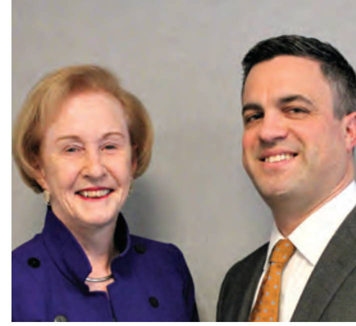
Don't Risk Leaving Potential Higher Education Money on the Table

Financial Aid Eligibility: Give It a Try



by Alexandra Armstrong, CFP, CRPC, and Christopher Rivers, CFP, CRPC

Each year September ushers in a new crop of students on college campuses across the country. For many families financial aid helps bridge the gap between the cost of attending college and the amount that students and their parents can afford to pay. Unfortunately, many students forgo applying for financial aid because they assume they won't qualify or it's too time consuming.

Although the initial effort can seem daunting, there's a significant amount of aid available to ease the burden of the cost of higher education, if you put in the time to investigate.

Free Application for Federal Student Aid (FAFSA)

The first step for all prospective college students and parents, regardless of their economic position, is to fill out the Free Application for Federal Student Aid, known as FAFSA. The FAFSA form for the following school year becomes available on Oct. 1 each year. Thus, the FAFSA form for the 2020-2021 school year is live on Oct. 1, 2019.

The FAFSA form asks more than 100 questions about personal information, tax and income data, household size and which schools you are applying to, among others. In addition, many schools require an additional financial aid application in addition to FAFSA, so be sure to check with each individual college or university as to their requirements.

Timing Is Tricky

The timing as to what data to use and when to apply can be tricky, so it's crucial to be clear about the timeline. As mentioned above, the next school year's FAFSA form is released on Oct. 1 each year. When completing the FAFSA form, the form looks back two years for tax and income data.

For a high school senior, parents would download the FAFSA form for 2020-2021 on Oct. 1, 2019, and would fill it out using data from their 2018 tax return. A key consequence of this is that tax and income data during the last two years of college won't be used on any FAFSA forms.

Split Households

When parents live apart and are divorced or separated, the custodial parent is the one who needs to provide information for the FAFSA. But since a custodial parent isn't defined as the parent who has legal custody, other factors must be considered to determine which parent's information must be provided. Typically, these include which parent the student lived with the most during the last 12 months and which parent provided the most financial support.

For situations where the custodial parent has remarried, the stepparent's information must also be included on the FAFSA. If the student's parents are divorced, are separated or were never married but live together, both are required to provide information on the FAFSA.

Expected Family Contribution

One of the key metrics in determining financial aid is the expected family contribution. The formula for determining the EFC considers parental assets and income, student assets and income, and how many family members are attending college at the same time. The EFC isn't the amount of money the family is expected to contribute to education costs. It's simply a number used by educational institutions to determine whether federal aid is available.

- **Parental assets.** The questions that the FAFSA asks about parental assets pertain to ownership interest at the time the application is completed. Reportable parental assets include cash and funds held in bank accounts, trust funds, 529 accounts and more. Parental assets are considered low-impact assets for financial aid purposes — only up to 5.64% of the value of parental assets affect the EFC.
- **Student assets.** Student assets include property in which the student has an ownership interest at the time that the FAFSA is completed. For example, custodial accounts — Uniform Transfer to Minors Act (UTMA) and Uniform Gift to Minors Act (UGMA) — fall into this category. Student assets are considered high-impact assets for financial aid purposes — up to 20% of the value of the student's assets will affect the EFC. 529 college savings plan assets are not considered assets of the student and should be listed as parental assets. (*More on 529 plans below*.)
- **Protected assets.** A number of assets are protected and are not included on the FAFSA, including 401(k)s, pension plans, 403(b)s, individual retirement accounts and other retirement plans. Equity in a family's primary residence, certain family-owned businesses and farms, life insurance, annuities and personal possessions are also nonreportable.

If your children are approaching college age, you can get an estimate of your family's EFC with the U.S. Department of Education's FAFSA4caster at:

https://studentaid.ed.gov/sa/fafsa/estimate

Grandparent-Owned 529 Plans

Often the grandparents will have established a 529 plan on behalf of their grandchildren to help pay for college where they are the owner of the account. Since assets owned outside of the immediate family aren't included on the FAFSA, funds in a grandparent-owned 529 plan aren't considered countable assets on the FAFSA.

But money taken out of the 529 plan and used to pay for education expenses is considered nontaxable income to the student. As a result, distributions from a grandparent-owned 529 plan reduce the eligibility of a student for need-based aid by as much as 50% of the amount of the distribution.

Therefore, while the mere existence of a grandparent-owned 529 plan does not affect financial aid, once distributions are taken from the 529 plan to pay for college, they can significantly reduce aid eligibility.

In this situation where the grandparents do own a 529 plan for the benefit of their grandchild, one solution is for the family to reserve those funds to be used in the last two years of college. This way since the FAFSA uses the prior-prior year's tax return to complete the income questions, distributions from 529 plans used to pay expenses in the student's junior and senior years of college would not be reported on the FAFSA forms.

Don't Leave Free Money on the Table

By some estimates, as many as 1 million students last year failed to claim a Pell Grant of up to $6,095 by simply failing to file the FAFSA to verify their eligibility in the first place. Since this is a grant and not a loan, it doesn't even need to be paid back!

Nearly 50% of those who were eligible but didn't file incorrectly assumed they wouldn't be eligible when they actually were. It's true that the higher your family's income, the lower your chances of receiving this type of federal grant. According to the College Board, 80% of Pell Grant recipients (dependent students) came from families with incomes below $40,000 in 2015-16.

Beyond the Pell Grant, a number of other non-federal grants (from states, private entities and colleges themselves) may also be determined through the FAFSA, even for some high-income students. Some of the merit-based scholarships offered by colleges and universities also require applicants to file the FAFSA even if the award itself is ultimately merit-based and not financially based.

Don't Procrastinate

The earliest date to submit the FAFSA form is Oct. 1, although the deadline is June 30 of the next calendar year. Many colleges, however, establish preferential filing deadlines for maximum consideration. A later application still may result in the award of some financial aid, but an earlier application is more likely to reap greater benefits. Colleges have different guidelines, so be sure to confirm the procedures with the schools to which you are applying.

Completing the FAFSA Form Has Become Easier

Many helpful resources for filling out the FAFSA are available; college financial aid offices or the student's high school counselor should be able to point you in the right direction. You can even complete the FAFSA online with real-time chat access to representatives

https://studentaid.ed.gov/sa/fafsa

When it comes time to fill out the form, most users will be able to pull in their family's tax information directly from the Internal Revenue Service using the IRS Data Retrieval Tool:

https://fafsa.ed.gov/fotw1819/help/irshlp9.htm

The benefit of using this tool is that data is transferred directly from the IRS and automatically populates the form, which saves time and ensures greater reporting accuracy.

Time Well Spent

In the time it takes you to stream one episode of your favorite TV show, you can put yourself in the best position to receive financial aid to pay for college. Even if the student wasn't eligible in the past, you should apply every year to see if the outcome might improve. As part of this process, it is critical that you meet with your financial adviser to determine how the cost of college will impact your overall financial well being. B

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