

Unpacking Treasury's Proposed Regulations for the Federal Scholarship Tax Credit

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On 10/2/26, the U.S. Department of the Treasury (Treasury) and the Internal Revenue Service (IRS) [published](#) long-awaited proposed regulations implementing section 25F of the Internal Revenue Code, also known as the Federal Scholarship Tax Credit (FSTC).¹ (For an overview on the FSTC, see [Appendix A](#).) The proposed regulations are subject to a 60-day comment period, with comments due [here](#) on 12/1/26, and a [public hearing](#) on 12/15/26. Although they are technically “proposed,” the regulations will govern the FSTC program initially as it goes into effect on 1/1/27.² They will remain in effect until Treasury issues final regulations with a new effective date, which will not likely be before 1/1/28.

This document unpacks the most significant provisions in the proposed regulations that will affect the implementation of the FSTC in states that choose to opt in to the program, particularly regarding uses of the tax credit to support public school students.³ We also flag several issues where the proposed regulations are unclear or raise new important questions.

First, we offer some initial, high-level takeaways:

- **The proposed regulations mostly track the [preview](#) Treasury issued in June about its intended approach, and they further clarify many technical aspects of FSTC implementation.** The regulations provide information about how this program will operate—at least in its first year—regarding state roles and responsibilities, SGO authority and (significant) administrative responsibilities, donor opportunities to receive the tax credit, and student eligibility.
- **Treasury left critical questions unanswered, particularly regarding qualified expenses, on which Treasury has indicated it will issue guidance as soon as possible before the end of the year.** The proposed regulations reference the list of qualified expenses used for Coverdell education savings accounts (including, for example, tutoring, special needs services, and

¹ The FSTC was added by section 70411 of Public Law 119-21, commonly known as the One Big Beautiful Bill Act (OBBBA). The tax credit is also sometimes referred to as the “Education Freedom Tax Credit.” For readability, this document will simply refer to “Treasury” as the primary agency responsible for the proposed regulations.

² Treasury stated that “[t]axpayers, organizations, and States may rely on these proposed regulations for qualified contributions made on or after January 1, 2027, ... provided that taxpayers, organizations, and States follow the portions of the proposed regulations applicable to each in their entirety and in a consistent manner.” Treasury and IRS also issued temporary regulations, which are a subset of the proposed regulations. Treasury’s Acting Assistant Secretary for Tax Policy Kevin Salinger explained that temporary regulations were necessary to comply with the Administrative Procedures Act, that they are identical in substance to the proposed regulations, and that comments on anything in the temporary regulation should be made through the proposed regulation’s comment process.

³ Consistent with our mission, EducationCounsel is working to update and support the field as federal actions consequential to education are unfolding. The information provided in this document is not legal advice and its receipt does not constitute an attorney-client relationship.

extended day programs), which Congress incorporated into the FSTC. But the regulations do not answer how narrowly or broadly Treasury might interpret that statutory list.⁴

- **The regulations restrict discretion for states but provide it to SGOs.** States that choose to participate have limited authority to add program requirements or to decide which organizations appear on their list of approved SGOs. On the other hand, SGOs have discretion over the types of schools, eligible students, and/or eligible expenses they support.
- **SGOs have significant responsibilities for FSTC program implementation, and the proposed regulations create both pathways and challenges for them.** Treasury required that an SGO must meet the annual rule that 90% of its income go to FSTC scholarships based on *all* of the organization's income (not just FSTC contributions). But the regulations also create a much more favorable exception or "safe harbor" for SGOs whose primary focus is on awarding scholarships (of any kind); these SGOs can meet the 90% income rule by defining "income" for these purposes only as the FSTC contributions they receive each year. Also, states have the option of including on their SGO lists any new organizations whose 501(c)(3) status is pending with the IRS.
- **The proposed regulations provide various incentives and clarifications for donors,** including allowing married couples filing jointly to receive up to a \$3,400 credit, explicitly permitting contributions via after-tax payroll deduction, sequencing state and federal tax credits in states that offer such credits, and ensuring that donors may rely on the IRS SGO list when making creditable contributions.
- **The proposed regulations establish multiple methods for SGOs to verify student eligibility, although Treasury only offered a narrow set of streamlined approaches that lower the burden on students and families.** The methods include direct income verification through documentation of income (e.g., W2s) and categorical verification through documenting participation in certain federal benefits programs (e.g., SNAP). Treasury also included two "safe harbors" which allow some students receive scholarships without individual income verification: one for students in foster care and one for students in certain low-income areas who have been identified for tutoring or special needs services.

