TEN MINUTE PROFESSOR

The ABCs of Financial Aid

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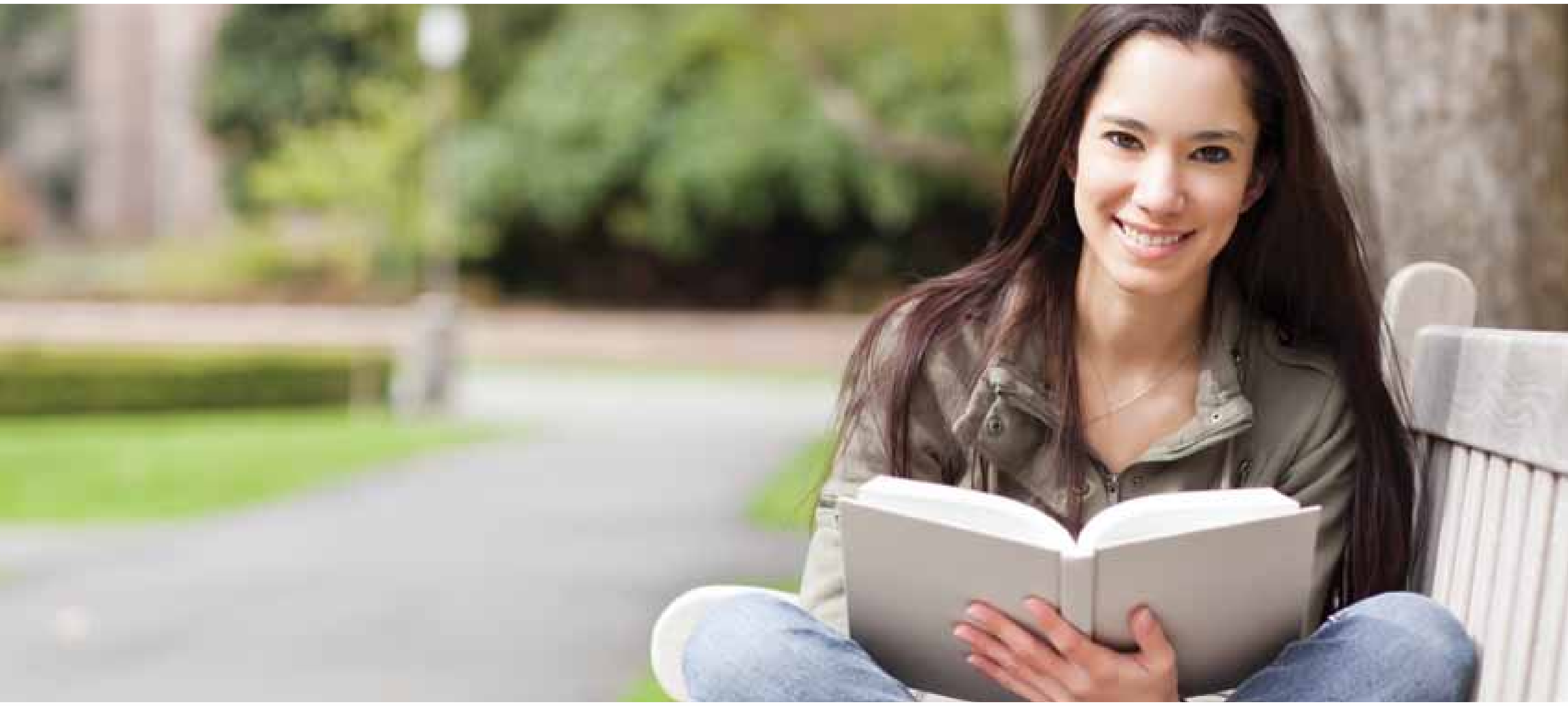

It's urgent to start saving now. The clock is ticking.

There are only two ways to pay for college – with your money (including help from other family members) and with other people's money.

Your money can only come from three sources:

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

Other people's money is what colleges refer to as **Financial Aid.**

Financial Aid Components

Colleges recognize three components of Financial Aid:

1. Scholarships
2. Loans (which are actually your future income)
3. Work-study.

Scholarships are obviously the most desirable of the three. Loans simply defer paying for college until later, and work-study is usually low-paying campus employment. Cafeteria and bookstore jobs are two 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. In other words, its purpose was to help students and their families achieve their ***personal*** objectives.

In addition to that worthwhile purpose, Financial Aid is now often used to help colleges achieve their ***institutional*** objectives. In particular, colleges often use Financial Aid to: (a) Enroll students who otherwise wouldn't be considering the school, and/or (b) Increase the "profile" (average SATs, class diversity, etc.) of the incoming first-year class.

Packaging

Colleges mix, or "package", the three above mentioned components 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.** Obviously, from the family's perspective, the most desirable Financial Aid "package" has the highest percentage of scholarship (also called "merit aid" or grants — terms that mean discounts off the "list price" of tuition).

Each student considered for Financial Aid is first determined to have, or not to have, financial "need." Need is determined as follows: The family – defined in different ways, depending upon the college – completes a standard form, FAFSA (Free Application for Federal Student Aid), that requires a declaration of both student and parental income, assets, and, to a lesser extent, obligations.

Need vs. Non-Need Aid

Using federally-approved formulas that place more emphasis on income than assets, a figure called the **Expected Family Contribution,** or **"EFC,"** is generated. The EFC, as the name implies, 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 – that is, 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 annual costs were $15,000/year – but would, theoretically, receive up to $20,000 at a college where total annual 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? Or Work Study?

