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Education Savings Accounts: A Path to Give All Children an Effective Education and Prepare Them for Life

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EXECUTIVE SUMMARY

All parents want an effective school for their child. But no parent should have to take the drastic steps that Yolanda Miranda took to give her children a chance at a good education: Yolanda went to jail and was charged with grand larceny for sending her children to better schools in their grandmother's district instead of their assigned schools.

"If I had to do it again 10 times over, I would," Yolanda says.[1]

Cases like Yolanda's have appeared all over the country, which is not surprising because choices in education vary widely from state to state.[2] We will see more parents like Yolanda as long as parents are denied the right to find the best school for their child. Is it fair for some parents to be able to send their children to better schools because of their zip code?

The most innovative solution to provide all America's children with better opportunities is education savings accounts.[3] Enacted in Arizona in 2011 and expanded in 2012, the savings accounts are parent-controlled bank accounts in which the state deposits funds from the education funding formula. Parents use the accounts much like health savings accounts (HSAs) for medical services and can pay for a variety of expenses, such as tutoring, private school tuition, and online classes.

With developments in technology, families have more options than ever in K–12 education. This report outlines how education savings accounts give parents even more flexibility. Moreover, it offers a road map for other states as they design a similar policy.

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Introduction

Arizona's unique education savings accounts are state-funded bank accounts that families use for education expenses. Parents operate the accounts, and they have discretion over different services and materials (see the bulleted list in the next paragraph). The state's department of education and treasurer's office coordinate to deposit student funds from the school funding formula into the accounts. Conceived by the Goldwater Institute in 2005 and passed into law in Arizona in 2011, the accounts offer parents and children more choices in a child's education and allow children to access options either online, across states, or through new devices such as iPads.[4]

Conceived by the Goldwater Institute in 2005 and passed into law in Arizona in 2011, education savings accounts offer parents and children more choices in a child's education and allow children to access options either online, across states, or through new devices such as iPads.

Like HSAs, which allow patients to buy prescription medicine, pay co-pays after a doctor's visit, and pay hospital fees, education savings accounts also give individuals discretion over how money is spent on different products and services. With education savings accounts, the state department provides parents an account number and a check or debit card, and parents use the card or online programs such as PayPal to make purchases or to pay school tuition. In Arizona, approved expenses include the following:

- Private school tuition
- Textbooks
- Education therapy
- Online classes
- Tutoring
- Standardized testing
- 529 college savings plans
- College tuition
- Individual public school classes and extracurricular programs

Arizona Governor Jan Brewer signed the accounts into law in 2011, after the state supreme court ruled unconstitutional the state's two opportunity scholarship or voucher programs (one for children with special needs and another for children in foster care). The 2011 law made students with special needs eligible for the accounts, and the accounts were expanded in 2012 to include children in failing schools, children of active-duty military families, and adopted children. Because the court's ruling cited the vouchers' limited uses—that is, a voucher could be used only for the single purpose of private school tuition—the new accounts were designed to include multiple uses.[5]

Who Benefits?

Education savings accounts benefit children, parents, and taxpayers alike.

- **Students**. Because the accounts allow families to choose from many different education services, a child's education can be precisely fit to his or her needs. For students with special needs, such as children with autism, cerebral palsy, or hearing or vision impairments, parents can use the funds to send their children to a school that specializes in addressing those challenges. In Arizona, schools such as the Hi-Star Center for Children and Lauren's Institute for Education are two institutions whose primary focus is to serve students who need accommodations. Goldwater Institute research, along with studies from the Manhattan Institute, provide evidence that children with special needs show improved performance when their public school is exposed to competition because of a school choice program.[6]

  Evidence strongly indicates that all types of children perform better academically when they exercise their option to attend a school of choice. Nine studies using the "gold standard" of empirical research—that is, random assignment—where students are chosen by lottery to participate in a school choice program have found that children using opportunity scholarships experience improved academic outcomes.[7] New research finds that the benefits can even extend beyond high school. In the first longitudinal, randomized study of students in a voucher program and college enrollment rates, researchers at Harvard University and the Brookings Institution found that African American students that used an opportunity scholarship to attend private school had college enrollment rates that were 24 percent higher than their peers in traditional schools.[8]

  Children in failing schools are now eligible under Arizona's law. These students should realize benefits similar to students using opportunity scholarships because children using education savings accounts have the same choices and more than students using scholarships.

