



The Florida Senate

Interim Project Report 2004-132

November 2003

Committee on Education

James E. "Jim" King, Jr., President

CORPORATE TAX CREDIT SCHOLARSHIP PROGRAM ACCOUNTABILITY

SUMMARY

Since its inception in 2001, the Tax Credit Scholarship Program has provided over 20,000 scholarships to students in need by offering parents an option of enrolling their children in a private school. However, the program has serious fiscal and academic accountability deficiencies that, if not corrected, threaten the continued viability of the program. Participation in the program by corporate taxpayers and the amount of contributions has significantly fallen. The drop in contributions may be attributed to the perceived lack of accountability in the program.¹ Whether designed by intent or by the failure of certain parties to implement their statutory required obligations, the system of self-policing and accountability by the scholarship-funding organizations and participating private schools does not appear to be working. Accordingly, the Legislature may need to prescriptively require accountability in the program to ensure that those students in need are adequately and properly served.

Findings from the committee's interim study reveal both administrative and legislative problems. Therefore, recommendations include certain legislative remedies and others that will require administrative implementation or changes in approach by the State Board of Education.

The program is extremely popular with the parents whose children are participating in the program. The challenge to the Legislature will be striking the proper balance between establishing accountability and improving the quality of the program without stifling educational improvement and parental choice.

BACKGROUND

The 2001 Legislature enacted the tax credit scholarship program for implementation in the 2002 tax year. Under the program, corporate taxpayers are authorized to take a dollar for dollar credit for contributions to nonprofit scholarship-funding organizations that provide scholarships to students who (1) qualify for free or reduced-price school lunches under the National School Lunch Act and (2) were counted as a full-time equivalent student during the previous state fiscal year for purposes of state per-student funding or are eligible to enter kindergarten or the first grade.

The program was initially capped at \$50 million in tax credits per year but was subsequently expanded to \$88 million in 2003 (s. 9, ch. 2003-391, L.O.F.) Five percent of the tax credit is reserved for small businesses as defined under s. 288.703(1), F.S. A taxpayer may not contribute more than \$5 million to any single scholarship-funding organization. A taxpayer may carry forward any unused amount of the tax credit for up to three years. A taxpayer may not designate a specific child or group of children as the beneficiaries of the scholarship.

A scholarship-funding organization must be a charitable organization exempt from federal income tax pursuant to s. 501(c)(3) of the Internal Revenue Code. In addition, a scholarship-funding organization must spend all of the contributions for scholarships in the state fiscal year in which received. A scholarship-funding organization may not use any portion of the contribution for administrative expenses. An annual financial and compliance audit is required of the scholarship-funding organization and must be submitted to the Auditor General for review. A scholarship-funding organization is authorized to offer two separate scholarships: a \$3500 maximum scholarship for tuition, textbook expenses, or transportation to attend an eligible private school, 75 percent of which must be used for tuition; and a \$500

¹ Pennsylvania maintains a similar tax credit scholarship program that is capped at \$30 million but has not experienced a decline in contributions.

maximum scholarship for transportation expenses to a public school located in another school district.

A participating private school must meet fiscal soundness requirements by having been in operation for at least one year or providing sufficient evidence that demonstrates its fiscal soundness through several statutorily prescribed methods. In addition, eligible private schools must comply with state and local health and safety laws and codes, federal antidiscrimination provisions of 42 U.S.C. s. 2000d, and all state laws relating to the regulation of private schools.

The Department of Education is required to annually submit to the Department of Revenue by March 15 a list of eligible scholarship-funding organizations that meet the statutory requirements. In addition, the Department of Education is required to monitor the eligibility of the scholarship-funding organizations, the private schools, and the expenditures under the program. The Department of Education is charged with adopting rules, as necessary, to determine the eligibility requirements of the scholarship-funding organizations and to identify qualified students.

The Department of Revenue is charged with adopting rules establishing the procedures and forms for applying for the tax credit and the allocation of the tax credit to a taxpayer on a first come, first-served basis.

For tax year 2002, the Department of Revenue approved 76 tax credit applications for 49 taxpayers in the amount of \$46,902,000. Four taxpayers were small businesses that were approved for tax credits in the amount of \$186,000. The Department of Revenue approved 60 tax credit applications for 32 corporations in the amount of \$29,270,000 for tax year 2003 (as of September 19, 2003). Two taxpayers were small businesses that were approved to contribute \$34,000. Approximately seven firms contributed both years of the program.