The big question: At the more expensive college, of the $20,000 of need-based financial aid ($38,000 minus an $18,000 EFC), how much is ***Scholarship? Loans? Work-Study?***

Governmental sources of Financial Aid must be **need-based**. In general, this means **public** (taxpayer or state-supported) colleges and universities **only** give need-based aid. (Athletic scholarships at NCAA Division I and II schools are a different story.)

Some Colleges Also Give Non-Need Aid

Of the approximately 1,540 private colleges and universities, however, all but perhaps 50 also give non-need based financial aid — usually called "grants" or "scholarships". In other words, most private colleges may give aid beyond what the EFC indicates "need" to be! It is this non-need aid that generally is used to help achieve institutional, not individual or family, 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 scholarships from non college sources (Rotary Club Scholarships, local newspaper essay winner, etc.), most colleges calculate at least a portion of the award to reduce the amount of scholarship provided by the college from the college's own resources. Some colleges actually use written formulas. Thus, a student receiving a $1,000 scholarship from his/her local newspaper or church 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 might be willing to offer.

The portion, if any, which reduces the family's EFC is called **"Stacking."** In other words, 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." High School Guidance Counselors recognize that many awards are simply "Blended" and are frequently less than anxious to provide recommendations, transcripts, etc. for a $500 award – knowing that it might not actually change the family's expected contribution.

Gapping

Many colleges and universities simply do not have enough government, institutional, or other sources of funding to totally meet individual student need – the difference between the EFC and the total cost of education. This difference, if it occurs, 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

Many private colleges and universities require information beyond the basic FAFSA to calculate the EFC. This is called **"Institutional Methodology."** Frequently, these colleges 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 particular attention to sudden increases in various retirement funding vehicles or cash-value insurance.

Both FAFSA and Institutional Methodologies more heavily weigh **student** assets than parental assets. Student assets traditionally have been calculated at **20%** (annually) to be used for college costs, compared to **5.6%** for family assets above an excluded amount (that rises as parents get closer to retirement age).

Grandparent Assets:

Assets of grandparents, aunts and uncles (unless they are guardians for the student) do not count toward the family's EFC. Income and assets of step-parents, 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 more often, even books!

What About Loans?

Loans are future income used to pay for today's expenses. Various subsidized and unsubsidized loans, sponsored by federal, state and private sources, are available to parents and student. Remember that borrowing is less efficient than saving and should be a "last dollar" strategy. Borrowing satisfies today's cravings at the expense of tomorrow's standard of living.

Borrow or Save? The penalty for "instant gratification" is severe. Consider the following table:

Few families realize the penalty they face by not adopting a disciplined, regular savings plan. The above table, using extremely modest assumptions, shows just how deleterious procrastination can be.

More realistically: How about a 4% interest rate on saving and a 7% interest rate on borrowing? The 10-year difference between the cost of saving $50,000 and the cost of borrowing $50,000 becomes nearly $37,000!

Assumptions:

Total Amount Needed: $50,000

Years to Borrow or Save: 10

Interest rate (borrowing or saving) 4%

	Save	Borrow	Difference
Monthly Amount	$330.56	$506.23	$175.67
10-Year Total	$39,667	$60,747	$21,080

Beware of Scams:

Some financial advisors may claim that they can: (a) Find "hidden" scholarships and/or (b) Guarantee that your child will receive more financial aid than he or she otherwise would qualify for. Beware:

- Never pay for scholarship searches. Any student or high school guidance counselor can do a free scholarship search on the Internet.
- It is true that, while the uniform methodology EFC formula does not consider certain assets in calculating the Expected Family Contribution for a student's college education, some of the more common "tricks" – such as hiding parents' assets by putting them in the child's name or making advance payments on a home mortgage and so on – can backfire.

Talking Points: FAQs

Here's what most families want to know:

1. How much income is "too much" to qualify for Financial Aid?

Short of filling our a FAFSA form, in a need-based situation, 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 for Financial Aid?

That depends upon the type of asset and the type of school – public (state) or private. Home Equity, Annuities, Retirement funds and Life Insurance are not counted toward the EFC at public schools — but might be, for need-based aid, at some private schools using Institutional Methodology.

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

Families with that mind-set can "spend it" and have to borrow to pay for college – or they can save and "lose" 5.6% of parental assets per year. Spend $20,000 and have to borrow the $20,000, plus thousands more in interest. Or, save $20,000 and have $18,880 available for college?

4. How can I calculate my EFC?

A quick, fairly accurate version is at www.FAFSA.ed.gov

5. Should we only consider colleges that we can "afford"?

No! Colleges have **huge** variations in the amount of Financial Aid they're willing to give – and how they "Package" it.

6. How does SAGE Scholars help?

Our **SAGE Tuition Rewards® program** provides participants with **non-need based aid.** Tuition Reward Points are not "hard dollars" — but discounts off the "list price" of tuition given by approximately 250 member colleges. Large Tuition Reward amounts are generally "blended" into other institutional awards; if the amount is relatively small (under $1,000 per year), the Tuition Reward Points are often "stacked."

Tuition Reward Points are **not** considered to be a family asset and thus have no effect on the Expected Family Contribution (EFC) calculation. Our contracts guarantee that participating colleges will give a **dollar award at least equal to the amount of Tuition Reward Points in the high school senior's account,** subject to maximums set by participating colleges.

Other Resources:

www.Finaid.com

www.FAFSA.ed.gov

www.waggonerfinancial.com

How Do I Get Started? Call 661-889-8638

Contact your financial planner – or, call or e-mail SAGE Scholars for the names of local Tuition Rewards-qualified financial members who may be able to assist you.