Because the accounts allow families to choose from many different education services, a child's education can be precisely fit to his or her needs and parents have a newfound ability to search and pay for learning experiences.

- **Parents.** With their newfound ability to search and pay for learning experiences, parents have more flexibility to meet their children's needs. And parents have never had more schools and services to choose from. As Quinn Cummings, author of *The Year of Learning Dangerously: Adventures in Homeschooling*, says,

  > Imagine that your high school junior spends half of every day at the brick-and-mortar school up the street. Two afternoons a week, he logs into an art history seminar being taught by a grad student in Paris. He takes computer animation classes at the local college, sings in the church choir, and dives at the community pool.

Nathan

When Nathan turned six, he was still unable to speak. A few years earlier, Nathan, a dark-haired boy with brown eyes and an infectious smile, had been diagnosed with autism. While his time at a developmental preschool had been a positive experience, said Amanda, Nathan's mom, "There wasn't really anything being learned, it was just fun for him."

Nathan's frustration with background noise, which made it hard for him to concentrate, was compounded by his inability to speak. He wasn't able to tell his mom or teachers what was frustrating him. As a result, he struggled when he entered kindergarten and sat in a class of 30 other children.

Nathan's mom applied for an education savings account for her son in the fall of 2011 and watched as Nathan blossomed in a new school.

Just weeks after using the account to change schools and to pay for a tutoring service, Nathan did something amazing: Amanda was reading to him, and he pointed to a picture on the page and asked, "What's that?" Now it was Amanda's turn to be speechless.

"He's starting to ask questions," Amanda said two months into the new school year, "something he's never done in his life."

> He studies Web design on YouTube. He and three classmates see a tutor at the public library who preps them for AP Chemistry. He practices Spanish on Skype and takes cooking lessons at a nearby restaurant every Saturday morning.[9]

Education savings accounts make potential experiences like these a reality. Today, education is not simply defined by where it is delivered but by how many different ways it is delivered. From online resources such as the Khan Academy videos on YouTube, which cover thousands of subjects, to full-time virtual schools such as Connections Academy and Primavera Online High School, those sources make it easier for students to access education anywhere through the Internet.[10] Parents can become more engaged than ever in their children's education either through the choice of a school (critical for families of children who have special needs, as indicated previously) or, as Cummings explains, through a set of alternatives.

- **Taxpayers**. Education savings accounts offer accountability in education spending and can be a cost savings for taxpayers. With the accounts, the state provides funds directly to families and audits every purchase, instead of funding schools, where revenues and expenses are difficult to track. Savings account families then report expenses to the state (Arizona's audit procedures are described on page 9). Every penny is accounted for. With savings accounts, the state and taxpayers know exactly where and how money is spent.

How do taxpayers save on costs? In Arizona, the state deposits 90 percent of student funds from the funding formula into an account that is available for individual students. The state's department of education reserves some of the remaining 10 percent of student funds to administer the program and saves the rest. Thus, each student using a savings account actually saves money for the state.

Education savings accounts will have drastic results for states with complicated funding formulas. In Arizona, taxpayers spend some $125 million on empty seats in traditional schools because of outdated student information software that is designed to fund the system, not students.[11] The money spent on empty seats unfairly pays the wrong institution for a child's education. Savings accounts eliminate inefficient practices like these.

