

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

BILL: CS/SB 2978

SPONSOR: Education Committee

SUBJECT: Corporate Tax Credit Scholarship Program

DATE: March 25, 2004 REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Matthews</u>	<u>O'Farrell</u>	<u>ED</u>	<u>Favorable/CS</u>
2.	_____	_____	<u>AED</u>	_____
3.	_____	_____	<u>AP</u>	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

I. Summary:

This committee substitute (CS) is designed to implement fiscal and academic accountability in the Corporate Tax Credit Scholarship Program (CTC) by:

- Requiring a nonprofit scholarship-funding organization (SFO) to file its audit with the Auditor General and the Department of Education (DOE) within 180 days after completion of the SFO's fiscal year;
- Requiring an SFO to obtain verification of student attendance at a private school;
- Prohibiting an SFO from commingling funds, transferring scholarship funds between SFOs, and drawing upon a line of credit to fund scholarships;
- Requiring an SFO to conduct income eligibility verification of students;
- Requiring criminal background checks of certain employees and officers of SFOs and private schools;
- Requiring the Department of Law Enforcement to retain certain fingerprint records in a database and match the records against arrest fingerprint cards;
- Eliminates certain private schools such as correspondence schools and distance learning from the list of eligible private schools under the CTC program;
- Revising the fiscal soundness requirements of private schools to require a surety bond in certain circumstances;
- Requiring a private school to employ or contract with certain qualified teachers;
- Prohibiting a home school from participating in the program;
- Requiring a private school to annually administer or make provisions for scholarship students to take the Iowa Test of Basic Skills, the Stanford-9, or the Florida Comprehensive Assessment Test;

- Requiring a private school to report to DOE and to scholarship applicants whether certain regional accrediting associations accredit the school and, if so, the name of the accrediting association.
- Prohibiting a student from simultaneously receiving a scholarship under the John M. McKay Scholarships for Students with Disabilities Program (McKay scholarship) or the Opportunity Scholarship Program (OSP) while receiving a CTC scholarship;
- Requiring the DOE to annually determine the eligibility of SFOs, private schools, and students;
- Requiring the DOE to revoke the eligibility of SFOs, private schools, and students who fail to meet the requirements of the CTC program;
- Requiring the DOE to select an independent private research organization to analyze student performance data and report to the DOE on year-to-year improvements without disclosing a student's or private school's identity;
- Requiring the DOE to report on its accountability activities to the Governor and the Legislature; and
- Requiring the State Board of Education (SBE) to adopt rules to implement the program.

In addition, the CS revises the small business participation cap to one percent and authorizes a taxpayer to rescind its tax credit application under certain defined circumstances.

This CS substantially amends s. 220.187, F.S.

II. Present Situation:

Since its inception in 2001, the Corporate Tax Credit Scholarship Program (CTC) has provided approximately 28,000 scholarships to students in need by offering parents an option of enrolling their children in a private school. Anecdotally, the program is extremely popular with the parents whose children are participating in the program. However, the CTC program has serious fiscal and academic accountability deficiencies that, if not corrected, threaten the continued viability of the program. As a result, the Senate President, James E. "Jim" King, Jr., directed the Senate Education Committee to conduct an interim study of the CTC program. The Education Committee specifically found that the CTC program suffered from any real meaningful state oversight and that the system of self-policing by participating SFOs and private schools had essentially failed.¹ Accordingly, the Education Committee voted unanimously to draft legislation to implement accountability in the CTC program.²

Section 220.187, F.S., the Statutory Framework

The 2001 Legislature enacted the CTC program for implementation in the 2002 tax year. Under the program, corporate taxpayers may take a dollar for dollar credit for contributions to SFOs that provide a scholarship to a student who qualifies for free or reduced-price school lunches under the National School Lunch Act, and who:

- Was counted as a full-time equivalent student during the previous state fiscal year for purposes of state per-student funding;

¹ The Florida Senate, *Corporate Tax Credit Scholarship Program Accountability*, Interim Project Report 2004-132.

² Agenda, Senate Education Committee, October 21, 2003.

- Is eligible to enter kindergarten or the first grade³; or
- Received a scholarship under the CTC program the previous school year.

The Legislature initially capped the CTC program at \$50 million in tax credits per state fiscal year but subsequently expanded the cap to \$88 million in 2003.⁴ Although s. 220.187(3)(b), F.S., sets the annual cap per state fiscal year, the provision has been interpreted to mean a tax year wrapped up in a calendar year. This interpretation results in a counterintuitive application of the tax credit to the annual cap. The following chart demonstrates two separate taxpayers and the differences between which cap year is used and when the contribution is made.

Taxpayer	Taxpayer's tax year	Tax Credit Application	Annual Cap	Contribution
Taxpayer A	Jan. 03 – Dec. 03	Approved in June 03	Counts toward 2003	Made before end of Dec. 03
Taxpayer B	Mar. 03 – Feb. 04	Approved in Jan. 04	Counts toward 2003	Made before end of Feb. 04

The tax credit application and the annual cap operate independently from the actual contribution made by the taxpayer to the scholarship-funding organization for distribution towards scholarships. The contribution must be made by the end of the taxpayer's tax year or the tax credit may not be used.