The Department of Education approved the following scholarship-funding organizations with contributions received per indicated state fiscal year according to information provided by the scholarship-funding organizations:

Scholarship-Funding Organization	FY 2001-2002	FY 2002-2003	FY 2003-2004 (As of 9/2003)
Academy Prep Foundation	\$0	\$237,000	\$0
Children First Central Florida	\$829,375	\$14,187,000	\$1,320,297
Faith Based Scholarship Foundation of Florida	\$0	\$0	\$0
FloridaChild	\$475,000	\$18,845,425	\$2,745,333
Florida PRIDE	\$468,000	\$8,913,500	\$2,604,125
H.E.R.O.E.S.	\$0	\$5,193,500	\$1,050,000
Silver Archer Foundation	unknown	unknown ²	unknown
Yes Opportunities	\$0	\$1,050,000	\$250,000

According to data provided by the scholarship-funding organizations,³ 970 students received scholarships in FY 2001-2002 to attend a private school and no students received scholarships to attend a public school. Scholarship values ranged from \$284 to \$1,775. In FY 2002-2003, 19,206 students received scholarships to attend a private school and 107 students received scholarships to attend a public school with a scholarship value ranging between \$100 and \$3500.

METHODOLOGY

Staff reviewed current law and legislative history and surveyed the Department of Education and all scholarship-funding organizations. Interviews were conducted with representatives of the Department of Education, the Department of Revenue, almost all of the scholarship-funding organizations, and certain private schools.⁴ Staff has reviewed the statutory

² The Silver Archer Foundation LTD received \$412,500 in tax year 2003. Silver Archer did not respond to the committee's survey. Silver Archer is also currently under investigation by the Department of Financial Services in conjunction with the statewide prosecutor regarding use of the contributions under the tax credit scholarship program. The Department of Education has removed Silver Archer Foundation from the list of approved scholarship-funding organizations.

³ Id.

⁴ The Silver Archer Foundation LTD did not respond to repeated attempts at contact.

framework and administration of similar programs in other states. Recommendations to improve accountability in the program were received from the Department of Education, several of the scholarship-funding organizations, and certain private schools.

FINDINGS

Lack of State Oversight over the Tax Credit Scholarship Program

Whether by intent, omissions in the statute, or as a result of the restructuring occurring in the Department of Education due to assimilating both an appointed State Board of Education and an appointed Commissioner of Education, and the rewrite of the Florida School Code, the record is clear that there is very little or no state oversight of the tax credit scholarship program. Instead, the scholarship-funding organizations appear to have been delegated the authority to operate the program. Although the Department of Education is attempting to provide accountability in the program by requiring a sworn compliance form be completed by participating private schools, it is too early to determine what effect, if any, the compliance form will have on improving accountability under the program. Most of the information required on the compliance form should have already been submitted to the Department of Education under s. 1002.42, F.S.

Role of the State Board of Education

The State Board of Education has not provided the Department of Education sufficient guidance to improve accountability in the program. The State Board has not used its rulemaking authority to resolve issues such as the eligibility criteria for scholarship-funding organizations, the identification of qualified students, and the monitoring of scholarship-funding organizations, private schools, and expenditures under the program. Consequently, the Department of Education relies entirely on the scholarship-funding organizations to manage the program. Unfortunately, when a scholarship-funding organization fails to implement its delegated authority, the Department of Education is unable to effectively account for the expenditure of funds, regulate the participation of private schools, and identify participating students.

It has been difficult to determine who at the Department of Education is actually running the tax credit scholarship program on behalf of the state.

Statements from some of the stakeholders involved indicate that at times the program has been directed by the General Counsel's Office; the Choice Office and its successor, the Office of Independent Education and Parental Choice; or even leaders of the scholarship-funding organizations.⁵ The State Board of Education, as head of the Department of Education, should assert leadership by defining a chain of command with respect to operating the program.

