

FEDERAL SCHOLARSHIP TAX CREDIT

Education Freedom Tax Credit

Executive Summary

The Federal Scholarship Tax Credit (FSTC), also known as the Education Freedom Tax Credit, was enacted on July 4, 2025, as part of the One Big Beautiful Bill Act. The program creates the nation's first federal scholarship tax credit, allowing individuals to claim a dollar-for-dollar federal tax credit of up to \$1,700 per year for contributions to scholarship-granting organizations (SGOs) that provide K-12 educational scholarships for eligible students.

The popular perception of this provision is that it can only be used to help families pay for private schools. This is not true. While private tuition is allowed, so too are supports for public school students—including many from low- and middle-income families—through academic tutoring, exam fees, test prep, internet services, and special-needs support.

The program becomes available for donations made on or after January 1, 2027, with credits claimable when taxpayers file their 2027 returns in 2028. As of February 2026, twenty-seven states have already declared their intent to participate.¹

Why Participate

Zero Cost to Your State Budget

Participation in FSTC requires no direct state expenditure and will have no impact on your state budget. Scholarships are funded entirely by voluntary donations from individuals who receive a federal tax credit for their contributions. This is not state money—it is federal tax dollars being redirected to support K-12 students.

Capture Federal Resources or Lose Them to Other States

If your state does not opt in, the first \$1,700 of every taxpayer's federal taxes will leave your

state and flow either to the U.S. Treasury's general fund or to SGOs in other states. Opting in allows your state to recoup as much of these funds as possible so that they can be used to support K-12 students in your communities.

"I would be crazy not to opt in. If Colorado doesn't participate, our federal tax dollars will simply flow to other states."

- Governor Jared Polis (CO)

States Can Raise Significant New Money for K-12 Supports

A recent analysis by Education Reform Now projects that FSTC could generate more than \$24 billion nationally each year if governors opt in and families are engaged effectively.² These dollars are entirely additive—they will not impact state education budgets by a single cent.

Since the \$1,700 contribution would be costless to the donor (because it is a 1-for-1 tax credit), we expect that a large number of residents will prefer to donate those \$1,700 to a local SGO as opposed to sending it to the IRS general fund. And over time, as awareness of the tax credit grows, it is likely that the number of participants will continue rising. Every \$1 billion in scholarships could fund tuition at a school of choice for 77,000 students or cover tutoring for more than 300,000 students.¹

Public School Students Can Access the Funds

While FSTC scholarships can be used to pay for private school tuition, they can also be used to pay for tutoring, test preparation

courses, exam fees, internet services, special-needs services, educational technology, uniforms, transportation, and other qualified educational expenses for students attending public schools. SGOs will design their own programs and determine which eligible services to fund, creating flexibility to address diverse community needs.

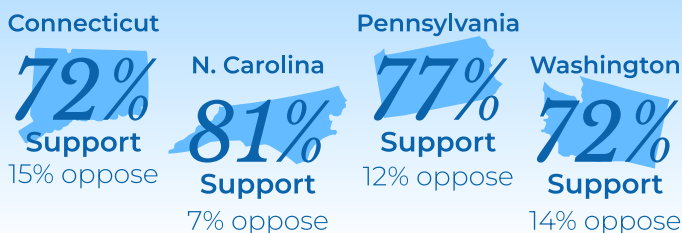
Address Inequities in Out-of-School Spending

The gap in enrichment spending between high-income and low-income families has grown dramatically over time. According to the Afterschool Alliance's *America After 3PM* survey, higher-income families spent more than five times as much on out-of-school opportunities as families in the lowest income bracket in 2020, roughly \$3,600 versus \$700 per year.⁴ By 2025, this gap had widened further, with high-income families spending