Taxpayers

A taxpayer may not contribute more than \$5 million to any scholarship-funding organization and may not designate a specific child or group of children as the beneficiaries of the scholarship. A taxpayer may carry forward any unused amount of the tax credit for up to three years; however, the carry-forward is counted towards the annual cap in each year the carry-forward is used. Five percent of the tax credit is reserved for small businesses as defined under s. 288.703(1), F.S.⁵

Scholarship-Funding Organizations (SFOs)

An SFO must be a charitable organization exempt from federal income tax pursuant to s. 501(c)(3) of the Internal Revenue Code. The SFO must spend all of the contributions for scholarships in the state fiscal year⁶ in which received. An SFO may not use any portion of the contribution for administrative expenses. An annual financial and compliance audit is required of the SFO, which must be filed with the Auditor General.

An SFO may offer two separate scholarships: a \$3500 maximum scholarship for tuition, textbook expenses, or transportation to attend an eligible private school, 75 percent of which

³ The 2002 Legislature expanded student qualification to include students eligible to enter kindergarten or the first grade. See s. 42, ch. 2002-218, L.O.F.

⁴ s. 9, ch. 2003-391, L.O.F.

⁵ Section 288.703(1), F.S., defines a small business as an independently owned and operated business concern that employs 200 or fewer permanent full-time employees and that, together with its affiliates, has a net worth of not more than \$5 million or any firm based in this state that has a Small Business Administration 8(a) certification.

⁶ July to June.

must be used for tuition; and a \$500 maximum scholarship for transportation expenses to a public school located in another school district.

Private Schools

A participating private school must meet fiscal soundness requirements by:

- Having been in operation for at least one year;
- Providing DOE with a statement from a certified public accountant confirming that the private school is insured and has sufficient capital or credit to operate the school for the upcoming year serving the number of students anticipated with expected revenues that are reasonably expected; or
- Providing a surety bond or letter of credit for an amount equal to the scholarship funds for any quarter.

In addition, eligible private schools must comply with state and local health and safety laws and codes, the 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 (DOE)

DOE is required to annually submit to the Department of Revenue (DOR) by March 15 a list of eligible SFOs that meet the statutory requirements. In addition, DOE is required to monitor the eligibility of the SFOs, the private schools, and the expenditures under the program. DOE must adopt rules, as necessary, to determine the eligibility requirements of the SFOs and to identify qualified students.

The Department of Revenue (DOR)

DOR must adopt 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.

Operation of the CTC Program

For tax year 2002, DOR approved 76 tax credit applications for 49 taxpayers for \$47,902,000. Four taxpayers were small businesses that were approved for tax credits for \$186,000. DOR approved 60 tax credit applications for 32 corporations for \$47,579,000 for tax year 2003. Two taxpayers were small businesses that were approved to contribute \$79,000. Approximately seven firms contributed both years of the program.

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

SFO	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	\$0	\$0	\$0

Scholarship Foundation of Florida			
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 ⁷	unknown
Yes Opportunities	\$0	\$1,050,000	\$250,000

According to unverified data provided by the SFOs,⁸ 970 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. In FY 2003-2004, 11,585 students received scholarships from 923 participating schools.⁹

Interim Project 2004-132

After surveying DOE and the SFOs, reviewing s. 220.187, F.S., and conducting numerous interviews, the Education Committee adopted the following findings made in the CTC interim project study:

- There is little or no state oversight of the CTC program;
- SBE has not provided any guidance in improving accountability in the CTC program;
- Initial approval criteria of SFOs are easily met and the documentation establishing the eligibility is not kept;
- There has been little or no monitoring of the eligibility of SFOs;
- There has been little or no monitoring of the eligibility of private schools;
- There has been little or no monitoring of the eligibility of students;
- DOE’s enforcement powers are not explicit;
- There is no statutory requirement to document attendance for purposes of receiving a scholarship;
- There is no statutory prohibition on an SFO designating a particular child for a scholarship;
- There is no statutory prohibition on a student receiving a scholarship from other state scholarship programs for students in private schools;
- There are insufficient criminal background checks being conducted on private school personnel having direct contact with students and SFO personnel having access to scholarship funds; and

⁷ The Silver Archer Foundation LTD received \$412,500 in tax year 2003. Silver Archer did not respond to the committee’s survey. The Chairman and Director of the Silver Archer Foundation was arrested and charged with Grand Theft in the first degree. DOE has removed Silver Archer Foundation from the list of approved SFOs.

⁸ Id.

⁹ According to DOE as of February 9, 2004.

- There is insufficient academic accountability.

Lack of State Oversight over the CTC program

The report found that there is very little or no state oversight of the CTC program. Instead, the SFOs appear to have been largely delegated the authority to operate the program. Unfortunately, when an SFO fails to implement its delegated authority, DOE is unable to effectively account for the expenditure of funds, regulate the participation of private schools, and identify participating students.

Role of the State Board of Education (SBE)

SBE has not provided DOE sufficient guidance to improve accountability in the program. SBE has not used its rulemaking authority to resolve issues such as the eligibility criteria for SFOs, the identification of qualified students, the monitoring of SFOs and private schools, and expenditures under the program.