We have organized this document into the following **four sections** summarizing key provisions of the proposed regulations, with additional relevant commentary in text boxes.

STATES: Limited Authority and Significant Responsibilities

SGOs: Wide Discretion, Clear but Challenging Pathways, and Significant Responsibilities

TAXPAYERS: Boosting FSTC Donations

STUDENTS: Verifying Student Eligibility

Appendix A: Overview of the FSTC Program

Appendix B: Topics Requested for Public Comment

⁴ That said, the preamble to the proposed regulations describes on page 62826 that the Coverdell list as "providing the outer boundaries of qualified expenses," which may suggest that the forthcoming guidance could lean toward a narrow interpretation at least in some areas. (The Coverdell list appears in full in [Appendix A.](#))

STATES: Limited Authority and Significant Responsibilities

Treasury's proposed FSTC regulations clarify how states may opt in (and by when) and establish both limitations and expectations regarding state involvement in the FSTC.

Opt-in Process

Treasury confirmed that a state must opt in on or by 11:59 pm on 1/1/27 to participate in the first year of the FSTC, but set a second deadline of 2/15/27 for states to submit their final list of SGOs that the state has certified. A state's opt-in is not "perfected" (or completed) until the state submits its SGO list. In other words, even if a state opts in on 1/1/27, the state will not participate in the FSTC for 2027 unless the state also submits its SGO list on time. The regulations state that in future years, states will have to both opt in and submit their SGO lists by the first day of each year.⁵ (Prop. Reg. § 1.25F-5(c)(4).)

Limited State Authority

Aside from states' ability to opt into the program (or to opt out by declining to opt in and submit an SGO list, or failing to do so in a timely fashion), the proposed regulations give states little authority to determine whether an SGO will appear on its state SGO list. A state must include on its list all SGOs that want to be on the list and that meet the statutory requirements. The proposed regulations prohibit states from requiring SGOs "to operate in a manner that is more restrictive" than the statutory requirements, such as by only approving SGOs that focus on certain types of students, schools, or categories of expenses. (Prop. Reg. § 1.25F-5(e)(2).) It is important to note both that SGOs themselves have authority to target certain types of qualified students or scholarships, and that states can likely encourage and incentivize donations to certain SGOs, such as SGOs focused on supporting public school students.

Significant State Responsibilities

At the same time, the proposed regulations charge states with certifying SGOs' compliance with the SGO responsibilities discussed in the [SGO section](#) below, most of which must be certified before an SGO can appear on states' SGO lists. States must require SGOs to meet all generally applicable state requirements for charitable organizations, including those related to "transparency, accountability, and fraud protection." (Prop. Reg. § 1.25F-5(e)(1)(i); 1.25F-1(a)(10).) Participating states also must require SGOs in particular "to comply with application, documentation, and financial reporting requirements that are reasonably tailored to" both ensure that the SGO meets the FSTC statutory requirements and "facilitate the prevention and detection of fraud and abuse."⁶ (Prop. Reg. § 1.25F-5(e)(1)(ii).) And importantly, states would have to certify that their own policies and procedures "[e]nable the state to make its own determination" that each SGO on its list is in compliance with the statutory and proposed regulatory

⁵ The proposed regulations also provide for an advance election process with a September 30 deadline that states would have to follow when opting into the FSTC for the first time. (Prop. Reg. § 1.25F-5(c)(3)(i)(B)(2).)

⁶ But note that the proposed regulations prohibit the addition of state requirements that are "more restrictive" than the statutory and regulatory requirements on SGOs. (Prop. Reg. § 1.25F-5(e)(2).)

requirements for SGOs (described in more detail below). The level of assessment that Treasury expects for these state certifications is not clear, and while the number and breadth of requirements on SGOs will give states some insight into SGOs' operations, the prohibition against more restrictive state requirements could limit states to a fairly superficial examination. Much will depend on Treasury's (and states') implementation of these provisions, but on their face, they seem to leave little room for states to add substantive or reporting requirements related to the quality or effectiveness of SGO-funded services or items, or even the detection of waste.