Initial Approval of Scholarship-Funding Organizations

The criteria for initial approval of scholarship-funding organizations are easily met and documentation supporting participation in the program is not routinely kept. Accordingly, it is difficult to ascertain whether the scholarship-funding organization approval process complies with the law. To initially qualify, a scholarship-funding organization is only required to be a nonprofit charitable organization exempt from federal income tax pursuant to s. 501(c)(3) of the Internal Revenue Code. Although not adopted in rule, the Department of Education's approval process for scholarship-funding organizations consists of requesting the following documents: (1) a copy of the IRS Determination Letter as a charitable organization, (2) the location of the nonprofit organization, and (3) the date of incorporation and registration with the Florida Division of Corporations, Office of the Secretary of State.⁶ However, the Department of Education has only recently been able to identify its personnel who approved the participation of the scholarship-funding organizations, and still has not produced the documentation that it requested from the scholarship-funding organizations.

There does not appear to be a mechanism in place to ensure the review of scholarship-funding organization filings requested by the Department of Education. Silver Archer Foundation was approved to participate in the program even though it was not registered with the Department of State. Silver Archer Foundation is actually a Colorado corporation that was administratively dissolved, yet it was approved for

⁵ Interview with Department of Education personnel, September 15, 2003.

⁶ Since participation in the program is contingent upon filing the requested documentation and since the statute only requires the scholarship-funding organization to be a nonprofit charitable organization described above, the requirement of submitting the requested documents should be adopted by rule.

participation in the tax credit scholarship program. Silver Archer did not file the necessary documents with the State of Colorado to have itself reinstated to active status as a Colorado corporation until August 2003 when it was under investigation in Florida. By requiring a scholarship-funding organization to be an active corporation qualified to do business in the state or a corporation formed in the state, the state can more effectively control the information that a scholarship-funding organization must provide. In addition, the registered agent requirements would bring greater certainty for citizens of the state seeking redress against a scholarship-funding organization.

Monitoring the Eligibility of Scholarship-funding Organizations

Once approved, scholarship-funding organizations are not routinely monitored to ensure compliance with the law. The Department of Education is required to monitor the continued eligibility of the scholarship-funding organizations. However, the department has narrowly interpreted this provision to mean that its oversight authority is limited to reviewing audits and responding to complaints.⁷ Since the earliest that any audits were filed was August 2003, by its own admission, the department did not exercise any oversight authority prior to that date, relying exclusively on the scholarship-funding organizations to police the program. Moreover, since FloridaChild has not filed an audit, the department has not exercised any oversight authority over FloridaChild.⁸ Finally, the law does not require the audits to be filed with the department; rather, audits are filed with the Auditor General.

The effectiveness on relying solely on audits to regulate the activities of the scholarship-funding organizations has also been undermined by a lack of clear direction as to what the audits should comprise. Subsequently, the Auditor General has adopted rules governing these types of audits. Although the Department of Education maintains that these audits are not subject to the Florida Single Audit Act, several scholarship-funding organizations have expressed an interest in the use of the Florida Single Audit Act to satisfy the audit requirement.

In any event, it is not clear who at the department reviews the audits. In response to the committee's request for a report on any scholarship-funding organization that did not comply with the requirement to spend all of its contributed funds for scholarships in the state fiscal year in which received, the department failed to acknowledge that a scholarship-funding organization had undisbursed scholarship funds at the close of the state fiscal year.⁹ In fact, the Auditor General's office had notified the department of this deficiency.

Finally, other proactive methods that could be used to monitor the activities of the scholarship-funding organizations are not being employed. The Department of Education has asked for clarification of its statutory authority to request information and reports from the scholarship-funding organizations.¹⁰ It should be noted that several of the scholarship-funding organizations have expressed a willingness to "open" their books to the department.

The Department of Education does not routinely or randomly conduct site visits to inspect the records of the scholarship-funding organization. Moreover, it is unclear that even if given clarification of their authority to conduct site visits would the department engage in random inspections.

Monitoring the Eligibility of Private Schools

Until creation of the Department of Education's sworn compliance form, only the scholarship-funding organizations were monitoring the eligibility of private schools. To participate in the program, a private school must demonstrate fiscal soundness, comply with federal antidiscrimination laws, meet state and local health and safety laws and codes, and comply with all state laws relating to private schools. Again, prior to the implementation of the department's compliance form and without the assistance of the scholarship-funding organizations, the department could not identify which private schools are participating in the program.