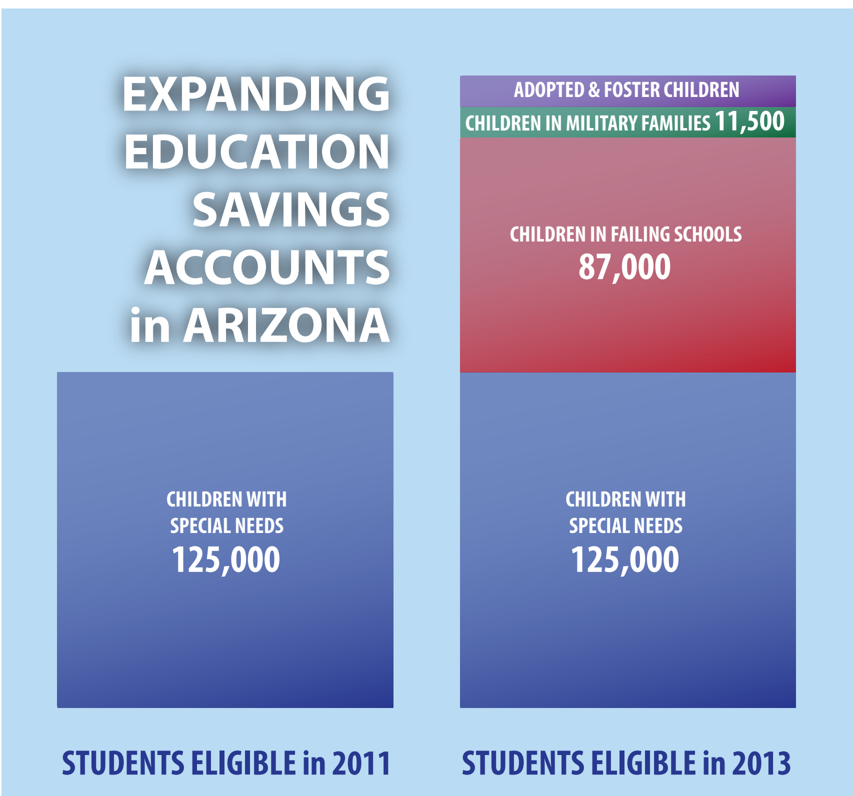
Arizona's Experience with Education Savings Accounts

Arizona lawmakers passed the first savings account bill, S.B. 1553, in 2011.[12] The bill made Arizona's 125,000 students with special needs eligible to apply. Students must have attended a traditional school in the previous year. Parents sign a contract with the state's department of education and agree not to enroll their child full time in a traditional school while using an account (otherwise, parents would be using student funds twice, once in the account and then again at a traditional school). Parents of students with special needs must also submit documentation on their children's needs, such as their Individualized Education Plans or Multidisciplinary Education Team plans. The allowable expenses listed on page 2 were included in this first law, although the program's expansion in 2012 specifically stated that public school classes could be purchased a la carte and that certain supplies (such as pencils and paper) were not eligible.

The 2012 bill that expanded the program extended eligibility to students in failing schools, children of active-duty military families, and children adopted out of the state's foster care system (those students will be eligible in the 2013–14 school year).[13] Now, nearly one out of every five Arizona public school students—more than 200,000 children, as shown in figure 1—are eligible for an account.[14]

Enacted in 2011, the first bill made 125,000 Arizona students with special needs eligible for an education savings account. The 2012 bill expanded the accounts to more than 200,000 children—nearly one out of every five public school students in the state.

Figure 1. Expanding Education Savings Accounts in Arizona, 2011–13



Aaron

Kelly simply wanted her son, Aaron, to feel welcome at school. Diagnosed with autism at age six, Aaron was assigned a one-on-one specialist because he was considered a flight risk. But Kelly said that he had been placed in a class with students of varying needs and that "I felt he was being overlooked."

His teachers struggled to provide for Aaron, Kelly explained, and the classroom setting just never seemed to fit.

Kelly applied for an education savings account in the program's first year. After moving her son to a school that specialized with autistic students, Kelly said, "We saw the improvement and the changes right away."

Kelly added, "We're grateful to have the Education Savings Account. It's been a really positive experience. We noticed a change from the moment he started going."

Families apply by filling out an application on the Arizona Department of Education's web site and returning it by the due date. Once the application is approved, the department of education and the treasurer's office notify the state's vendor (Bank of America) to send the parents an account number and a check card.

As parents make purchases, they must keep all receipts and submit a report along with the receipts to the department of education at the end of each fiscal quarter. The department reviews the receipts to make sure all purchases are for educational expenses, and then the department signals the treasurer to make the next disbursement. Quarterly disbursements are withheld if any expense did not qualify. In Arizona's first year with the accounts, most of the discrepancies that the department investigated were with parents who did not understand what expenses were qualifying educational expenses and what expenses were not. To provide parents with clearer direction, the department of education offered meetings in the department's offices and online and will release a spending guide for parents in the 2012–13 school year.[15]

In addition to withholding funds, the Arizona Department of Education relies on two measures to prevent fraud and abuse of the accounts. First—and similar to food stamp debit cards—the department "unlocks" certain vendors while restricting others.[16] For example, as the first set of parents using the accounts told the department what schools they had chosen, the department of education allowed the cards to be used at those schools. Likewise, as parents made purchases at online retailers for special equipment or curricular materials, the department allowed those vendors.