Initial Approval of Scholarship-Funding Organizations (SFOs)

The criteria for initial approval of SFOs are easily met and DOE does not routinely retain documentation supporting participation in the program. To initially qualify, an SFO 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. By requiring an SFO 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 an SFO must provide.

Monitoring the Eligibility of Scholarship-funding Organizations (SFOs)

Once approved, SFOs are not routinely monitored to ensure compliance with the law. DOE has narrowly interpreted its oversight authority as being limited to reviewing audits and responding to complaints.¹⁰ Since the earliest that any audits were filed was August 2003, by its own admission, DOE did not exercise any oversight authority prior to that date, relying exclusively on the SFOs to police the program. In any event, it is not clear who at DOE reviews the audits. In response to the committee's request for a report on any SFO that did not comply with the requirement to spend all of its contributed funds for scholarships in the state fiscal year in which received, DOE failed to acknowledge that an SFO had undisbursed scholarship funds at the close of the state fiscal year.¹¹

Monitoring the Eligibility of Private Schools

Without the assistance of the SFOs and before implementation of the sworn compliance form, DOE could not identify which private schools are participating in the program.

Current 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

¹⁰ Response from DOE to committee survey dated October 14, 2003.

¹¹ 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.

operation for more than one year indicates that a private school is more likely to be in operation the following year.

Monitoring the Eligibility of Students

DOE has largely delegated determinations of eligibility for students to participate in the program to the SFOs. Prior to the implementation of the database, DOE did not know which children are participating in the program unless supplied this information by the SFOs.

The law requires DOE to adopt rules establishing the eligibility of students. However, SBE has not adopted rules mandating income verifications for purposes of determining a student's eligibility. Certain SFOs have voluntarily contracted with a company that performs income determinations for the National School Lunch Act to determine student eligibility. However, certain SFOs only conduct income determinations on a sampling basis.¹²

Enforcement of the Law

The law should be amended to clarify DOE'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 an SFO require proof of a student's attendance at a participating private school prior to each scholarship payment. Accordingly, DOE and certain SFOs do not know whether a student is actually attending the private school.¹³ 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 an SFO designating a particular child or private school for receipt of a scholarship. An SFO that administers a private school could circumvent the statutory prohibition and allow a taxpayer to contribute to a specific SFO 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 the McKay scholarship, the OPS program, or the CTC program.

Criminal Background Checks

The criminal background checks currently performed fail to ensure that private school personnel who have been convicted of a crime involving moral turpitude do not have direct contact with students. The personnel of an SFO 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.

¹² FloridaChild

¹³ FloridaChild

Academic Accountability

There are no state-mandated academic accountability requirements under the CTC 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 OSP established under s. 1002.38, F.S., students receiving a scholarship under the CTC 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.

Recommendations

The Education Committee adopted the following recommendations with respect to preparing a bill for improving accountability in the CTC program:

- Require SBE to use its rulemaking authority to implement the program. As the head of DOE, SBE should be a much more visible and active force in providing leadership to improve the program.
- Require SBE to establish by rule the SFO approval process.
- Clarify existing statutory enforcement powers of DOE to include, but not be limited to, the power to revoke participation of an SFO, a private school, or a student who fails to follow the law.
- Require DOE to act on an SFO'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 SFOs.
- Authorize DOE to request any necessary information related to the program from SFOs and private schools. DOE's use of the sworn compliance form for private schools and SFOs should be expanded and authorized by law. DOE in turn should be required to annually report to the Legislature on its oversight activities.
- Tighten initial eligibility requirements for an SFO 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 an SFO to obtain proof of a student's attendance at a private school prior to distribution of scholarship funds.
- Require an SFO to verify student income eligibility for every student prior to each academic year through an independent income verification entity.
- Prohibit an SFO from being an actual provider of education services, funding an affiliated entity, or targeting scholarships to particular private schools or students.

- Require an SFO to comply with the Florida Single Audit Act with the caveat that the threshold requirements of the act do not apply to the SFOs.
- 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 SBE 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 DOE 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 CTC 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 SFOs 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 an SFO. In addition, private school personnel having direct contact with students should be fingerprinted and the results forwarded to DOE. 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 DOE.
- 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.
- Clarify that a student in home education programs is ineligible to participate in the CTC program.
- Amend current law to make technical changes to conform to rulemaking authority as provided in the Florida School Code.

Department of Financial Services Audit

Subsequent to the interim project study, the Department of Financial Services (DFS) conducted a review of the CTC program and made the following findings:

