Education Savings Account 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 Education Savings Account 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 $2000 annual contribution limit to Education Savings Accounts does not apply to these rollover contributions. For example, an older brother who has $2,000 left in his Education Savings Account after he graduates from college can roll over the full $2,000 balance to an Education Savings Account for his younger sister who is still in high school without paying any tax on the transfer.

Q19: What happens to the assets remaining in an Education Savings Account after the designated beneficiary finishes his/her postsecondary education?

A19: 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 higher education expenses in the same taxable year he/she makes the withdrawal. Alternatively, if the amount in the designated beneficiary's Education Savings Account is withdrawn and rolled over (as described in Q&A18 of this section) to another Education Savings Account for the benefit of a member of the designated beneficiary's family, the amount rolled over will not be taxable.

Q20: Rather than rolling over money from one Education Savings Account to another, may the designated beneficiary of the account be changed from one child to another without triggering a tax?

A20: Yes, provided (1) the terms of the particular trust or custodial account permit a change in designated beneficiaries (each trustee or custodian will control whether options like this one are available in the accounts they offer), and (2) the new designated beneficiary is a member of the previous designated beneficiary's family. (See Q&A18 in this section).

Q21: 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 an Education Savings Account on a tax-free basis?

A21: No. If a student is receiving a tax-free distribution from an Education Savings Account in a particular taxable year, none of that student's expenses may be claimed as the basis for a Hope Scholarship Credit or Lifetime Learning Credit for that year. However, the student may waive the tax-free treatment of the Education Savings Account distribution and elect to pay any tax that would otherwise be owed on an Education Savings Account distribution so that the student or the student's parents may claim a Hope Scholarship Credit or Lifetime Learning Credit for expenses paid in the same year the Education Savings Account distributions are received.

Q22: May contributions be made to both a qualified state tuition program and an Education Savings Account on behalf of the same designated beneficiary in the same taxable year?

A22: No. Any amount contributed to an Education Savings Account on behalf of a designated beneficiary during any taxable year in which an amount is also contributed to a qualified state tuition program on behalf of the same beneficiary will be treated as an excess contribution to the Education Savings Account. (See Q&A6 in this section for the treatment of excess contributions.)

II. Pentagon Federal Account Disclosures

Education Savings Account — all provisions.

a. The credit union reserves the right to make changes in the terms and conditions of its ESA program without prior notice.

b. Education Savings Account Share and certificate accounts are insured separately from any other account you may have with PenFed up to $250,000 by the NCUA.

c. Education Savings Account Share accounts are subject to the following terms and conditions:

- (1) Dividends are calculated on a simple-interest basis from day of deposit until day of withdrawal, compounded and paid monthly at a rate declared by the Board of Directors. Dividends are paid from current income and available earnings, after required transfers to reserves at the end of a dividend period.
- (2) The minimum amount required to establish and maintain an Education Savings Account Share account is $25.00.
- (3) Additions may be made at any time, in any amount, subject to the limits provided by law for the type of ESA selected.
- (4) Withdrawals:
  - (a) Only the responsible individual may request a withdrawal from your Education Savings Account share account.
  - (b) Partial withdrawals or full withdrawals made for the purpose of transferring ESA Share account funds to a PenFed ESA certificate will receive day-of-deposit to day-of-withdrawal dividends.
  - (c) The credit union reserves the right to require a written notice of up to 60 days of intention to withdraw from your ESA Share account.

d. ESA certificates are subject to the following terms and conditions:

- (1) Maturities of either 1, 2, 3, 4, 5, or 7 years are available.
- (2) The minimum amount required for a 1-, 2-, 3-, 4-, 5-, or 7-Year ESA Certificate is $500.
- (3) The dividend rate is set weekly by the Board of Directors.
- (4) Dividends:
  - (a) Dividends are compounded daily on a 365/365 day basis and are credited monthly.
  - (b) Dividends will be paid from day of deposit to day of maturity on the actual value of the certificate. They will be paid at the contracted rate.
- (5) Additions to certificates may be made only at maturity. New certificates may be purchased at any time subject to PenFed minimum deposit requirements and applicable annual contributions limits established by the government.
- (6) Withdrawals:
  - (a) Only the responsible individual may request a withdrawal from your ESA certificates.
  - (b) Partial withdrawals may be made, subject to early withdrawal penalties as described in sub-paragraph (7) below, providing the requested withdrawal amount does not reduce the original issue below a minimum of $500 for 1-, 2-, 3-, 4-, 5-, or 7-Year ESA Certificates, in which case the funds will be transferred to the ESA Share account.
  - (c) The credit union reserves the right to require a written notice of up to 60 days of intention to withdraw funds from your ESA certificate(s).
  - (d) Funds are available for withdrawal on the business day following the maturity date. If the maturity date is a Sunday, funds are available for withdrawal in two business days.
- (7) Certificates having a term of 1 year up to and including 4 years:
  - (a) If redeemed within 180 days of the initial term or any renewal date, all dividends will be forfeited.
  - (b) If redeemed thereafter, but prior to the maturity date, dividends for the most recent 180 days will be forfeited.
- (8) Certificates with a term of 5 years or greater:
  - (a) If redeemed within 365 days of the initial term or any renewal date, all dividends will be forfeited.
  - (b) If redeemed thereafter, but prior to the maturity date, dividends for the most recent 365 days will be forfeited.