SAGE Scholars

Ten Minute Professor

The ABCs of Financial Aid

Learn the basics of financial aid.

There are only 2 ways to pay for college—with your money (including help from family members) and with other people's money. Your money can only come from 3 sources:

1) Past income (assets)
2) Present income (available cash)
3) Future income (loans)

Financial Aid Components

Other people's money is financial aid. Colleges recognize three components of financial aid:

1) Scholarships
2) Loans (future income)
3) Work-study

Scholarships cost only the conditions you need to meet in earning them (for example, band practice to qualify for a music scholarship). Loans simply defer paying for college. Work-study is usually low-paying campus employment. Cafeteria and bookstore jobs are 2 classic examples of work-study opportunities.

Intent

The original intent of financial aid was to help students attend college who otherwise could not afford to do so. Its purpose was to help students and their families achieve their personal objectives.

Now, financial aid is primarily used to help colleges achieve their institutional objectives and affordability isn't a primary concern. Colleges often use financial aid to:

a) Enroll students who otherwise wouldn't be considering the school

b) Increase the profile (average SATs, class diversity, etc.) of the incoming first-year class

Packaging

Colleges mix (package) scholarships, loans, and work-study according to their resources and institutional objectives. As a result, two students receiving the same total amount of financial aid may have very different combinations of the three components.

The most desirable financial aid package has the highest percentage of scholarship(s) (also called merit aid or grants). Scholarships mean discounts off the list price of tuition.

Each student considered for financial aid has their financial need calculated when the student's family completes the Free Application for Federal Student Aid (FAFSA), which requires a declaration of both student and guardian income, assets, and obligations.

Need vs. Non-Need Aid

Using federally-approved formulas that place more emphasis on income than assets, the Expected Family Contribution (EFC) is calculated. The EFC is the dollar amount that the family is expected to contribute annually to the student's total college costs (tuition, room and board, books, travel, incidentals, etc.).

The EFC figure is a constant—it does not change depending upon the cost of college.

For example, a family with an EFC of $18,000 would receive no need-based aid at a college where total costs were $15,000/year—but would, theoretically, receive up to $20,000 at a college where total costs were $38,000/year.

In other words, at a college costing $15,000/year, the family (including the student) would be expected to pay $15,000, out of pocket—but, at a college costing $38,000/year, the family would pay just $3,000 more ($18,000 total)!

Scholarship? Loan? Work-Study?

The big question: at the more expensive college, of the $20,000 of need-based financial aid ($38,000 tuition minus an EFC of $18,000), how much are scholarships, loans, and work-study?

Governmental sources of financial aid must be need-based. In general, this means public (taxpayer- or state-supported) universities primarily give need-based aid.

Some Colleges Also Give Non-Need Aid

Of the approximately 1,665 private colleges and universities in America, all but perhaps 50 also give non-need based financial aid—usually called grants or scholarships. Most private colleges give aid beyond what the EFC indicates the student's need to be! It is this non-need aid that generally is used to help achieve institutional objectives.

Non-need aid, other than certain loans, can come from private sources, from funded college sources (endowment), and/or from non-funded college sources (simply a price discount). Non-need aid does not come from the government.

Blending vs. Stacking

When students receive scholarship awards from non-college sources, most colleges take at least a portion of that award to reduce the scholarship amount provided from the college's own resources.

Thus, a student receiving a $1,000 scholarship from an outside program may find that the college simply reduces its non-endowment funded award by $1,000! This practice is known as blending—external funds reduce what the college is willing to offer.

The portion, if any, which reduces the family's EFC is called stacking. If a student was previously to receive $20,000 in aid and now, including the $1,000 outside award, receives $21,000—that award was stacked, not blended.

Gapping

Many colleges and universities simply do not have enough government, institutional, or other sources of funding to meet total individual student need—the difference between the EFC and the total cost of education. This difference is called gapping—providing less financial aid than the student needs to attend college.

FAFSA vs. Institutional Methodology

Subject to minimum allowances, FAFSA requires 5.6% of certain parental assets be used for college costs and count toward the family's EFC. However, FAFSA exempts some assets, specifically:

- Home equity
- Retirement funds
- Life insurance, including annuities

Most colleges require information beyond the basic FAFSA to calculate the EFC. This is institutional methodology. Frequently, these colleges use a form called the CSS Profile. Some colleges do look at home equity, believing that families should be willing to use a portion of their home equity to pay for college. Some schools will also pay attention to sudden increases in retirement funding vehicles or cash-value life insurance.