Additionally, under the proposed regulations, a state may remove an SGO from the state list if the SGO does not meet the statutory or regulatory SGO requirements or the state criteria described above, so long as the state provides the SGO with due process. (Prop. Reg. § 1.25F-5(d)(7)(iii).) But this suggests that removal must be limited to noncompliance with specific, existing provisions and, again, the proposed regulations likely curtail states' authority to add requirements beyond those specified.

Opportunities for States to Protect Consumers and Support Public School Students

As detailed above, the proposed regulations both limit states' ability to shape the FSTC program and charge states with significant compliance duties. However, there are also opportunities for states to do more. At a minimum, these requirements suggest that states can—and should—play an important consumer protection role in ensuring that taxpayers contribute funds to legitimate organizations and that SGOs are responsible stewards of those funds.

And because proposed section 1.25F-5(e)(2) only limits what states may *require* SGOs to do, states likely can encourage or incentivize voluntary actions by SGOs and donors that align with states' goals and theories of action for how the FSTC will operate in their contexts. For instance, although the state list must include all eligible SGOs, a state could likely use a number of strategies to highlight those SGOs that align with the state's theory of action, support public school students, serve students under a certain income threshold, and/or submit information on the value, quality, and effectiveness of the expenses paid with their scholarships. States could also explore creating lawful incentives for taxpayers to donate to this subset of SGOs.

See [*Implementing the Federal Scholarship Tax Credit to Maximize Supports for Public School Students: Considerations for State-Level Leaders*](#) for more considerations for state-level leaders in participating states who are seeking to use the FSTC to support public school students.

SGOs: Wide Discretion, Clear but Challenging Pathways, and Significant Responsibilities

Treasury's proposed FSTC regulations define how SGOs can meet the "90 percent of income spending requirement" ("90% income rule") and assign them multiple responsibilities that will require significant capacity and infrastructure.

90% Income Rule and Safe Harbor

The FSTC statute requires that SGOs spend 90% of each year's income on scholarships to remain eligible to appear on a state's list. As Treasury previewed, the proposed regulations would define "income" to be *all* of an SGO's income, so an organization seeking to qualify as an SGO could only use 10% of its income for overhead expenses and any non-FSTC-scholarship programs.⁷ (Prop. Reg. § 1.25F-3(c)(4)(ii).) Under the proposed regulations, SGOs must spend 90% of income by the end of the year following the taxable year the donations were received.⁸ (Prop. Reg. § 1.25F-3(c)(4)(iii).) Even with the additional year, Treasury's interpretation of this 90% rule will likely be a significant challenge for many non-profit organizations, including education foundations, that often provide other (non-scholarship) types of support to school districts and their students.

However, the proposed regulations also create a significant safe harbor that allows some SGOs to calculate compliance with the 90% income rule using only the funds in the SGO's segregated account for its FSTC donations.⁹ (Prop. Reg. § 1.25F-3(c)(3).) The proposed regulations clarify that an SGO can qualify for the safe harbor if 85% of its activities are scholarship-granting in nature ("85% calculation"). For purposes of this test, the activities can be about any type of scholarships, not just FSTC-funded scholarships.¹⁰ Furthermore, SGOs can include in the 85% calculation all expenses that support their scholarship granting, such as "administrative, fundraising, governance, investment, compliance, outreach, and other activities...to the extent each such activity is conducted in support of scholarship granting activities." (Prop. Reg. § 1.25F-3(c)(2)(i).)

The proposed regulations allow for "multistate SGOs" that appear on multiple states' SGO lists. These SGOs must maintain a separate FSTC-segregated account for each relevant state. (Prop. Reg. § 1.25F-1(a)(11); 1.25F-3(c)(3).) A multistate SGO must meet the 85% calculation, and then the SGO's

⁷ Prop. Reg. § 1.25F-3(c)(4)(ii) defines "income of the organization" as "the total gross receipts of the organization from all sources computed using the cash receipts and disbursements method of accounting under § 446(c)(1) and § 1.446-1(c)(1)(i) during its annual accounting period, unreduced by any expenses, regardless of the overall method used by the organization in its books and records."

⁸ As Treasury summarized, "[t]hus, satisfaction of the 90 percent of income spending requirement for the SGO's first year of operation does not need to be met until the end of its second year of operation." This additional flexibility will be helpful both at the beginning of the FSTC program as well as each year in the future, given how much charitable giving tends to occur toward the end of the calendar year.

⁹ The FSTC statute, reaffirmed in Prop. Reg. § 1.25F-3(b)(2), requires that all SGOs maintain a segregated account to prevent commingling of FSTC donations with other income the SGO may have.

