Scholarship Tax Credits

Scholarship tax credits encourage private donations to expand educational opportunities for low- and middle-income families. STCs grant tax credits to individual and/or corporate taxpayers who contribute to nonprofit scholarship organizations. Those nonprofits use the money to provide financial assistance to parents so that they can choose the education that works best for their children.

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Ideally, any individual or corporate taxpayer who donates to a scholarship organization should be able to claim a dollar-for-dollar credit. Since STCs are intended to serve families who do not sufficiently benefit from personal-use education tax credits (ETCs), scholarship should be restricted to families below a certain income threshold. The income eligibility cut-off should be high enough to allow middle-income families to participate since the personal-use ETCs may not sufficiently cover the cost of a child's education. Within that framework, scholarship organizations should have the flexibility to tailor the size of scholarships to the particular needs of particular families. They should also have the freedom to set their own funding priorities and scholarship eligibility standards — just as other charitable organizations do.

Scholarship recipients should be able to use the funds for a wide range of education-related expenses, including tuition, tutoring, textbooks, educational materials, home-schooling curricula, online courses, and more. As with personal-use ETCs, flexibility in spending is crucial to the effective operation of the market. Granting parents broad discretion in their educational spending will foster innovation in educational services as entrepreneurs seek new ways of providing value to families. By contrast, limiting the credits to private school tuition or textbooks would enshrine the existing system of education. Likewise, policymakers should not impose additional regulations on private schools accepting scholarship students, thereby limiting the very diversity and innovation that give educational choice its value.

As of July 2015, 16 states have enacted 20 STC programs. The oldest of these is Arizona's individual-donor tax credit, enacted in 1997. Montana and Nevada were the two most recent states to enact a scholarship tax credit. The programs vary in size and design from state to state. The two major factors that distinguish STC programs are the sources of donations (donor type) and the eligibility criteria for scholarship recipients:

- **Donor Type:** The criteria that a taxpayer must meet to be eligible to receive a tax credit in return for a donation to a scholarship organization. Some states limit the credits to individual taxpayers while others limit credits to corporate donations. Eight states allow both individuals and corporations to receive tax credits for donating to scholarship organizations.

- **Scholarship Recipient Eligibility:** The criteria that a student must meet to be eligible to receive a scholarship. Most states limit scholarships only to low-income students while others restrict eligibility to special needs students and/or students assigned to low-performing district schools.

State	Donor Type	Scholarship Recipients	# of Recipients	Year Enacted
Alabama	Individual & Corporate	Low-Income	2,851	2013
Arizona (Individual)	Individual	Low-Income Priority	40,918	1997
Arizona (Corporate)	Corporate	Low-Income	12,955	2006
Arizona (Lexie's Law)	Corporate	Special Needs, Foster Care	345	2009
Arizona (Switcher)	Individual	Switchers, Low-Income Priority	n/a	2012
Florida	Corporate	Low-Income, Foster Care	69,671	2001
Georgia	Individual & Corporate	All Pre-K-12	13,268	2008
Indiana	Individual & Corporate	Low-Income	11,067	2009
Iowa	Individual & Corporate	Low-Income	10,254	2006
Kansas	Corporate	Failing Schools (Low-Income)	n/a	2014
Louisiana	Individual & Corporate	Low-Income	53	2012
Montana	Individual & Corporate	100% Eligibility	N/A	2015
Nevada	Corporate	Low-Income	N/A	2015
New Hampshire	Corporate	Low-income	40	2012
Oklahoma	Individual & Corporate	Low-Income or Failing Schools	709	2011
Pennsylvania (EITC)	Corporate	Low-Income	38,278	2001

Pennsylvania (OSP)	Corporate	Failing Schools (Low-Income)	7,601	2012
Rhode Island	Corporate	Low-Income	411	2006
South Carolina	Individual & Corporate	Special Needs	405	2013
Virginia	Individual & Corporate	Low-Income or Special Needs	982	2012

Source: Friedman Foundation for Educational Choice, Alliance for School Choice Yearbook.

Studies of the financial impact of STC programs in three states found that they saved money by decreasing government expenditures more than they decreased tax revenue. The Florida legislature's nonpartisan Office of Program Policy Analysis and Government Accountability found that their state's STC program saved $1.44 in state expenses for everyone $1 of forgone state tax revenue. The Commonwealth Foundation reported that Pennsylvania saved $512 million a year and an independent study of Arizona's STC program estimated savings of between $99.8 million and $241.5 million.

To ensure that the tax credits are fiscally neutral or save money at the state level, policymakers limit the size and growth of the scholarship tax credits in various ways, including

- **Credit Value:** The percentage of donations eligible for tax credits. These range from 50 percent to 100 percent in existing programs. Higher percentages encourage more giving, thereby increasing the amount of funds available to expand educational choice for families.
- **Total Credit Cap:** The total amount of tax credits available for eligible donors to claim in a given year. Ideally, states would not limit participation in STC programs through such caps, but policymakers sometimes view the cap as a fiscal (or political) necessity. Some states include "escalator" provisions so the caps automatically increase over time, allowing the supply of scholarships grow to meet demand.
- **Credit Cap Escalator:** The amount that the total credit cap increases each year, if at all. In some states, the escalator is triggered only when the total cred-

its claimed in the previous year reach a certain percentage of the total credit cap. In other states, the total credit cap increases automatically.