Legislative recommendations

- Each SFO should pass a fiscal sufficiency test. This would involve each SFO demonstrating that there is sufficient current and future expectation of revenue sources to properly administer scholarships.
- New SFOs should demonstrate that they have processes in place to properly account for scholarship funds.
- The SFO principals and private school officials need to pass a criminal background check. Other due diligence procedures for SFOs should include bankruptcy history, credit checks and lawsuit history.
- The SFOs and private schools should have a state charter and be physically located within the State.
- For program purposes, the types of eligible private schools should be defined by statute.
- The Legislature should consider the imposition of suspension or permanent removal of SFO eligibility when an SFO cannot demonstrate accountability of funds or there is material noncompliance with law.
- The Legislature should consider adding a statutory provision so that scholarships granted under the CTC program cannot be combined with the McKay or OPS scholarships.
- The Legislature should consider amending s. 220.187(4)(e), F.S., and include a provision that each SFO shall demonstrate the matching of current funding received to pay scholarship obligations for the current or upcoming school year.
- The Legislature should address the timeframe of funding availability. Currently, there is no provision in the statute to prevent an SFO from developing financing schemes with current corporate contributions or from granting scholarships for past or future periods.
- In addition, some SFOs have managed irregular short-term cash flow patterns with the use of a line of credit. An SFO should not use a line of credit to finance an increase in the scholarship base with the anticipation that future corporate contributions will be greater to debt service the obligation.
- The Legislature should consider limiting scholarship funding transfers between SFOs. Funding transfers conflict with the current statute and increase the level of risk, that funding may not be appropriately used.
- The Legislature should consider establishing a mechanism to restore unused tax credit allocation when corporations contribute less than the DOR preapproved amounts.
- The Legislature should consider a scaled phase-out of a student's scholarship if the student becomes ineligible due to a slight increase in the parent's salary.
- The Legislature should address the Auditor General's use of audit reports, unless it is determined that the single audit provision should be included in s. 220.187, F.S.

State Board of Education (SBE) recommendations

- The SBE should adopt administrative rules for the effective administration of the CTC program.
- The CTC program meets the requirements of "State Financial Assistance" and is therefore subject to the Florida Single Audit Act.
- To provide reasonable assurance that program funding is being used for the purpose as prescribed by law, DOE should establish a program management function. Program management should include, but is not limited to the following functions:

- Procedures and actions to ensure legal compliance and accountability of funding.
- Procedures and actions to ensure eligibility determinations of students, private schools and SFOs.
- The DOE's use of financial audit reports (single audit) as a component of program management.
- The DOE's requirement for SFOs to submit monthly reports on funding and students.
- Verification of school attendance for scholarship recipients.
- On an exception basis, perform site visits of SFOs and private schools.
- Perform reconciliations of tax credits, SFOs, schools and students.
- Perform database crosschecks for public school enrollments and other scholarship programs to prevent multiple payments per student.
- The DOE must establish a database with relevant program, SFO, school, student and funding data. Contrary to information provided by DOE, prior to October 2003, no system existed for tracking funding by student.
- Within the context of rules, DOE should establish and implement written operating procedures to meet legal compliance and accountability requirements.
- DOE should establish a formal process to ensure that all participating private schools have met the statutory eligibility requirements. Prior to October 2003, DOE could not demonstrate how these requirements were being met. Currently, DOE has chosen to use a sworn compliance form as a means of updating the private school database and determining school eligibility. DOE should also implement a process to spot check and confirm reported compliance through requests for supporting documentation.
- In order to facilitate the program management function and to implement provisions of the Florida Single Audit Act, DOE should enter into written agreements with each SFO. The agreements should include, but not be limited to the following:
 - Description of the allowable uses of program funds.
 - SFO and scholarship recipient responsibilities.
 - Attendance and a testing mechanism to ensure that a student received a quality education.
 - State single audit requirements.
 - Required information to be sent to DOE to assist in the program management function.
 - The suspension or permanent removal of SFO eligibility.
- DOE should reconcile tax credit funding to students. To provide subsequent accountability and to develop an expectation for the current funding levels, DOE should reconcile pre-approved tax credits to funding for each SFO, school and student.
- Each SFO should establish a process to corroborate and document school attendance. Currently, most SFOs rely on the honor system whereby it is up to each private school to notify the SFO when students are not attending.
- DOE should require each SFO to formalize their processes by including written procedures, corroborating evidence and signed approvals.
- Each SFO should establish accounting processes and bank accounts to maintain funding identity. DFS noted one SFO where the receipt, transfer and subsequent disbursement of funds were conducted in such a way as to not maintain funding identity.