¹⁰ The proposed regulations specify that the activities would count "whether pursuant to section 25F, in accordance with State tax credit scholarship rules, or any other scholarship granting activities." (Prop. Reg. § 1.25F-3(c)(2)(i).)

compliance with other statutory requirements (like the 90% income rule and the requirement to grant at least 10 scholarships per year) will be measured separately for each state account.

Because many of the nonprofit organizations currently using donations to support public schools, like education foundations, likely engage in a range of activities (i.e., scholarship granting does not make up 85% of their activities), such organizations may have to establish a new 501(c)(3) organization if they want to serve as an SGO. If the new nonprofit organization is focused on FSTC scholarships, or generally on granting scholarships of all types, it will likely be well-positioned to take advantage of the safe harbor and thus more easily satisfy the 90% income rule.

Recognizing that the 90% income rule likely will require the creation of new nonprofit organizations, and that the granting of tax-exempt status can sometimes take many months, Treasury included a provision that allows states to include all SGOs with a pending 501(c)(3) status to appear on their SGO lists.¹¹ This should make it easier for organizations to establish public-school focused SGOs in the first year of FSTC implementation because, without the rule, these “pending” SGOs would have been excluded from the state list until at least 2028. At the same time, states are not required to take advantage of this option, and donors likely cannot rely on SGO eligibility for tax credit until the SGOs receive tax-exempt status and are added to the IRS SGO list.¹² Given these timing pressures, establishing SGOs that are seeking to serve public school students in participating states is likely a priority area for action.

Significant SGO Responsibilities

The proposed regulations place a number of substantive and administrative responsibilities on SGOs. Depending on Treasury's implementation of these requirements, this may pose a challenge for new SGOs aiming to support public school students, but it may also give rise to opportunities for states to monitor SGOs for fraud and abuse and for schools and districts to create collaborative relationships with SGOs.

Among other things, each SGO must:

- Maintain compliance with FSTC statutory requirements (e.g., maintaining a segregated account for FSTC contributions, ensuring 90% of its annual income is used on scholarships, and annually granting at least 10 scholarships to students at more than one school) (Prop. Reg. § 1.25F-3(b));
- Register for the IRS SGO portal and consent to being placed on the IRS SGO list, which will be distinct from the state lists (Prop. Reg. § 1.25F-4(b));
- Timely provide donors with acknowledgment and information about their contributions (Prop. Reg. § 1.25F-4(c)(1)(i)–(ii));
- Verify the individual or categorical eligibility of scholarship recipients (Prop. Reg. § 1.25F-3(c)(6));¹³

¹¹ The regulations require that these “organization[s] tax-exempt status, if granted, will be effective retroactively to a date that is on or before January 1 of the year for which the State SGO list applies.” (Prop. Reg. § 1.25F-5(d)(5).)

¹² SGOs with a pending 501(c)(3) status will not also be added to the IRS's SGO list until their status is approved. (Prop. Reg. § 1.25F-5(d)(9)(ii).) The regulations allow taxpayers to rely on the IRS SGO list but not on individual state SGO lists. (Prop. Reg. § 1.25F-2(b)(1).)

¹³ In addition to verifying a student's household income before awarding them a scholarship, SGOs must also make sure the student resides solely in the state in which the SGO is operating (regardless of what state the student's

- Verify that its scholarships are used only for qualified expenses (Prop. Reg. § 1.25F-3(c)(5)(i));
- Make payments in one of four approved ways (Prop. Reg. § 1.25F-3(c)(5)(ii)–(v)), including:
 - reimbursements to families who have paid for qualified expenses and can provide appropriate documentation;
 - direct payments to schools for “tuition, fees, room and board, and other similar expenses described in [the statutory list of eligible expenses] that are charged by the school” (note that these “must” be paid directly to the school);
 - payments to verified third-party vendors (see text box below); and
 - use of a “qualified digital wallet” that the SGO does not retain control over.¹⁴
- Complete two annual audits—a financial audit and a programmatic audit, described in more detail below—and submit them to each state in which they participate.

Potential Opportunity for Schools/Districts to Influence Provider Quality

An SGO may pay the providers of services or items (i.e., “third-party vendors”) directly if the vendor has “been verified as an appropriate provider of such services or items.” (Prop. Reg. § 1.25F-3(c)(5)(iv).) Because SGOs may not be in the best position to evaluate providers, schools or school districts may consider creating lists of trusted providers (i.e., those that use evidence-based methodology or demonstrate their effectiveness, etc.) that they can share with SGOs.