The department cannot state with any confidence that the private schools participating in the program are

⁷ Response from the Department of Education to committee survey dated October 14, 2003.

⁸ Academy Prep Foundation has not filed a compliance audit.

⁹ On June 30, 2002, Children First – Central Florida, Inc., had \$92,970 of scholarship funds that were not disbursed in contravention of s. 220.187(4)(d), F.S. These funds were distributed during the next school year.

¹⁰ Speech by Commissioner of Education Horne on August 28, 2003.

meeting health and safety laws or are complying with all state laws relating to private schools. There is no department procedure for verifying compliance with the law for private schools other than waiting for a complaint to be filed. The department does not engage in any random site visits to verify compliance.¹¹ There are no cooperative agreements between the department and local code enforcement offices indicating the presence of a private school or for transmitting code findings to the department.¹²

Fiscal soundness requirements do not provide sufficient indicia that a private school would be able to continue operations for the upcoming school year. This inability to effectively demonstrate financial stability would be a detriment to student education continuity if a private school ceases operations. While it may appear intuitive, there is no evidence that being in operation for more than one year indicates that a private school is more likely to be in operation the following year. In addition, if a private school has been in operation for more than one year, the fiscal soundness determination is rubberstamped by the scholarship-funding organization and the information is not reported to the department.

Maintaining sufficient capital appears to provide the most information to determine whether a private school is likely to be in operation the following academic year. However, the State Board of Education has not adopted rules identifying what constitutes sufficient insurance coverage or assets to satisfy the fiscal soundness requirements. Demonstration of fiscal soundness through insurance and reporting of assets is meaningless without administrative guidance as to what constitutes sufficient insurance coverage or capital to continue operations. Finally, the purchase of a surety bond in the amount of scholarship funds that are under management for one quarter does not provide sufficient indicia that a private school is financially stable beyond the quarter for which the surety bond is purchased.

¹¹ According to the Department of Education General Counsel's Office, conducting random site visits is not practicable because there are numerous private schools participating in the program. Interview with Department of Education on September 5, 2003.

¹² County health department sanitary inspection data is available from the Florida Department of Health.

Monitoring the Eligibility of Students

The Department of Education has largely delegated determinations of eligibility for students to participate in the program to the scholarship-funding organizations. This has occurred because of two potentially conflicting provisions in the law that requires both the department and the scholarship-funding organizations to identify qualified students. However, the department's reliance on scholarship-funding organizations to regulate eligibility determinations means the department does not know which children are participating in the program unless supplied this information by the scholarship-funding organizations. Although the department has indicated that it now has an existing database that identifies student participation in the program, the department only recently crosschecked its list of students who qualify for free or reduced-price school lunches with a list of students receiving scholarships under the tax credit scholarship program. Moreover, the department has only recently notified the scholarship-funding organizations which children were counted as a full-time equivalent student in the public schools the prior school year.

The law requires the department to adopt rules establishing the eligibility of students. However, the State Board of Education has not adopted rules mandating income verifications for purposes of determining a student's eligibility. Certain scholarship-funding organizations have voluntarily contracted with a company that performs income determinations for the National School Lunch Act to determine student eligibility. These income determinations are performed on a sampling basis.

Enforcement of the Law

The Department of Education would prefer explicit statutory enforcement powers to be outlined in the law.¹³ Upon discovery that a private school participating in the program was allegedly affiliated with an individual under investigation by federal authorities for sponsoring terrorism, the Commissioner of Education directed a scholarship-funding organization to halt scholarship payments to the private school. The scholarship-funding organization complied and the private school did not challenge the action. In a separate case, it was discovered that a scholarship-funding organization had allegedly violated the law by

¹³ Interview with Department of Education on September 5, 2003.

failing to disburse scholarship funds to students in the same year funds were donated and to properly account for those funds. The Commissioner of Education ordered an investigation and revoked the eligibility of the scholarship-funding organization to participate pending the results of the investigation. Even though the actions may be appropriate, it has been suggested that there is no explicit statutory authority for the Commissioner to take these actions. The law should be amended to clarify the Commissioner's or department's authority to enforce the requirements of the program including the power to revoke the right of participation.