- Each SFO should establish written procedures and prohibitions on certain related party transactions. DFS noted where one SFO is affiliated with two schools to which all of the SFO's scholarship funds are directed. This appears to violate s. 220.187(2) (b), F.S., where a taxpayer cannot direct funding to a specific child as beneficiary. In addition, DFS noted some instances where parents of students were also employees of the schools where the students attended.
- Each SFO should establish a system to ensure that checks are endorsed in accordance with law. Each SFO should establish a system of review and follow-up of cleared scholarship checks to ensure that parents and schools are in compliance with law. DFS noted various check endorsements that did not comply with statute. In addition, the Legislature may consider providing additional statutory language prohibiting a restrictive power of attorney where a school can endorse checks on behalf of parents.
- Each SFO should provide periodic information transfers to DOE to track students and funding and to prevent possible double dipping between SFOs and other scholarship programs.
- DFS reviewed the six funded SFOs authorized by DOE. DFS concluded that five SFOs maintained a process to accomplish program objectives and that program funding was used to pay scholarships. However, DFS noted that Florida Child had the following irregularities:
 - DFS was unable to attest to the validity of the information maintained in the financial system. In addition, DFS noted that the information is not always complete and does not always agree with the banking records.
 - DFS was unable to attest to the validity of the eligibility process. In the second year of the program, eligibility of the applicants was only verified on a sample basis. Coupled with the online application process, this increases the risk of phantom students.
 - FloridaChild has not maintained a system of budgeting and cash management. FloridaChild has borrowed \$5.2 million on a line of credit with SunTrust Bank. This is to maintain and expand a scholarship base that cannot be maintained on current cash projections. The most significant problem is that future corporate contributions are obligated to pay the liability. This affects the period of funding availability where current corporate contributions should match to current obligations. This also violates the securing of corporate contributions to meet current needs. The scholarship base should not be leveraged.
 - FloridaChild has received \$1.85 million in funds from other SFOs in order to fund the scholarship base. This violates the law where each SFO secures funds for the current need.
 - Other SFOs wrote \$1.7 million in checks to fund the FloridaChild scholarship base. These other SFOs are relying on whether Florida-Child has conducted proper eligibility requirements and there is a satisfactory system of internal control to account for the disbursement of these funds.
 - FloridaChild employs the honor system of attendance reporting from private schools prior to disbursing funds.
 - FloridaChild did not perform bank reconciliations in the second year of the program.
 - FloridaChild charges a \$15 dollar application fee to the parent in order to cover their administrative costs.

- FloridaChild sent a letter to each school requesting 2 percent of the scholarship funding awarded be provided as a donation to fund administrative expenses.

DFS referred the irregularities to the Office of Fiscal Integrity.

Department of Education actions

DOE has instituted some reforms. It did implement a sworn compliance form in October 2003. As a result, 41 schools participating in the CTC and McKay Scholarship programs did not receive voucher funding because of a failure to comply with the sworn compliance form.¹⁴ DOE instituted its database for CTC students sometime between October and December 2003 and discovered eight students in 2002 received more than the \$3500 allowed under the CTC program.¹⁵ DOE also suspended CTC funds to a private school when it was informed by an SFO that someone other than the parents signed the scholarship checks.¹⁶ Finally, DOE has recommended legislative action to improve the CTC program.

III. Effect of Proposed Changes:

The CS purports to provide both fiscal and academic accountability with respect to the CTC program by requiring the following:

Taxpayers

The CS reduces the small business cap reserve from five percent to one percent. This reduction would allow larger corporations to contribute more funds for scholarships based on their contribution history. Based on a \$55 million cap, DOR reserves \$2.5 million for small businesses and \$4.4 million for small businesses based on an \$88 million cap.¹⁷ However, for tax credit years 2002 and 2003, DOR only approved \$186,000 and \$79,000 in tax credit applications for small businesses, respectively.¹⁸ Accordingly, \$2,314,000 was not allocated in tax credit year 2002 and \$2,421,000 has not been allocated for tax credit year 2003.

The CS authorizes a taxpayer to rescind its application for a CTC tax credit if DOR has accepted the rescindment application, the taxpayer has not made a rescindment within the previous three tax years, and the taxpayer has not contributed under its tax credit application that it intends to rescind. Any rescindment tax credit shall be reallocated to the annual cap for approval by DOR on a first-come, first-served basis following the date the rescindment is accepted by DOR. This provision would free up tax credit approvals for other eligible taxpayers if a taxpayer determines that it does not have any tax liability for that tax year. According to DOR, two taxpayers have indicated their desire to rescind their tax credit approval based on their estimated tax liability at the conclusion of their tax year.

¹⁴ Palm Beach Post, November 13, 2003, *State drops schools from voucher list*

¹⁵ Monday Report, Volume XXXVIII, Number 25, October 20, 2003.

¹⁶ Palm Beach Post, February 21, 2004, *Check flap may fuel close of voucher-supported school*

¹⁷ For Fiscal Year 2003-2004 only, the statewide tax credit allocation cap was reduced to \$50 million pursuant to s. 1, ch. 2003-424, L.O.F.

¹⁸ DOR approvals of small businesses tax credit are as of February 25, 2004. However, the tax credit year 2003 does not end until the earlier of the exhaustion of the cap or December 2004.

Scholarship-Funding Organizations (SFOs)

The CS requires an SFO to file an annual financial and compliance audit with the Auditor General and DOE within 180 days after completion of the SFO's fiscal year. This provision shortens the time in the current Auditor General rule for providing an audit from nine months to six. A reduction in the timeframe for conducting the audit ensures that DOE can detect any programmatic shortcomings of an SFO more quickly. Any timeframe for compliance shorter than six months is potentially unsustainable. This deadline for submission of the audit is more stringent than the nine months provided in the Florida Single Audit Act.

The CS requires the Auditor General to review all SFO audit reports and request any significant items that were omitted. The SFO has 45 days to submit the requested information. If the SFO does not comply with the additional item request, the Auditor General must report the SFO to the Legislative Auditing Committee, who may schedule a hearing and determine if the SFO should be subject to further state action. If the Legislative Auditing Committee determines that further state action is needed, it shall inform DOE to revoke the eligibility of the SFO to participate in the CTC program. This provision ensures that SFO audits are conducted properly and to provide any additional information necessary for DOE to determine if an SFO complies with the programmatic requirements of the CTC program. This provision tracks the powers of the Auditor General under s. 11.45(7)(b), F.S.