Oversight of SGOs

As noted above, SGOs will be required to submit annually to each state in which they participate both a financial and programmatic audit. The programmatic audit would evaluate the SGO’s compliance with FSTC statutory and regulatory requirements (e.g., spending 90% of income on scholarships).

The proposed regulations will also require SGOs to submit annual reports to the IRS containing information on the number of students who applied for scholarships, the number of scholarships granted, the number of schools recipients attended, the amounts of the scholarships, the types of education expenses for which scholarships were used, and the SGO’s income and spending. (Prop. Reg. § 1.25F-4(d)(3).) Treasury explained in its preamble that this data will help states assess SGO’s statutory and regulatory compliance.

school is located in). The proposed regulations take a more flexible approach to this residency rule for children in military families and children of people living on Indian Lands. (Prop. Reg. § 1.25F-3(c)(7)(ii).)

¹⁴ Treasury defines “qualified digital wallets,” which are more commonly used in connection with states’ education savings account programs, as “an electronic payment platform in which a third-party provider provides a streamlined interface for managing the administration of section 25F scholarships by having eligible students and their families submit purchase requests, tracking approved expenses, and maintaining controls to ensure that all payments are made for qualified elementary or secondary education expenses by pre-approving vendors and paying vendors directly or requiring timely submission of receipts.” Treasury is seeking comments on this.

TAXPAYERS: Boosting FSTC Donations

Treasury's proposed regulations include multiple provisions that seem designed to encourage donor participation in the FSTC. Indeed, Treasury estimates that by 2030—after only three years of implementation of the tax credit—eleven million taxpayers will contribute to SGOs, generating \$26 billion per year. That level of revenue would surpass the largest federal elementary and secondary funding programs, including Title I (currently \$18 billion) and IDEA (currently \$13 billion).

The proposed regulations make it easier for taxpayers to contribute to SGOs in a number of ways, by clarifying that:

- The \$1,700 credit cap is on each individual, so married individuals filing jointly can receive up to a \$3,400 credit each year (Prop. Reg. § 1.25F-2(a)(2));
- Donations may be made through after-tax payroll deductions, which can help donors reach the \$1,700 maximum without affecting their take-home pay, making it much more likely that individuals at various income levels can contribute (Prop. Reg. § 1.25F-1(a)(12)(iii)(A));¹⁵
- Under certain circumstances, taxpayers may be able to take advantage of both the federal tax credit and any available state tax credit for donations to SGOs, although not on the same dollars (Prop. Reg. § 1.25F-1(a)(22) and § 1.25F-2(c)(2));
- Taxpayers can carry over any unused portion of the tax credit for five years, meaning that anyone who contributes to an SGO but whose tax liability for that year is ultimately less than \$1700 (or the amount of the donation, if the donation is less than \$1700) can instead use the unused portion against a future year's tax liability (Prop. Reg. § 1.25F-2(e)(1)–(3)).

Donor Obligations and Process

Additionally, the proposed regulations place other requirements on donors before they can receive the tax credit. When making a donation, taxpayers must declare their intent to apply the donation to the FSTC (Prop. Reg. § 1.25F-1(a)(12).), and they must file a form with their taxes providing the IRS with information about each qualified contribution.¹⁶

¹⁵ Note that taxpayers would have to both elect to take payroll deductions and adjust their withholding in order to ensure that their take-home pay is unaffected.

¹⁶ The proposed regulations refer to “Form 8525, Federal Scholarship Tax Credit.”

STUDENTS: Verifying Student Eligibility

Treasury's proposed regulations include several provisions regarding the eligibility of students and families who can benefit from FSTC-funded scholarships. The statute itself established a broad program, setting the income threshold at 300% of area median gross income, which on its own Treasury estimates would make 95% of all schoolchildren eligible for the program. Treasury's proposed regulations include provisions designed to streamline income verification for some students who will be able to more easily demonstrate their eligibility, including two safe harbors that allows some students to be deemed eligible without first providing individual documentation.