Attendance

There is no statutory requirement that a scholarship-funding organization require proof of a student's attendance at a participating private school prior to each scholarship payment. Accordingly, the Department of Education and the scholarship-funding organizations do not know whether a student is actually attending the private school. Coupled with the ability to execute a power of attorney on behalf of the private school, funds could be disbursed for students that are not enrolled in the private school.

Designating a Specific Child as the Beneficiary of the Scholarship

There are currently no statutory restrictions on a scholarship-funding organization designating a particular child or private school for receipt of a scholarship. Section 220.187(2)(b), F.S., prohibits a taxpayer from designating a specific child as the beneficiary of the contribution. Academy Prep Foundation operates as a scholarship-funding organization for its affiliated institutions and other schools. This arrangement, coupled with the relatively lax qualification requirements for scholarship-funding organizations and private schools, could be used to circumvent the statutory prohibition and allow a taxpayer to make a contribution to a specific scholarship-funding organization knowing which children would benefit from the contribution.

Simultaneous Receipt of Funds under Scholarship Programs

There is no current statutory prohibition on simultaneously receiving scholarship funds under a state scholarship program and under the tax credit scholarship program. This "double-dipping" would reduce the overall funds available to serve other students in need.

Criminal Background Checks

The criminal background checks currently performed fail to ensure that private school personnel having direct contact with students have not been convicted of a crime involving moral turpitude. Pursuant to s. 1002.42(2)(c), F.S., only the owners or operators of a private school in the state are required to be fingerprinted. Fingerprints are filed with the Florida Department of Law Enforcement but not with the Federal Bureau of Investigation. The results of the criminal records check are forwarded to the owner or operator and are required to be made available for public inspection in the private school office. Any individual convicted of a crime involving moral turpitude may not own or operate a private school. An owner or operator may require school employees to file a complete set of fingerprints with the Department of Law Enforcement for criminal background processing. The results of the check are forwarded to the owner for use in employment decisions.

Owner/Operator of a Private School

The criminal background checks on an owner or operator of a private school do not provide adequate safeguards. The Department of Law Enforcement does not routinely review the results of the background checks prior to forwarding the results to the owner or operator of a private school. Results are not forwarded to the Department of Education. Similarly, there is no standard operating procedure at the Department of Education to verify the owner or operator of a private school is making the results available to the public. Accordingly, an individual who has been convicted of a crime involving moral turpitude could own or operate a private school.

Private School Personnel

Although s. 1002.42, F.S., authorizes a private school owner or operator to conduct criminal background checks on private school personnel, the criminal background checks are not required. Accordingly, the state does not know if students under the tax credit scholarship program are having direct contact with individuals who have been convicted of crimes involving moral turpitude. This ignorance is exacerbated by the fact that s. 1002.42, F.S., merely requires the Department of Law Enforcement to report the optional criminal background checks to the owner or operator of the school. The report is not forwarded to the Department of Education and is not required to be made available to the public by the owner or

operator of the private school. A criminal background check of private school personnel does not preclude an individual with a criminal history from having direct contact with a student in a private school; the decision to employ the individual is left to the discretion of the private school owner or operator.

Scholarship-Funding Organization Personnel

Finally, the personnel of a scholarship-funding organization are not required to undergo a criminal background check. Accordingly, there is no state mechanism in place to ensure that individuals with a criminal history to include fraud or theft are not handling scholarship dollars.

Academic Accountability

There are no state-mandated academic accountability requirements under the tax credit scholarship program. Consequently, the state does not know if the program is adequately serving participating students. If a student fails to make adequate progress and returns to the public school system, the state and the student would be at a disadvantage.

Unlike the Opportunity Scholarship Program established under s. 1002.38, F.S., students receiving a scholarship under the tax credit scholarship program are not required to take the Florida Comprehensive Assessment Test (FCAT). FCAT is designed to promote accountability in the state's education system by measuring annual learning gains. The FCAT tests whether a student has achieved the Sunshine State Standards as adopted by the state.

For the most part, private schools do not teach the Sunshine State Standards. Rather, most private schools have indicated that they administer some form of a standardized examination to measure student performance against a comparable peer group. The results on these nationally standardized examinations are not reported to the state. Moreover, these results are not correlated with the FCAT to compare student performance in the private and public schools or with the Sunshine State Standards.