This approach will not prevent all illegal expenses, however. Whereas families cannot purchase gas at a Shell service station, for example, because Shell is not an approved seller, families can use the cards at large retailers such as Walmart, where they can buy books and curricular materials. If parents make a purchase at one of those approved retailers, the department must be responsible for reviewing the purchases to make sure all of the expenses are lawful.

Second, the Arizona Department of Education conducts quarterly and annual audits. The annual audit and account balance reconciliation will help the department identify families that spent savings account money but did not submit receipts (suggestions on fraud-prevention procedures are outlined later in this report).

A Model for Education Savings Accounts in Other States

Arizona's experience can inform other states as they consider enacting education savings accounts. State leaders considering the program will need to address four critical areas:

1. **Eligibility.** All students should be eligible for a savings account, just as all children can attend public schools. Whereas savings accounts have the potential to provide specific experiences for children with special needs or in unique circumstances, it is this very feature that makes them so valuable for every student.

   More and more states are enacting private school choice programs with broad eligibility rules. In 2011, Indiana Governor Mitch Daniels signed into law an opportunity scholarship program that allows middle-income and low-income families across the state to participate. In its first year, the Choice Scholarships program enrolled 3,919 students, the largest number of students ever to participate in a scholarship program's inaugural year.[17]

   In 2012, Louisiana Governor Bobby Jindal expanded the state's opportunity scholarship program to include students attending schools rated "C" or below on the state report card. Approximately 380,000 students are eligible.[18]

   Some states may not be prepared to process so many new savings accounts in the program's first year, and Arizona policymakers found that establishing a new financial arrangement with a bank requires time and study. So, as Arizona lawmakers expanded the program, the additional students, such as children in failing schools, were phased in over a short time. This phase-in allowed the state's administrative capability to keep pace with family participation.

2. **Funding**. State funding policies must be updated to accommodate real-time student transfers and funding models where education dollars follow the child.

   In Arizona, schools are paid one year in arrears on the basis of enrollment.[19] Traditional schools submit enrollment reports to the state department of education at the end of the year, and the department sends checks to schools in the next school year on the basis of those counts from the previous year. However, traditional schools can apply for current-year funding increases if the school experiences an enrollment increase. However, no adjustment is made if enrollment decreases. This reporting delay costs taxpayers millions in payments to schools for students who have transferred elsewhere.

Education savings accounts have the potential to provide specific experiences for children with special needs or in unique circumstances. But it is this very feature that makes them so valuable for every student.

When the original education savings account law was passed, lawmakers funded the accounts outside of the traditional funding system. Student accounts were financed through a separate set of funds that had been set aside for children with special needs (the 2012 expansion changed the funding protocols so that accounts now receive money from the traditional school funding stream). Still, the system holds traditional schools harmless for one year after children with special needs leave or are enrolled in the savings account program.

Instead of insulating public schools from the reality of parental options or creating unique funding mechanisms, lawmakers should adopt protocols whereby school funds follow a child to his school, online class, tutor, or any other educational service of choice in real time.

Arizona's charter school funding process is designed to reflect accurate enrollments in the schools, and this procedure is a model for the savings account program. Under Arizona's charter law, schools report enrollment periodically through the year, and as the state sends monthly payments to schools, the payments are updated to reflect the current enrollment numbers.[20] Likewise, traditional schools should update their enrollment reports throughout the year and should have their payments adjusted accordingly. Students who opt for a savings account should be able to take their funds with them as they find educational opportunities outside the traditional public school system.

Lawmakers should have school funds follow a child to his school, online class, tutor, or any other educational service of choice in real time.

3. **Allowable expenses**. State leaders must carefully define the list of expenses for which parents can use savings account funds.

   As mentioned previously, Arizona parents can use such funds for private school tuition, individual public school classes, textbooks, educational therapy services, online classes, standardized test fees, tutoring services, college savings plans, and college tuition.

   But there are at least four other expenses parents incur when providing an education for their child and should be allowable expenses for education savings account funds: transportation fees; school uniform expenses; educational summer camps; and classroom materials such as pens, paper, calculators, computers and tablet devices.