Income Verification

SGOs may verify students' eligibility through a direct income verification method by reviewing documents. SGOs will be permitted to accept a variety of documentation, including but not limited to W-2s, pay stubs, and the previous year's tax returns. This method would also limit the type of income that will count for purposes of calculating a family's income.¹⁷

Importantly, the regulations also allow for a categorical verification method, which automatically deems a student eligible for the FSTC if they produce documentation indicating that someone in the student's household is already participating in one of five means-tested federal programs: Supplemental Nutrition Assistance Program (SNAP), Temporary Assistance for Needy Families (TANF), the Special Supplemental Nutrition Program for Women, Infants, and Children (WIC), Section 8 housing, or Supplemental Security Income (SSI). Note that the list of qualifying programs does not include others that could have been part of the categorical method, such as the Free and Reduced Meals (FARM) program.¹⁸

Safe Harbors for Automatic Eligibility

The proposed regulations also contain two "safe harbors" that would deem students eligible even without individualized income verification. First, as originally previewed by Treasury, students in foster care will be automatically eligible for FSTC scholarships. Second, the proposed regulations create a safe harbor for students in certain low-income areas receiving scholarships for tutoring or special needs services that meet a number of programmatic requirements. (Prop. Reg. § 1.25F-3(c)(6)(iii)(C).)

Under this latter safe harbor, students must attend a school located in a low-income area or attend a school in which 80% of the students live in a low-income area, regardless of the location of the school.¹⁹

¹⁷ Treasury explained on page 62827 of the preamble that "in determining the household income of an eligible student, the proposed regulations would disregard items not received in cash by a member of the household because such items are unlikely to be documented and verifiable. The proposed regulations, therefore, would disregard the amount of a Section 8 housing allowance, any imputed return on assets, and other items not received in cash."

¹⁸ Treasury explained that participation in FARM would not suffice where a student attends a school with community eligibility for that program. However, it stopped short of including individualized FARM eligibility on this list for categorical eligibility under the FSTC, perhaps because it relies on self-attestation by families.

¹⁹ For purposes of this safe harbor, a low-income area is one that "is located in a qualified census tract, as identified at https://www.huduser.gov/portal/sadda/sadda_gct.html (or successor website), or in guidance published in the

But the safe harbor includes several restrictions. Students are only eligible if they are receiving scholarships for individual academic tutoring or special needs services, rather than the full range of qualified expense categories—a narrowing that the proposed regulations do not explain. And students must be “selected by the school on the basis of the particular student’s academic or special need.” Further, an SGO providing a scholarship pursuant to this safe harbor would be required to annually obtain and provide to the relevant state a third-party audit demonstrating that:

- The school meets one of the safe harbor’s income standards;
- Scholarship recipients were selected by the school based on academic or other need; “tutors or other providers were qualified to render the services obtained with scholarship funds”;
- Each student’s need for services was independently diagnosed by a professional unaffiliated with the provider or vendor; and
- “[S]ervices met appropriate quality standards, were provided with a duration and frequency commonly required to produce benefit and their impact on each individual scholarship recipient was assessed.”

The proposed regulations do not explain what standards the auditor should use to assess the providers or services.

Eligibility for Pre-K Students

Treasury left open a significant question about the eligibility of a subset of students: those in pre-kindergarten (pre-K). The proposed regulations adopt the definition of “school” used for Coverdell accounts: “any school which provides elementary education or secondary education (kindergarten through grade 12), as determined under state law.” In practice, the terms in this definition are in tension with one another. The definition seems to defer to state law, but states differ in what they include in the term “elementary education.” In many states, it begins in pre-K, rather than kindergarten as the Coverdell definition’s parenthetical suggests. The proposed regulations do not resolve this tension. It is possible that Treasury shares more about its interpretation of this issue in its forthcoming guidance. (It is also worth noting that, under the statute’s definition of “eligible student,” a student’s FSTC eligibility is not based on the grade they are in but rather their eligibility to enroll in an elementary or secondary school.)

Federal Register or Internal Revenue Bulletin (see §§ 601.601(d)(2) and 601.602 of this chapter) or, as appropriate, in forms, instructions, and publications available on <https://www.irs.gov>.” According to the U.S. Department of Housing and Urban Development, these tracts are [defined](#) as having “50 percent of households with incomes below 60 percent of the Area Median Gross Income (AMGI) or have a poverty rate of 25 percent or more.”