The CS requires an SFO to make at least quarterly payments of a scholarship to an eligible private school on behalf of a qualified student. The law is silent concerning the timing of scholarship payments to qualified students. This provision codifies the existing practice of certain SFOs that make scholarship installments on a quarterly basis. In addition, the provision provides uniformity to the scholarship warrants such that parents and eligible private schools can have a greater certainty in the delivery of scholarship funds.

The CS requires an SFO to maintain scholarship funds in a separate account. This provision provides greater assurances that the statutory prohibitions on using scholarship funds for administrative expenses and the statutory requirement that all interest on scholarship funds is used for scholarships are properly implemented.

The CS requires an SFO to obtain verification from a private school of each student's attendance at the private school prior to each scholarship payment. The law is silent on requiring proof of a student's attendance and invites the potential for a fraud by a private school by collecting scholarship funds for a student that is not in attendance at the private school. This provision codifies the existing practice of certain SFOs that require proof of attendance prior to submitting scholarship warrants.

The CS requires an SFO to verify the income eligibility of each scholarship applicant participating in the program at least once each school year pursuant to rules of SBE. The law defines a qualified student, in pertinent part, as a student who qualifies for free or reduced-price lunches under the income eligibility requirements of the National School Lunch Act. This provision is necessary to ensure that only students who are eligible for free or reduced-price lunches may receive a CTC scholarship. The CS accomplishes this objective by requiring an annual income verification to ensure that a student who initially qualified under the National

School Lunch Act for a scholarship has not had a significant increase in family household income such that the student is ineligible.

The CS requires an SFO to prepare and submit quarterly reports to DOE. In addition, an SFO must immediately respond to any DOE request for additional information relating to the CTC program. This provision is necessary to ensure that DOE can monitor and verify the continued eligibility of an SFO.

The CS requires certain individuals at an SFO, upon employment and every five years thereafter, to undergo and meet level two criminal background-screening standards as provided in s. 435.02, F.S. The CS defines those individuals subject to the criminal background check as the SFO owner, president, chairperson of the board of directors, superintendent, principal, or person with equivalent decision-making authority who owns, operates or administers an SFO. In addition, any individual at an SFO that has access to scholarship funds is also subject to a criminal background check. These individuals must file a complete set of fingerprints, taken by an authorized law enforcement agency or an employee of the SFO trained to take fingerprints, with DOE. DOE shall file the fingerprints with the Department of Law Enforcement (FDLE) for state processing, which shall in turn file the fingerprints with the Federal Bureau of Investigation for federal processing. Individuals found to have committed a crime involving moral turpitude or failing to meet level two screening requirements may not be employed, contracted with, or engaged to provide services. The SFO or the SFO personnel being checked must absorb the cost of the background check.

The CS requires FDLE to retain fingerprint records beginning July 1, 2004, and to match the retained fingerprints, beginning December 15, 2004, with any arrest fingerprint records. FDLE shall report any match of an arrest record with a retained fingerprint record to DOE. The SFO must report any change in status of an owner to FDLE. FDLE shall adopt a rule establishing a fee, which shall be borne by the SFO or the owner. This provision is necessary to ensure that scholarship funds are not entrusted to an individual with a prior criminal record.

The CS requires an SFO to comply with the antidiscrimination provisions of 42 U.S.C. s. 2000d. Under current law, only private schools were statutorily required to comply.

The CS prohibits an SFO from owning or operating a private school participating in the CTC program. This provision is designed to prohibit an SFO from targeting scholarships to a particular school or child. Under current law, only the taxpayer is prohibited from targeting scholarships. In practice, this provision may require the SFO, Academy Prep Foundation, to reorganize or discontinue its relationship with the Academy Prep private schools, which it currently provides CTC scholarships.

The CS requires an SFO to report to the DOE any private school not in compliance with the CTC program. Pending resolution by the SBE, the private school may not receive CTC scholarships from an SFO. This provision is designed to ensure that a private school that does not comply with the law does not continue to receive scholarships.

The CS requires an SFO to allow a qualified student to transfer his or her scholarship to another eligible private school. This provision codifies the existing practice of SFOs and provides parents an option to transfer their student if the current private school does not meet their needs.

The CS requires an SFO to distribute scholarships to qualified students on a first-come, first-served basis unless the student qualifies for priority by virtue of being a prior year scholarship recipient. This provision is designed to promote fairness in the selection of students for a scholarship.

The CS prohibits an SFO from transferring scholarship funds to another SFO. This provision matches the DFS report and is designed to accomplish three objectives:

- Once scholarship funds are transferred between SFOs there are no means of detecting the identity of the funds such that the \$5 million cap on a taxpayer to a particular SFO can be circumvented;
- An SFO may only accept contributions for which it has identified qualified students; and
- The bar prohibits an SFO that is leveraging its scholarship base from receiving a bailout from other SFOs to continue operations.