   The state department of education should make a list of all the types of approved expenses available to parents through the Internet and periodic mailings.

4. **Preventing fraud and abuse.** Every state and federal program that offers public assistance is subject to fraud and abuse. Education savings account programs should be designed with fraud protections that use the experience of other benefit systems, such as Medicare and food stamps. For example, the Arizona Department of Education limits the vendors at

which parents can use debit cards, but food stamp debit cards also limit the items that cardholders can purchase, similar to food stamp policies. Savings account cards should have this protection added, so that when families use the check cards at large retailers (again, such as Walmart), the cards cannot be used to purchase groceries at the same time that curriculum or textbooks are being purchased. State officials should also list vendors that have been "unlocked" on a state website or should distribute such a list to account families so that parents know which stores have already been unlocked. Maintaining an updated database such as this, along with accurate records on participating students, should be a central task for department officials who are overseeing the program.

State leaders should conduct quarterly and random audits of the accounts to reconcile the balances of families that turned in few or no receipts. With Arizona's accounts, parents could be spending the money at approved stores on unapproved purchases and could be not submitting receipts. If the state audits the accounts only annually, state officials may not identify those purchases until conducting an annual audit. Strengthening investigative units such as this led to success against Medicaid fraud in Texas, reports Manhattan Institute's *City Journal.* Between 2003 and 2004, Texas recovered $441 million from fraudulent transactions.[22]

Lawmakers should create a toll-free hotline where families or retailers can report fraud; those hotlines are a common practice in Medicare systems around the country. Arizona's Health Care Cost Containment System offers a telephone hotline and a form that can be submitted online to report misuse of funds.[23] This measure alone will not prevent every misuse of state funds, but such a hotline could be part of the larger plan to prevent fraud.

State officials should also commission "compliance buyers," or investigators who pose as individuals trying to commit fraud. The Special Supplemental Nutrition Program for Women, Infants, and Children uses investigators in this way.[24] This process will help to identify weaknesses in the state's oversight of its education savings accounts and of vendors that are operating illegally so Arizona can ensure that funds are being spent appropriately.

Finally, state officials should outsource some of the fraud and abuse preventions through surety bonds. Those bonds are a form of insurance and are often used by building contractors,

An Unexpected Surprise: Parents Create Their Own Buyer's Guide

Shortly after Arizona's education savings accounts became law, parents created an online message board on Yahoo.com.[21] More than100 parents signed up, a remarkable number considering only 150 accounts were awarded in the program's first year.

The message board is now a virtual buyer's guide for savings account families, with recommendations about private schools, textbooks, online classes, tutoring programs, and extracurricular activities such as swim lessons and special events at museums.

Parents ask and answer questions about how to apply and complete audit reports, and—now that savings accounts are entering their second year—parents from the first year are sharing their experiences with new families. Parents also arranged "meet-ups" with other families, a further extension of the virtual community.

Today, more than 1,500 messages have been posted online, and those messages serve as an online handbook for the accounts.

How Surety Bonds Work

Surety bonds are a form of insurance.[27] This insurance vehicle could be used by a department of education to guarantee that parents fulfill their agreement for the education savings account with the state and that they spend funds only according to stipulations in the state contract. In turn, the department of education uses a bank—outsourcing the insurance—to provide the bonds, and the department then requires parents to pay a quarterly or annual fee for a bond.

What happens if a parent uses savings account funds for expenses that are not educational—for example, dinner at a restaurant or airfare for a vacation? When the department discovers the transaction through its auditing process, the surety company would attempt to recover the funds. If a parent refuses to repay or cannot repay the money, the surety company could send a collection agency to get the money back.

If this approach fails, the surety company would repay the state using money from the bond fees that parents paid when they were awarded an account.

public notaries, and even public officials.[25] The bonds protect state taxpayers by requiring individuals to pay a small fee (usually much smaller than a typical insurance premium), and the surety company (a third party such as a bank) will guarantee that the individual complies with the provisions in a contract. The bond's cost should be affordable for parents and should be an allowable expense for savings account money. For example, the National Notary Association offers bonds for Arizona public notaries at an annual cost to a notary of $26 (for a $25,000 bond).[26] If necessary, the surety company could use a collection agency to recoup funds if a parent misuses savings account money and either cannot repay or refuses to repay the funds. In the event that a parent cannot repay misused account money, the surety company will repay the state using money from the bond fees that parents paid.