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Although the proposed regulations likely will govern at least the first year of the program, there is still much that needs to be finalized at the federal, state, and local levels to maximize supports for public school students (particularly those most disadvantaged) and minimize risks to public education. On the federal level, it is important that Treasury produce clear, accurate, inclusive guidance on both qualified expenses and schools, and commenting on the proposed regulations (including at the public hearing) is an important opportunity to shape the final regulations.²⁰

As discussed in our [recent FSTC publication](#), there are many practical considerations, decision points, and strategies that state leaders (in and out of government) in participating states may want to consider as they contemplate how to implement the FSTC in a way that promotes public school uses. And significant infrastructure building is needed to support SGOs (and schools) in participating states that provide scholarships for public school students and to ensure the appropriate quantity and quality of providers to meet new demand. Although the proposed regulations provide some much-needed information on the FSTC, the clarity and work needed to implement it to the benefit of public school students is just beginning.

²⁰ A list of topics on which Treasury specifically requested comments is available at Appendix B. Treasury has also said publicly that it welcomes feedback on stakeholders' on-the-ground experience with implementation throughout the 2027 rollout of the FSTC.

Appendix A: Overview of the FSTC Program

The One Big Beautiful Bill Act established a significant new federal scholarship tax credit (FSTC). Beginning in 2027, taxpayers can receive a dollar-for-dollar federal tax credit up to \$1,700 each year for contributions to Scholarship Granting Organizations (SGOs) in participating states that fund scholarships for eligible students to support qualified education expenses related to enrollment in a public (including charter), private, or religious school.

The FSTC has very limited statutory language, including the following key program elements:

- Each governor (or other state official designated under state law) must choose each year for the state to participate in the tax credit program and provide the U.S. Department of the Treasury (Treasury) with a list of eligible SGOs in the state to which taxpayers can donate and receive federal tax credit.
- SGOs are nonprofit organizations (excluding private foundations) that, among other requirements, spend at least 90% of income on scholarships and provide scholarships for 10 or more eligible students who do not all attend the same school. The SGOs also cannot “ earmark or set aside” contributions for any particular student.
- Eligible students are members of a household with income less than 300% of the area median gross income and are eligible to enroll in public elementary or secondary school in the state (though they need not be enrolled in public school).
- Scholarships can be provided for any amount but must be used only for eligible expenses, which are defined in the law by reference to the existing federal Coverdell education savings account program, which names the following as “qualified elementary and secondary education expenses”:
 - “expenses for tuition, fees, academic tutoring, special needs services in the case of a special needs beneficiary, books, supplies, and other equipment which are incurred in connection with...enrollment or attendance...at a public, private, or religious school,”
 - expenses for room and board, uniforms, transportation, and supplementary items and services (including extended day programs) which are required or provided by [the school] in connection with such enrollment or attendance, and
 - Expenses for the purchase of any computer technology or equipment or internet access and related services, if such technology, equipment, or services are to be used by the beneficiary and the beneficiary’s family during any of the years the beneficiary is in school.”

Appendix B: Topics Requested for Public Comment

Below is a list of topics (with references to the relevant page of the [proposed regulations](#)' preamble) about which Treasury has specifically requested comments. Commenters need not comment on all, or any, of these topics in order to submit comments.

- The definition of qualified digital wallet and whether final regulations should include additional safe harbors for verification that scholarships are spent on qualified elementary or secondary education expenses (p. 62820).
- The need for further guidance regarding how an organization measures its scholarship-granting activities and whether 85% is a reasonable threshold (p. 62824).
- How requirements in section 501(c)(3) interact with section 25F and whether any clarifications are needed in the final regulations (p. 62826).
- Whether there are other needs-based programs, including State or Tribal programs, that also should be considered as categorical evidence of eligibility when verifying household income (p. 62827).
- The certifications States would be required to make, including any that would be required for a multistate SGO (p. 62834).
- Whether any of the required State certifications would be too burdensome (p. 62834).
- The number of entities affected by the proposed regulations and their economic impact on small entities (p. 62850).
- Whether there are less burdensome alternatives that would adequately mitigate the risk of fraud or improper scholarships (p. 62851).
- Whether the proposed rule would create any overlapping, duplicative, or conflicting requirements (p. 62851).
- “[A]ll aspects of the proposed regulation” (p. 62852).

In addition to submitting public comments by 12/1/26, Treasury has [set](#) the same deadline for “[r]equests to speak and outlines of topics to be discussed at the public hearing.” Anyone seeking to attend the public hearing must submit a request by 5:00 pm ET on 12/10/26.