- **Donation Cap:** The maximum amount that an individual or corporate taxpayer can donate. Sometimes these caps are a percentage of the taxpayer's tax liability, other times they are a fixed amount for all taxpayers. Such caps make fundraising more difficult, necessitating scholarship organizations to attract more donors to raise the same amount of funding that they could without such a cap.
- **Scholarship Cap:** The maximum amount of money that a scholarship organization can disburse to each scholarship recipient. New Hampshire mandates a maximum average scholarship size, which gives scholarship organizations more flexibility while ensuring that the tax credits are fiscally neutral or save money. Larger scholarships are obviously more useful to low-income families.

State	Credit Value	Total Credit Cap	Credit Cap Escalator	Donation Cap	Scholarship Cap
Alabama	100%	$30 million	None	Individual: up to $50,000 or 50% of tax liability / Corporation: 50% tax liability	$6,000 (elementary); $8,000 (middle); $10,000 (high)
Arizona (Individual)	100%	None	N/A	$535 ($1,070 married), adjusted annually for inflation	None
Arizona (Corporate)	100%	$43 million	20% Annual Increase	None	$5,000 (K-8); $6,300 (HS), caps increase by $100 annually
Arizona (Lexie's Law)	100%	$5 million	None	None	Lesser of full tuition or 90% of state per pupil formula funding
Arizona (Switcher)	100%	None	N/A	$523 ($1,064 married) after donating maximum for original individual tax credit	None

Florida	100%	$357.8 million	25% Increase If 90% Cap Reached	50% to 100% of tax liability, depending on tax	Lesser of 80% of state public school funding formula ($5,272) or full tuition
Georgia	100%	$58 million	None	Individual: $1,000 ($2,500 married) / Corporate: $10,000 (up to 75% of total corporate tax liability)	Total average state and local expenditures per pupil
Indiana	50%	$8.5 million in 2015-16; $9.5 million in 2016-17	None	None	Full tuition
Iowa	65%	$12 million	None	None	Full tuition
Kansas	70%	$10 million	None	None	$8,000
Louisiana	100%	None	N/A	None	Lesser of full tuition or 80% (K-8) / 90% (HS) of state per pupil formula funding
Montana	100%	$3 Million	10% Annual Increase	Individual: $150	50% of district school per-student funding
Nevada	100%	$5 Million	10% Annual Increase	None	$7,775
New Hampshire	85%	$5.1 million	25% Increase If 80% Of Cap Reached	No corporation can receive more than 10% of total credits	$2,541 max average ($635 homeschool), minimum $4,447 special ed, adjusted annually for inflation
Oklahoma	75%	$3.5 million	None	Individual: $1,000 ($2,000 married) / Corporate: $100,000	Greater of $5,000 ($25,000 special needs) or 80% of average per pupil expenditure in assigned district school.

Pennsylvania (EITC)	75% (90% for two-year commitment)	$100 million	None	$750,000	Full tuition
Pennsylvania (OSP)	75% (90% for two-year commitment)	$50 million	None	$750,000	$8,500 ($15,000 special needs)
Rhode Island	75% (90% for two-year commitment)	$1.5 million	None	$100,000	None
South Carolina	100%	$8 million	None	60% of tax liability	$10,000
Virginia	65%	$25 million	None	Corporations: None / Individuals: Minimum $500; Maximum $125,000	Lesser of full tuition or 100% of state per pupil formula funding

Source: Friedman Foundation for Educational Choice, Alliance for School Choice Yearbook.

Additional Resources

Books

- *Market Education: The Unknown History* by Andrew J. Coulson

Studies

- "The Public Education Tax Credit" by Adam B. Schaeffer
- "Forging Consensus" by Andrew J. Coulson
- "On the Way to School: Why and How to Make a Market in Education" by Andrew J. Coulson
- "Do Vouchers and Tax Credits Increase Private School Regulation?" by Andrew J. Coulson
- "The Fiscal Impact of a Large-Scale Education Tax Credit Program" by Andrew J. Coulson
- "Live Free and Learn: A Case Study of New Hampshire's Scholarship Tax Credit Program" by Jason Bedrick

- "Giving Kids Credit: Using Scholarship Tax Credits to Increase Educational Opportunity in Massachusetts" by Jason Bedrick and Ken Ardon
- "Choosing to Learn: Scholarship Tax Credit Programs in the United States and Their Implication for New Hampshire" by Jason Bedrick
- "Earning Full Credit: Learning from and Improving Indiana's School Scholarship Tax Credit Law" by Jason Bedrick
- "The Arizona Scholarship Tax Credit: Giving Parents Choices, Saving Taxpayers Money" by Carrie Lips and Jennifer Jacoby
- "Reclaiming Our Schools: Increasing Parental Control of Education through the Universal Education Credit" by Darcy A. Olsen and Matthew J. Brouillette

Model Legislation

- Scholarship Tax Credits by the Cato Institute's Center for Educational Freedom

Commentary

- "School Choice's Ace in the Hole" by Adam B. Schaeffer
- "Design Matters: The Future of School Choice" by Jason Bedrick
- "Low-Income Parents Highly Satisfied with New Hampshire's Scholarship Tax Credits" by Jason Bedrick
- "Expanding Educational Opportunity" by Jason Bedrick and Ken Ardon
- "A 'Winn' For Education and Freedom of Conscience" by Andrew J. Coulson