Federal Scholarship Tax Credit: Employer FAQ

Beginning in 2027, an individual may be eligible for a Federal income tax credit under section 25F of the Internal Revenue Code for certain cash contributions to scholarship granting organizations (SGOs) that fund scholarships for elementary and secondary education expenses. Employers may choose to facilitate employee contributions through after-tax payroll deductions and share general information about how the employee can adjust their Federal income tax withholding using Form W-4.

This guide describes section 25F and the proposed and temporary regulations published on October 2, 2026. The proposed regulations may be relied upon but may change once public comments are received and reviewed.

Facilitating automatic payroll deductions is voluntary. Before starting automatic payroll deductions or providing other advice, employers who wish to effectuate a contribution for which an employee may claim a credit should:

- Check IRS forms and instructions.
- Consider any relevant State and local laws, such as State wage payment laws.
- Confirm that the payroll provider or benefits administrator can transmit employee contributions and donor information.
- For each participating employee, obtain an employee authorization specifying the amount, SGO recipient, designation as a section 25F qualifying contribution and other appropriate designations, start date, and any annual limit or stop date.
- Configure an after-tax deduction and a remittance schedule with your payroll provider.

1. What is the Federal Scholarship Tax Credit (FSTC)?

The FSTC is available for qualified contributions to an SGO made by an individual who is a citizen or resident of the United States. The credit is limited to $1,700 per individual taxpayer for a tax year. A married couple filing jointly may be able to claim up to $3,400 if each spouse makes qualified contributions of up to $1,700.[1]

The credit is nonrefundable: the credit used in a year cannot exceed the applicable Federal income tax liability limit. Unused credits generally may be carried forward for up to five years.[2]

Any qualified contribution for which a credit is allowed, including a credit carried forward to a later year, cannot also be taken into account as a charitable contribution for purposes of section 170. Annual qualified contributions in excess of $1,700 may qualify for a charitable contribution

[1] I.R.C. § 25F(a), (b)(1); Prop. Treas. Reg. § 1.25F-2(a)(2), (h)(2).

[2] I.R.C. §§ 25F(f), 26(a).

deduction if all requirements of section 170 are met. Employees should consult their tax adviser about that deduction.[3]

The amount of the FSTC is reduced by any State tax credit allowed for the same qualified contributions.[4]

Note that contributions cannot be earmarked or set aside for scholarships on behalf of any particular student,[5] and scholarships may not be made to disqualified persons.[6]

2. How will an employee know that the selected charity is an SGO for purposes of the FSTC?

The IRS intends to publish a list of qualifying SGOs that consent to having their information appear on the IRS website (IRS SGO list) starting on or around January 1, 2027. States may finalize their initial 2027 lists through February 15, 2027. The IRS SGO list will be updated as those submissions are processed and will reflect later removals; employees should use the current list instead of relying on earlier versions of the list.[7]

An SGO must be listed on the State SGO list of at least one State for the calendar year in which a contribution is made to that SGO. A taxpayer generally may rely on the fact that an organization is listed on the IRS SGO list (and not listed as removed from that list) at the time a contribution is made to establish that the taxpayer's contribution is being made to an SGO.[8]

The SGO does not need to be in the same State as the employee or employer; a taxpayer can contribute to any SGO on any State SGO list.

As a practical safeguard, the employee should periodically recheck the current IRS SGO list if making recurring contributions. If an SGO is shown as removed, the employee should pause future remittances and consider giving to a different SGO.

3. Does the employee need to have children or have income under a certain threshold in order to claim the FSTC?

No, the employee does not need to have children, and there is no income limitation on donors for eligibility for the FSTC. However, the employee must have sufficient Federal income tax liability, after other applicable credits, to use the credit in that year. Any unused credit is subject to the carryforward rules described in the answer to Question 1.

4. Can an employer facilitate contributions through payroll deductions?

Yes. An employer may facilitate voluntary payroll contributions beginning January 1, 2027, by obtaining the employee's authorization for an after-tax payroll deduction, consistent with applicable law. The program may offer one-time contributions or recurring contributions, not to

[3] I.R.C. § 25F(e)-(f); Prop. Treas. Reg. § 1.25F-2(f).

[4] I.R.C. § 25F(b)(2); Prop. Treas. Reg. § 1.25F-2(c).