Additional Considerations

Policymakers must be prepared to give parents flexibility with the accounts—even beyond the classroom—while still holding parents accountable for how funds are spent.

- For funds that are unused by the time a child graduates from college, parents should be allowed to roll the money into a retirement savings plan or a health savings account for the (now) young adult.
- While students are enrolled in a savings account, policymakers should enact provisions that require parents to have students tested at regular intervals using an assessment of choice. Parents should be afforded the opportunity to choose the test and report the results to the state. State officials should maintain a database of student test scores and should make the results publicly available while protecting student privacy. State officials should report changes to test scores over time in addition to reporting changes to average scores.

  This requirement has two primary benefits for children, parents, and policymakers: First, policymakers will be able to monitor the accounts' effectiveness. Lawmakers must hold accountable the schools or the learning programs that post consistently low achievement scores. Second, parents and taxpayers should know if their tax money is benefiting students, and test results should be used as a leading indicator.

- As in Arizona, other states should include provisions to distinguish homeschooling families that are not using savings accounts from those that are using the accounts. This way, families that homeschool using only their own money will not be required to take assessments and report the results to the state. Many homeschool laws around the country were designed so that homeschool students would not be required to take state tests, and this freedom should be preserved as states adopt education savings accounts. For families that choose to homeschool and not use an account, savings account laws that do not apply to them should not interfere with their home-school program.

Conclusion

In the years between *A Nation at Risk*, released in 1983, and the Council on Foreign Relations' *U.S. Education Reform and National Security*, published in 2012, the conventional wisdom about U.S. public education has not changed. The council's report opens with "It will come as no surprise to most readers that America's primary and secondary schools are widely seen as failing," which is eerily similar to *A Nation at Risk*'s now-iconic words from three decades earlier: "If an unfriendly foreign power had attempted to impose on America the mediocre educational performance that exists today, we might well have viewed it as an act of war."[28]

In the years between the two reports, lawmakers have paid schools more tax money, have attempted to lower class sizes by hiring more teachers, and have enacted various other institutional reforms.

Those top-down reforms have not changed the trajectory of student achievement. What is more, advances in technology are changing the way we consider education. Online and hybrid schools, along with free educational content through YouTube and iTunes, have helped shift the focus of a child's experience from the schoolhouse to, well, any house. Parents and children need to be able to pursue education wherever it is found. Education savings accounts allow them to do just that. The accounts are a model for what education in the 21st century should look like: flexible, innovative, and child-centered.

Kasey

Jeff and Rebecca Locke didn't want Kasey to be frustrated in school—or out of it. Kasey, age six and diagnosed with autism, responded the best when her parents used a behavioral technique called Applied Behavioral Analysis (ABA). The Lockes encouraged her teachers to use some of the techniques in the classroom, explaining the success they had with the approach at home.

"They couldn't really ever bake the ABA stuff into the cake," Jeff says. But when the Lockes learned about the new savings account program, "It was almost too good to be true."

"So far, it's just been great," Jeff says, adding, "it has opened a lot of doors." Kasey's new school can implement the behavior strategies into the teaching Kasey is now much less frustrated, and she has begun to communicate better with her parents. Jeff reports, "She likes to go to school. She's a lot happier in the morning. On the car ride down there, she is more excited."

"It's been a huge success for us," Jeff says.

ENDNOTES

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11 Jonathan Butcher, "Ghost Busters: How to Save $125 Million a Year in Arizona's Education Budget" (Goldwater Institute Policy Report No. 246, May 21, 2012), http://goldwaterinstitute.org/sites/default/files/Policy%20Report%20246%20Ghost%20Busters.pdf.

12 Arizona State Legislature, Fiftieth Legislature, First Regular Session, S.B. 1553, http://www.azleg.gov/DocumentsForBill.asp?Bill_Number=SB1553&Session_ID=102.

13 Arizona State Legislature, Fiftieth Legislature, Second Regular Session, H.B. 2622, http://www.azleg.gov/legtext/50leg/2r/laws/0360.pdf.

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25 With education savings accounts, the relationship between a parent and the state is similar to that of the state and a private contractor, where the state is contracting out the job of educating a child. Since surety bonds are readily available for public contracts, bonding vehicles that would suit a savings account program likely already exist.

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