Qualifying for Financial Aid

Investors saving for college often wonder what effect saving may have on a student's chances of qualifying for financial aid. There are several types of financial aid (federal, state and institutional), but federal aid is the most widely dispersed, and a family seeking any financial aid must complete the Free Application for Federal Student Aid (FAFSA).

There are three basic ingredients in determining how much need-based aid your child is eligible for.

1. The cost of the school your child will be attending or is attending otherwise known as the Cost of Attendance (COA).
2. The dollar amount provided to the student from outside sources. Scholarships would be considered an outside resource. Also payments made directly to the college by a grandparent for example.
3. The expected family contribution (EFC). This is the amount your family is expected to pay for college based on your finances. This figure is determined each school year you apply for the Free Application for Federal Student Aid (FAFSA). The calculation considers the student's income and assets and the parent's income and assets. Refer to the chart on the next page.

Example:
Let's assume your child will be attending an in-state public college costing $22,000 per year. Your expected family contribution is $10,000 based on your child's contribution of $1,000 and your contribution of $9,000. Your child received a private scholarship for $1,000. Your child's financial need is $11,000 computed as follows:

(COA-EFC-Outside Resources = Financial Need)

COA		**$22,000**
EFC		
Student's contribution	$1,000	
Parents' contribution	$9,000	
Total EFC		**$10,000**
Outside Resources		**$1,000**
Financial Need		**$11,000**

After completing the FAFSA the schools financial aid office will provide you information of what type of student aid is available and what amount will be available to your child. Federal student aid includes grants, work-study and loans. A **grant** does not have to be repaid and are typically awarded to students with exceptional financial aid need. The **Federal Work-Study** program is a program where students while attending can earn money for college through an on-campus or off-campus job. A **loan,** either a subsidized or unsubsidized, must be repaid back with interest.

The chart below shows the ranges of parent, student and grandparent income and assets used to calculate an annual Expected Family Contribution (EFC) for a student. Once EFC is determined, an institution's financial aid officer subtracts it from the institution's cost of attendance to determine annual financial need. The chart below shows income is more heavily factored than assets.

	PARENT	STUDENT	NON-PARENT
INCOME	22% - 47% of available income	50% of student income (after certain allowances)	Not included
ASSETS	**<u>0% of assets</u>** • Retirement Accounts such as IRAs[1] or 401(k) • Equity in your primary home, a family-owned business, insurance policies and annuities **<u>0% - 5.6% of assets</u>** • 529 savings plan (where parent is owner)[2] • Prepaid tuition plans (where parent is owner) • Coverdell ESA (where parent is owner)[2] • Securities • Mutual Funds • Bank accounts, CDs	**<u>0% of assets</u>** • Retirement Accounts such as IRAs[1] or 401(k) **<u>0% - 5.6% of assets</u>** • 529 savings plan (student owned 529 where student is a dependent)[2] • UTMA-529 (where student is a beneficiary)[2] • Coverdell ESA (where student is owner)[2] **<u>20% of assets held in student's name</u>** • 529 savings plan (student owned 529 where student is an <u>in</u>dependent)[2] • UGMA/UTMA accounts • Minor trusts • Savings bonds (in student's name) • Money, investments, business interests and real estate	**<u>0% of assets</u>** • Retirement Accounts such as IRAs[1] or 401(k) • 529 savings plan (where a non-parent is owner) - *Simply owning a 529 account for a child will not affect that child's financial aid eligibility*[3] • Coverdell ESA (where a non-parent is owner) **Word of caution:** Financial aid offices are required to treat distributions from non-parent owned 529s as aid to the student that will count as income for the year the withdraw was taken (remember 50% of a student's income counts towards the EFC). Therefore when the non-parent takes a distribution to pay for higher education it may negatively affect the beneficiary's financial aid eligibility when they apply for Financial Aid in the future.

[1] Though the tax law now permits penalty-free withdrawals from traditional or Roth IRAs to pay for qualified college costs, doing so could jeopardize financial aid in the following year. The entire withdrawal, principal and earnings, counts as income on the following year's aid application.

[2] Withdrawals from a 529 plan and an ESA are treated advantageously. Such withdrawals when used for college are excluded from your federal income tax return, and according to the U.S. Department of Education are not required to be "added back" when reporting your family income on the student's federal financial aid application.

[3] Most financial aid offices interpret the rules as requiring distributions from grandparent-owned and other non-parent owned 529s to be included as student income, even when the distributions are not reportable for federal income taxes (i.e. they are tax-free).

Note that some colleges will calculate financial need using a different formula when offering their own grants and tuition discounts. The "institutional methodology" used by many of these colleges may count home equity, sibling assets, and certain investment accounts in a manner that differs from the federal methodology.

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