The CS prohibits an SFO from using a line of credit or other financing schemes to fund scholarships in anticipation of eligible contributions. This provision matches the DFS report and is designed to prevent an SFO from:

- Circumventing the requirement that an SFO spend 100 percent of the eligible contributions in the same state fiscal year in which the contribution was received;
- Using non-eligible contributions to fund scholarships;
- Leveraging its scholarship base as the SFO is unable to meet its liability (scholarship payments to qualified students) if an eligible contribution that is pledged to a particular SFO is not received; and
- Undermining any certainty in the enrollment estimating conference for purposes of determining the budget.

Certain SFOs have been able to successfully use a line of credit as a means of smoothing out the peaks and troughs associated with the different timeframes for contributions and scholarship payments.¹⁹ Unfortunately, other SFOs have not been so lucky. FloridaChild drew upon a \$5.2 million line of credit and found it unable to make payment with pledged contributions.

The CS prohibits an SFO that fails to comply with this section from participating in the CTC program. This provision operates in tandem with DOE's enforcement powers to revoke the participation of SFOs that fail to comply with the law.

Parental and Student Obligations

The CS imposes additional parental and student obligations to ensure accountability and provide an opportunity for a quality education. In particular, the CS:

- Requires a student to comply with the private school's attendance policies;
- Requires a parent to comply with the private school's parental involvement policies;

¹⁹ Arguably, using a line of credit in this manner violates s. 220.187, F.S.

- Prohibits a parent from authorizing the private school, its owners, or employees from acting as an attorney in fact for purposes of endorsing scholarship warrants; and
- Requires a parent to ensure that their student participates in the required testing.

A student or parent that fails to comply with these requirements may not participate in the CTC scholarship program.

Private Schools

The CS imposes accountability measures on private schools as a condition for participating in the scholarship program.

The CS places additional restrictions on the type of private schools that may participate in the program. The CS prohibits a correspondence school or distance learning school from participating in the CTC program. In addition, a private school must maintain a physical location in this state where a scholarship student regularly attends classes and may not direct or provide scholarship funds to a parent of a scholarship student who receives instruction under the program at home. This provision clarifies the original legislative intent to preclude the participation of these entities in the CTC program.

The CS requires a private school demonstrate fiscal soundness by filing with DOE a surety bond equal to the scholarship amount per each quarter of the school year. This surety bond requirement extends from the time of initial participation in the program and for three consecutive years thereafter. However, a private school that has participated in the program for three consecutive years and has not had any disciplinary action taken against it by DOE is exempted from this requirement. Any private school that was disciplined by DOE for actions in violation of the CTC program must file a surety bond following the disciplinary action and prior to the next quarter, and for two additional consecutive years thereafter.

Under current law, a private school only needs to be in operation for at least one year and it is exempted from demonstrating fiscal soundness through a letter of credit, surety bond, or a statement from an accountant that the private school has sufficient capital or credit. More than 90 percent of all private schools demonstrated fiscal soundness by being in operation for more than one year. However, these schools are not regulated by the state with respect to their fiscal integrity. Accordingly, the number of years a school has operated does not provide adequate safeguards that a student's education continuity would not be disrupted because of a weak business model or poor financial management. Of the 1167 private schools participating in the Opportunity Scholarship Program, McKay Scholarship Program, and the CTC program, only three percent have been in operation less than one year and only 19 percent have been in operation less than three years.²⁰ This provision provides assurances to the state that a participating private school is fiscally sound.

The CS requires a private school to employ or contract with teachers who have regular and direct contact with each student receiving a CTC scholarship at the school's physical location. This provision is designed to prevent internet and correspondence schools from participating in the CTC program. In addition, the CS requires a private school to hire teachers who hold at least a

²⁰ Source: Department of Education

baccalaureate degree, have at least 3 years of teaching experience, or have special expertise that qualifies the teacher to provide instruction in subjects taught. The CS requires the private school to report to DOE the number of teachers employed or under contract, along with the manner in which the teacher is qualified to provide instruction to CTC students. The reporting requirement is designed to present DOE with information that may be included in the online prospectus of each private school participating in the program for the benefit of parents.

The CS requires the private school to annually register with DOE by providing the school's legal name, location, list of owners, list of students participating in the CTC program, and a notification of the private school's intent to participate in the program.

The CS requires certain individuals at a private school, upon employment and every five years thereafter, to undergo and meet level two criminal background-screening standards as provided in s. 435.02, F.S. The CS defines those individuals subject to the criminal background check as the private school owner, president, chairperson of the board of directors, superintendent, principal, or person with equivalent decision-making authority who owns, operates or administers a private school. In addition, any individual at a private school that has direct contact with students or has access to scholarship funds is also subject to a criminal background check. These individuals must file a complete set of fingerprints, taken by an authorized law enforcement agency or an employee of the private school trained to take fingerprints, with DOE. DOE shall file the fingerprints with the Department of Law Enforcement (FDLE) for state processing, which shall in turn file the fingerprints with the Federal Bureau of Investigation for federal processing. Individuals found to have committed a crime involving moral turpitude or failing to meet level two screening requirements may not be employed, contracted with, or engaged to provide services. The private school or the private school personnel being checked must absorb the cost of the background check.