Both FAFSA and institutional methodologies more heavily weigh student assets than guardian assets. Student assets are calculated at 20% annually to be used for college costs, compared to 5.6% for family assets (after a deductible based on the guardians' ages).

Grandparent And Other Relatives' Assets

Assets of grandparents, aunts and uncles, and other non-custodial relatives do not count toward the family's EFC. Income and assets of stepparents, divorced parents, and remarried, non-adopting partners are treated in a variety of ways, depending upon the college. Accordingly, the off-balance sheet income or assets of such alliances are what typically pay for, at a minimum, the extras of fraternities or sororities, or even books!

What About Loans?

Various subsidized and unsubsidized loans, sponsored by federal, state, and private sources, are available to guardians and students. Borrowing satisfies today's cravings at the expense of tomorrow's standard of living.

Borrow or save? The penalties for instant gratification are serious. Consider this table:

Total Amount Needed:		$50,000	
Years to Borrow or Save:		10	
Interest rate, PLUS loan:		7.00%	
Investment return:		8.00%	
	Save	Borrow	Difference
Monthly	$273.30	$584.74	$311.44
10-Year Total	$32,797	$70,168	**$37,371**

Few families realize the penalty they face by not adopting a disciplined, regular savings plan. The above table shows just how harmful that can be over time.

7.00% is the rate for 2017-18 Parent PLUS loans. Interest rates are fixed for the life of the loan. Annually, the rate for new loans is adjusted based on 10-year U.S. Treasury note rate as of July 1st of that year.

Beware of Scams

Some financial advisors may claim that they can:

a) Find hidden scholarships

b) Guarantee that your child will receive more financial aid than they would otherwise qualify for

Keep these points in mind as you evaluate offers:

- Never pay for scholarship searches. Anybody can do a free online scholarship search.
- While the uniform methodology EFC formula

does not consider certain assets in calculating the student's EFC, some of the more common tricks—such as hiding parents' assets in these unconsidered assets—can backfire.

How Do I Get Started?

Contact your financial planner. Or, contact us at SAGE Scholars.

Talking Points: The Big Questions

Here's what most families want to know:

1. How much income is too much to qualify for financial aid?

A wildly-generalized guideline for private colleges is that an annual income of less than $100,000 to $125,000 will frequently qualify for at least some financial aid (if no significant qualifying assets are involved).

2. Will my assets disqualify me from financial aid?

That depends upon the type of asset and the type of school—public or private. Home equity, annuities, retirement funds, and life insurance are not counted toward the EFC at public colleges. But these assets might be, for need-based aid, at some private schools using institutional methodology (typically, the CSS Profile).

3. Why bother saving if it only counts against me?

Families with that mindset can spend now and later have to borrow for college—or they can save now and risk losing 5.6% of parental assets per year (above a certain threshold). Borrow the $20,000 plus thousands more in interest, or save $20,000 and have $18,880 available for college?

4. Should we only consider colleges that we think we can afford?

No! Private colleges have huge variations in the amount of financial aid and merit aid they're willing to give—and how they package it. You won't know what you can afford until you apply.

5. How does SAGE Scholars help?

Our SAGE Tuition Rewards program provides participants with aid that is not need-based. Tuition Rewards points are not hard dollars, but discounts off the list price of tuition given by almost 400 member colleges. Large Tuition Rewards amounts (each point represents a guaranteed minimum discount equivalent to one dollar) are generally blended into other institutional awards. If the amount is under $1,000 per year, the Tuition Rewards points are often stacked. Colleges that participate in our program tend to be generous with financial aid.

Tuition Rewards points are not considered to be a family asset and thus have no effect on the EFC. Our contracts guarantee that participating colleges will give a dollar award at least equal to the amount of Tuition Rewards points submitted by the high school senior, subject to maximums set by participating colleges.

6. What are Tuition Rewards® deadlines?

Tuition Rewards points must be transferred from sponsor accounts to students by August 31st of the year that 12th grade begins. Families must submit a Tuition Rewards statement to participating colleges within 10 days of application. A college's normal admission standards apply. For a current list of participating colleges and universities, visit tuitionrewards.com.