Voters Strongly Support It

National and state polling shows widespread public support for FSTC³

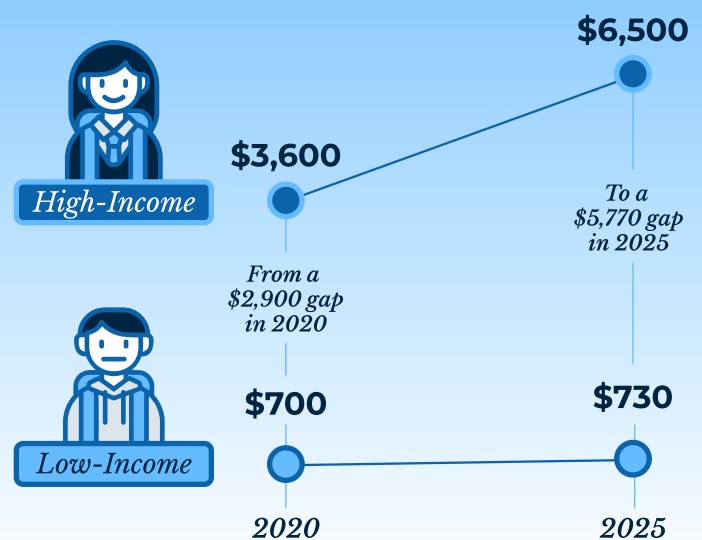
64% of all voters favor their governor opting into FSTC, compared to just 19% who oppose



The Widening Gap in Out-of-School Enrichment Spending

Low-Income vs. High-Income Families

Annual Spending per Child (2012 dollars)



Note: Spending includes afterschool programs, tutoring, music lessons, summer camps, and other educational enrichment activities.

Source: Afterschool Alliance, "America After 3PM" surveys (2020, 2025)

about nine times more, approximately \$6,500 per child, compared to around \$730 spent by low-income families.⁴ This growing inequity in access to tutoring, summer camps and other enrichment activities directly impacts educational outcomes. Scholarships provided through FSTC can help address this opportunity gap and positively contribute to students' academic success.

Spur Community-Led Educational Innovation

In states with programs similar to FSTC, educators are starting small education-related businesses to provide services that can be funded by scholarships, including microschoools and tutoring services. This creates opportunities for educators to innovate and meet diverse student needs while stimulating local economic activity.

How FSTC Works

The Basics

- **Tax Credit:** Individuals can receive a dollar-for-dollar federal tax credit of up to \$1,700 per year for contributions to qualifying SGOs
- **No Aggregate Cap:** There is no nationwide limit on the number of tax credits that can be claimed
- **Effective Date:** Donations become eligible starting January 1, 2027, with credits claimable on 2027 tax returns filed in 2028
- **Carryforward:** Unused credits may be carried forward for up to 5 years
- **State Opt-In Required:** States must voluntarily elect to participate and provide an annual list of qualified SGOs to the U.S. Treasury by January 1 of each calendar year

Step-by-Step Process

1. **State Opt In:** The Governor (or designee by state law) elects to participate and provides a list of qualified SGOs to the U.S. Treasury
2. **Taxpayer Contributes:** An individual makes a cash contribution to a qualified SGO on the state's list
3. **SGO Awards Scholarships:** The SGO uses donations to provide scholarships to eligible students for qualified educational expenses
4. **Taxpayer Claims Credit:** When filing their federal tax return, the taxpayer receives a credit of up to \$1,700 against their federal tax liability

How FSTC Differs From State Tax Credit Programs

Unlike state tax credit scholarship programs that often cap donations and focus on high-net-worth donors for private school tuition, FSTC offers uncapped dollar-for-dollar federal tax credits to any

individual donor and supports students in public schools, after-school programs, and summer programs. This dollar-for-dollar credit is far more advantageous than many state programs, making it essentially free for participating taxpayers.