[5] I.R.C. § 25F(d)(1)(E); Prop. Treas. Reg. § 1.25F-3(c)(1)(vii).

[6] I.R.C. § 25F(d)(2); Prop. Treas. Reg. § 1.25F-3(b)(4).

[7] Temp. Treas. Reg. § 1.25F-5T(c)(3)(ii)(B), (d)(7)-(9).

[8] Prop. Treas. Reg. § 1.25F-2(b).

exceed a total amount of $1,700 in any year for any employee. Any benefits administrator that offers payroll deduction services may be used if the arrangement preserves the employee's contribution to the SGO and transmits the information listed in question 5 to allow the SGO to issue the employee a timely written acknowledgement.

Employees also may contribute directly to SGOs outside of the employer's program.[9]

The table below shows approximate regular payroll deductions for an elected annual contribution of $1,700. That amount is the annual credit cap, not a required contribution. Adjust the final deduction to reach the employee's elected total.

	Annual		Single Paycheck
	Contribution	Pay Cycles	Contribution
Weekly	$1,700	52	$32.69
Biweekly	$1,700	26	$65.38
Semimonthly	$1,700	24	$70.83
Monthly	$1,700	12	$141.66

- With the regular deductions shown in the table, the amounts will not add up to the full $1,700 for the year. To ensure the full contribution, the final deduction should be increased to $32.81 for weekly pay, $65.50 for biweekly pay, $70.91 for semimonthly pay, or $141.63 for monthly pay. For a midyear start, divide the elected amount by the actual remaining paychecks and adjust for rounding.
- Do not reduce otherwise reportable wages in Form W-2, Box 1, or applicable Social Security and Medicare wages by the contribution. Do not add the contribution to wages a second time. Follow the applicable Form W-2 instructions for employer reporting and check for updates before implementing the program.[10]
- Take the contribution from net pay after required withholding and deductions. Apply any other deduction priorities required by applicable law.

The SGO is responsible for providing the donor a timely written acknowledgement and also reporting the donor's contribution to the IRS. An employer may provide an annual payroll contribution summary to help employees reconcile amounts, but it does not replace the SGO's timely written acknowledgement.

By January 31 following the contribution year, the SGO must provide the employee with a timely written acknowledgement that includes a unique donor number. Employees will substantiate their qualified contributions by reporting this unique donor number on their tax return, as required by the applicable return instructions.

Employees should contact the SGO promptly if a timely written acknowledgement is missing or incorrect. Pay statements may show the payroll deductions, but the timely written acknowledgement provides the donor number and contribution information used to substantiate

[9] I.R.C. § 25F(a)-(c); Temp. Treas. Reg. § 1.25F-1T(a)(12)(iii)(A).

[10] Temp. Treas. Reg. § 1.25F-4T(c)(1)-(2); IRS, General Instructions for Forms W-2 and W-3, Specific Instructions, Boxes 1, 3, and 5 (2026).

the credit. Employers should remind departing employees to keep their contact information current with the SGO.

5. What information must accompany payroll contributions?

For the employee's contributions to be eligible for the credit, the employer must provide the SGO with the employee's name and address, as well as the amount designated by that employee as a qualified contribution under section 25F. Employers should obtain that designation with the employee's authorization to make the payroll deduction. If the SGO is on the State SGO list of more than one State, the employee's authorization also should specify the State(s) to which the contribution is to be allocated. The SSN of the employee should not be provided to the SGO.

6. How does an employee's 25F designation work?

A section 25F designation is irrevocable once made; employees may change future payroll elections but cannot revoke a designation for a completed contribution.[11]

An employee cannot authorize a payroll deduction for any contribution attributable to the employee's spouse or any other person. Thus, for example, if each spouse wants to contribute $1,700 to an SGO to obtain a $3,400 credit on their joint return, then each spouse must donate separately and obtain a separate unique donor number. One spouse may not authorize payroll deductions for both spouses' contributions.

7. Can the employee adjust Federal income tax withholding to account for an expected credit?

Yes. The employee may submit a new Form W-4 to adjust Federal income tax withholding to account for an expected credit. The employee would do this by listing the expected FSTC in Step 3 of the Form W-4, together with any other applicable credits. The expected credit estimate should reflect expected qualifying contributions, the $1,700 cap, relevant State credits, and the tax liability limitation.