The CS requires FDLE to retain fingerprint records beginning July 1, 2004, and to match the retained fingerprints, beginning December 15, 2004, with any arrest fingerprint records. FDLE shall report any match of an arrest record with a retained fingerprint record to DOE. The private school must report any change in status of an employee, contractor, or volunteer to FDLE. FDLE shall adopt a rule establishing a fee, which shall be borne by the private school, the employee, contractor, volunteer, or the owner. This provision is necessary to ensure that an individual with a prior criminal record does not have direct contact with students.

The CS requires the private school to annually administer or make provisions for scholarship students to take the Iowa Test of Basic Skills, the Stanford-9, or the Florida Comprehensive Assessment Test, or subsequent versions of these tests. A participating private school must report a student's scores to the parent and to the independent private research organization selected by DOE. This provision is designed to provide academic accountability in the program such that the state can measure if it is receiving an appropriate rate of return on its investment. In addition, academic accountability would provide a parent with more information to assist a parent in making an informed decision on whether to enroll or continue the studies of his or her child in a particular private school.

The CS requires a private school to annually comply with DOE's affidavit requirements. This provision provides statutory authority for DOE to conduct the sworn compliance form.

The CS requires a private school to provide written notification to DOE and the SFO within seven days if a student is ineligible to participate in the program.

The CS requires a private school to annually report to DOE and to scholarship applicants whether the school has been in existence for 3 years or less. This provision is designed to give parents more information concerning the longevity of the private school.

The CS requires a private school to annually report to DOE and to scholarship applicants whether the private school is accredited or in the process of receiving accreditation candidate status, and if so, the name of the accrediting association. DOE must make the list of accredited and nonaccredited private schools available to the public by county. This provision is designed to give scholarship applicants information concerning the accreditation status of private schools participating in the program so that the parent can make an informed decision concerning the enrollment of their child at the private school.

The CS provides that a private school that fails to comply with this section is ineligible to participate in the CTC program. This provision operates in tandem with DOE's enforcement powers to revoke the participation of private schools that fail to comply with the law.

Department of Education

The CS imposes additional obligations on DOE and clarifies existing ones to improve accountability in the CTC program.

The CS requires DOE to annually determine the eligibility of SFOs and private schools to participate in the program. DOE must act on a first year SFO's application for participation in the program within 90 days of receipt, and must provide written notice of approval or denial and the reasons for the determination to the SFO. DOE must maintain a list of eligible private schools and make that list accessible to the public.

The CS requires DOE to annually verify the eligibility of students. DOE must maintain a database of CTC students and run the database, at least quarterly, to ensure that a student is not receiving a McKay Scholarship, Opportunity Scholarship, attending another private school, or attending a public school. This provision is designed to prevent a private school from double dipping or reporting phantom students.

The CS requires DOE to annually review all SFO audit reports for compliance with this section.

The CS requires DOE to annually administer affidavits to private schools in accordance with SBE rules. This provision provides statutory authority for the sworn compliance form.

The CS requires DOE to select an independent private research organization (IPRO) to which participating private schools must report CTC student scores. The IPRO must annually report to DOE the year-to-year improvements of participating students. In addition, the IPRO must analyze and report student performance data in a manner that comports with 20 U.S.C. s. 1232g to protect the identity of students. The IPRO is prohibited from reporting data at a disaggregated level, which would reveal the student's identity or the private school. This provision is designed

to ensure that the state can monitor the performance of students under the CTC program and measure program effectiveness on an output basis. DOE has indicated that it will fund the IPRO out of existing funds of the department and will not require an appropriation.

The CS clarifies that DOE must revoke the eligibility of SFOs, private schools, or students who fail to meet the requirements for participation in the CTC program.

The CS requires DOE to report annually to the Governor and the Legislature on its accountability actions, including an annual report on substantiated allegations or violations of law or rule by an SFO or a private school and the specific corrective action taken by DOE to cure the violation. This provision is designed to provide information to the Legislature to determine the scope of program defects and to ensure that DOE is complying with its programmatic requirements.

Rulemaking

Section 120.54(1)(a), F.S., provides that agency rulemaking is not a matter of agency discretion. Unfortunately, SBE has decided not to adopt any rules in the three years that the CTC program has been in existence. The CS requires SBE to adopt rules pursuant to ss. 120.536(1), F.S., and 120.54, F.S.:

- To administer s. 220.187, F.S.;
- To determine the eligibility of SFOs and private schools;
- To identify qualified students;
- To identify the documentation required to establish eligibility for SFOs;
- To require an affidavit of private schools; and
- To identify the income verification requirements of students.

Delegation

The CS authorizes SBE to delegate its authority, with the exception of rulemaking, to the Commissioner of Education.

Effective date

This act shall take effect upon becoming law.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:**A. Tax/Fee Issues:**

None.

B. Private Sector Impact:

The CS imposes fiscal accountability requirements on private schools and SFOs that would require these entities to incur additional administrative costs. The quantum of these costs is indeterminate at this time.

C. Government Sector Impact:

The extent to which the state may experience a savings by virtue of qualified students entering the CTC program is indeterminate at this time.

DOE has indicated that it will fund the IPRO out of existing funds of the department and will not require an appropriation, although the source of these funds has not been identified.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Amendments:

None.