State Tax Credit Programs

- Often have aggregate caps and focus on high-net-worth donors
- Most focus exclusively on private school tuition
- Credit value varies by state

Federal Scholarship Tax Credit

- No aggregate cap; anyone can claim a credit up to \$1,700
- Supports students in public schools, private schools, tutoring, after-school programs, and more
- Dollar-for-dollar federal credit up to \$1,700

Scholarship Granting Organization (SGO) Requirements

To qualify for FSTC, an SGO must:

- Be a 501(c)(3) organization
- Not be a private foundation
- Prevent co-mingling of FSTC donations with other donations by maintaining separate accounts
- Provide scholarships to 10 or more students who do not all attend the same school
- Spend at least 90% of FSTC funds raised on scholarships

- Provide scholarships only for qualified elementary or secondary education expenses
- Give priority to students awarded a scholarship in the previous year and their siblings
- Not earmark or set aside contributions for particular students (though donors may earmark for particular schools)
- Verify annual household income and family size of applicants
- Limit scholarships to eligible students (households earning up to 300% of area median gross income)

Student Eligibility

Students are eligible to receive FSTC scholarships if they:

- Are eligible to enroll in a public elementary or secondary school (K-12)
- Come from a household with income not greater than 300% of the area median gross income (this covers approximately 85-90% of K-12 students nationwide)

Qualified Educational Expenses

Scholarships can be used for expenses incurred in connection with enrollment or attendance at any public, private, or religious K-12 school, including:

- Tuition and fees
- Academic tutoring
- Special needs services
- Books, supplies, and equipment

- Room and board (when required by the school)
- Uniforms (when required by the school)
- Transportation
- Supplementary items and services, including extended day programs
- Computer technology, equipment, internet access, and related services
- Test preparation courses and exam fees

Implementation Timeline

July 4, 2025: FSTC enacted as part of the One Big Beautiful Bill Act

December 2025: Treasury Department and IRS issued request for comments and guidance allowing states to make Advance Elections

January 1, 2026 – Present: Treasury Department and IRS issued request for comments and guidance allowing states to make Advance Elections

2026: Treasury Department and IRS expected to issue implementing rules and additional guidance

January 1, 2027: Program becomes available; donations to qualified SGOs become eligible for the tax credit

2028: Taxpayers file 2027 returns and claim credits for 2027 donations

Key Takeaways For Governors

This is a no-brainer opportunity: FSTC requires no state spending, no budget impact, and delivers billions in new educational resources at zero cost to state budgets

Act now or lose out: States that don't opt in will see their residents' federal tax dollars flow to other states' communities

Voters support it: Nationally, 64% of voters—including strong majorities of Democrats (61%), Black voters (63%), and Hispanic voters (68%)—want their governor to opt in

Broad benefits: FSTC supports public school students as well as private school students, funding tutoring, special needs services, technology, and more

Evidence-based: Research shows school choice programs improve academic outcomes, increase parental satisfaction, and generate fiscal savings for taxpayers

Opportunity for leadership: Governors who opt in can shape how FSTC works in their state, support working families, and demonstrate they put students above partisan politics

References

1. U.S. Department of Education, 'Education Freedom Tax Credit Fact Sheet,' January 2026. Available at: <https://www.ed.gov/media/document/education-freedom-tax-credit-fact-sheet-113147.pdf>
2. Education Reform Now, 'Federal Scholarship Tax Credit – State Projections' February 3, 2026. Available at: <https://edreformnow.org/fstc-projections/>
3. Democrats for Education Reform, 'New National Polling Shows an Overwhelming Majority of Voters Support Educational Choice for Children Act (ECCA),' Emerson College Polling, August 25–26, 2025 (n=1,000 registered voters, ±3 percentage points). Available at: <https://dfer.org/2025/09/22/new-national-polling-shows-an-overwhelming-majority-of-voters-support-educational-choice-for-children-act-ecca/>
4. Afterschool Alliance, 'America After 3PM' surveys (2020, 2025). The 2020 survey found higher-income families spent roughly \$3,600 vs. \$700 per year for low-income families. The 2025 survey found high-income families spent approximately \$6,500 per child vs. around \$730 for low-income families. Available at: <https://afterschoolalliance.org/>

This factsheet provides an overview of the Federal Scholarship Tax Credit (FSTC) program. For the most current information on implementation and guidance, please consult the U.S. Department of Treasury and IRS resources.