An employee with multiple jobs or a working spouse should follow the Form W-4 instructions for the household and avoid counting the same expected credit on multiple forms. The IRS Tax Withholding Estimator at www.irs.gov/W4App can help account for multiple jobs, other income, credits, and changes during the year.[12]

Making a payroll contribution election and revising a Form W-4 are two separate decisions. Employees may contribute without changing Form W-4, and authorizing a contribution does not itself change withholding. Submitting Form W-4 does not claim the credit or guarantee eligibility. If contributions change or stop, employees should review their withholding and submit a new Form W-4 if needed. Employees making midyear changes should recheck withholding for the following year.

[11] Temp. Treas. Reg. §§ 1.25F-1T(a)(12)(i), 1.25F-4T(c)(2)(i); Prop. Treas. Reg. § 1.25F-3(c)(3).

[12] IRS, Form W-4, at 1-2 (2026), Steps 2-3 and instructions (directing completion of Steps 3-4(b) on only one job's Form W-4); I.R.C. § 25F(b), (f). Use the applicable year's form and instructions.

7. What is a simple example of a modified Form W-4?

Assume an employee starts contributing at the beginning of the year, receives 26 biweekly paychecks, expects to make a total of $1,700 of qualifying contributions, expects no State credit for them, and has enough Federal income tax liability after other applicable credits to use the full FSTC. The employee adds $1,700 to Step 3 of Form W-4. This generally reduces Federal income tax withholding by approximately $65.38 per paycheck, provided sufficient tax would otherwise be withheld.[13]

For a regular paycheck in this example:

- After-tax contribution: $65.38 reduction in take-home pay.
- Federal income tax withholding adjustment: approximately $65.38 increase in take-home pay.
- Combined effect: approximately no change in take-home pay, apart from rounding and the final contribution adjustment described in Question 9.

Without the W-4 change, the contribution reduces take-home pay, and the employee claims any allowable credit when filing a return.

An employee commencing contributions mid-year should use the tax withholding estimator: entering $1,700 in Step 3 does not automatically divide that amount over only the remaining paychecks.

8. How should employers handle remittance timing and year-end contributions?

The credit is allowed for qualified contributions made during the employee's taxable year. Establish a regular remittance schedule with the benefits administrator and SGO and communicate to employees which pay cycle will include the final contribution. For contributions intended for 2027, ensure that deductions are delivered within 2027.[14]

9. How should the deductions be treated for Federal employment tax purposes?

The payroll deduction for the contributions should be taken from the employee's wages after Federal income tax withholding and employment taxes, including Social Security and Medicare withholding. The contributions are not excludable from wages and may not be offered as a pre-tax salary reduction under a cafeteria plan. The employee claims any allowable credit on the employee's Federal income tax return. The employer's role in facilitating an after-tax contribution does not in and of itself establish that the employee qualifies for the credit.[15]

10. Does the employer need to track contributions outside its payroll program?

[13] IRS, Publication 15-T, Worksheet 1A, lines 1b and 3a-3c (2026) (dividing the annual Step 3 amount by annual pay periods and limiting withholding to zero).

[14] I.R.C. § 25F(a), (c)(3); cf. Treas. Reg. § 1.170A-1(b) (ordinarily treating delivery, not transmittal, as the time a charitable contribution is made).

[15] I.R.C. §§ 3121(a), 3401(a) (defining wages); Temp. Treas. Reg. § 1.25F-1T(a)(12)(iii)(A).

No. The employee is responsible for tracking contributions outside the employer's program, combining contributions for the credit limit, and determining the employee's eligibility and other tax consequences. However, employers should reconcile their own payroll deductions and remittances and retain authorizations, contribution amounts and dates, recipient information, and the donor data transmitted.

11. Can an employer match the contribution?

Yes, an employer can match the contribution. Section 25F does not change the employer's Federal income tax treatment of the expense.

An employer-funded match is the employer's contribution and does not increase the employee's section 25F credit. For example, a $1,000 employee contribution and a $1,000 employer match produces only a $1,000 employee contribution for credit purposes, subject to the other credit limits. Identify the match separately in payments and donor records.

Provided that the match was not available to the employee as compensation, the employer's match would not be taxable as gross income or wages to the employee. An arrangement allowing the employee to choose cash instead of the match would require a separate tax analysis.