Technical Changes

The law should be amended to conform to the terminology and the vesting of rulemaking authority in the State Board of Education contained in the rewrite of the Florida School Code.

RECOMMENDATIONS

Recommendations with respect to the tax credit scholarship program are designed to improve accountability under the program:

- Require the State Board of Education to use its rulemaking authority to implement the program. As the head of the Department of Education, the State Board of Education should be a much more visible and active force in providing leadership to improve the program.
- Require the State Board of Education to establish by rule the scholarship-funding approval process.
- Clarify existing statutory enforcement powers of the Department of Education to include, but not be limited to, the power to revoke participation of a scholarship-funding organization, a private school, or a student who fails to follow the law.
- Require the Department of Education to act on a scholarship-funding organization's application to participate in the program within a statutorily prescribed timeframe and to keep adequate records to document its activities with respect to approving scholarship-funding organizations.
- Authorize the Department of Education to request any necessary information related to the program from scholarship-funding organizations and private schools. The Department of Education's use of the sworn compliance form for private schools and scholarship-funding organizations should be expanded and authorized by law. The Department of Education in turn should be required to annually report to the Legislature on its oversight activities.
- Tighten initial eligibility requirements for a scholarship-funding organization to require the entity to be an active corporation in the state appropriately registered with the Department of State and the Department of Agriculture and Consumer Services.
- Require a scholarship-funding organization to obtain proof of a student's attendance at a private school prior to distribution of scholarship funds.

- Require scholarship-funding organizations to verify student income eligibility for every student prior to each academic year through an independent income verification entity.
- Prohibit a scholarship-funding organization from being an actual provider of education services or funding an affiliated entity. A scholarship-funding organization should be prohibited from targeting scholarships to particular private schools or to particular students.
- Require the scholarship-funding organizations to comply with the Florida Single Audit Act with the caveat that the threshold requirements of the act do not apply to the scholarship-funding organizations.
- Restrict the methods of demonstrating fiscal soundness to participate in the program. Private schools should be required to document what insurance types and coverage they possess to include a general liability or premises liability policy. In addition, private schools must provide an opinion letter from an independent certified public accountant that they possess sufficient assets or capital to ensure continued operations through the upcoming academic year. This requirement should be an annual obligation. The number of years in operation by a private school and the purchase of a surety bond for one quarter's scholarship funds should be eliminated as a ground for indicating fiscal soundness.
- Require the State Board of Education to adopt rules identifying the amount of coverage and the amount of assets or capital that constitutes sufficient indicia of fiscal soundness to participate in the program.
- Require the Department of Education to continue to run student lists to verify that a student was previously counted as an FTE the prior academic year in a school district, that a student is not simultaneously receiving funds from other separate scholarship programs, and that a student is not currently enrolled in both a public school and a private school.
- Prohibit a student under the tax credit scholarship program from simultaneously receiving funds from multiple state scholarship sources. In addition, the law should be clarified that a student may not receive scholarship funds from multiple scholarship-funding organizations and provide a mechanism for return of the funds.
- Prohibit a scholarship recipient from authorizing a private school to act as an attorney in fact for purposes of endorsing scholarship checks.
- Require criminal background checks be performed on personnel having direct contact with scholarship funds at a scholarship-funding organization. In addition, private school personnel having direct contact with students should be fingerprinted and the results forwarded to the Department of Education. An individual found to have been convicted of a crime involving moral turpitude should be precluded from being employed in a private school capacity having direct contact with students. Finally, the results of criminal background checks of private school owners or operators should be forwarded to the Department of Education.
- Require the use of certain standardized examinations and the reporting of results to the appropriate parties for use in measuring the effectiveness of the program.
- Amend current law to make technical changes to reflect the participation of private schools. The use of the term "nonpublic school" in s. 220.187, F.S., should be amended to conform to the use of the term "private school" in s. 1002.42, F.S. This amendment would clarify that students in home education programs, as defined in s. 1002.01(1), F.S., are not eligible to participate in the tax credit scholarship program.
- Amend current law to make technical changes to conform to rulemaking authority as provided in the Florida School Code.