CollegeBoard

Back to Basics: Simplifying the Financial Aid Process to Increase Access & Success

Leading up to the Reauthorization of the Higher Education Act, the Bill & Melinda Gates Foundation funded 16 national organizations to examine the federal financial aid system and make recommendations to reimagine aid design and delivery. The 2012-13 Reimagining Aid Design and Delivery (RADD) project resulted in a variety of white papers and meetings exploring common themes and possible system improvements to remove barriers and increase success for low-income students.

The Gates Foundation provided a second round of funding to support four consortia in developing consensus recommendations related to common ideas and themes. As a result, the College Board joined six organizations[1] to focus on increasing simplification and transparency in the financial aid system. The goals of the RADD 2.0 consortium on simplification and transparency are:

- Continue to raise awareness about federal financial aid simplification and transparency issues.
- Inform the debate on the desirable outcomes and possible unintended consequences of reforms.
- Drive towards policy coherence on financial aid simplification and transparency.

The College Board supports the following strategies to simplify the financial aid system and increase transparency for students and families:

- Create a simpler federal financial aid application process;
- Develop a more transparent federal aid eligibility determination;
- Use “prior-prior” year income data to streamline the application process;
- Meet the data needs of states and institutions, and;
- Provide early information about paying for college to families based on their financial resources.

1 Other members of the Simplification and Transparency RADD 2.0 Consortium include: The National College Access Network (NCAN), the New America Foundation, the Center for Law and Social Policy (CLASP), the Institute for Higher Education Policy (IHEP), the U.S. Chamber of Commerce Foundation, and the Young Invincibles.

A Simpler Federal Financial Aid Application Process

To receive federal student aid, students and families must complete the Free Application for Federal Student Aid (FAFSA). Although the U.S. Department of Education (ED) has made good progress in recent years in developing a smarter online application, requiring only information appropriate to the student's circumstances, many students do not complete the application because of its perceived complexity. Novak and McKinney (2011) estimate that 2.3 million students do not file a FAFSA, but would qualify for federal student aid if they applied[2]. Some of these students never enroll in postsecondary education. Those who do manage to enroll, many from very low-income backgrounds, often need to work to pay their education and living expenses, reducing the probability that they will complete their education programs.

The IRS has cooperated with the U.S. Department of Education to further simplify the process, permitting students and parents to access their tax data and populate their FAFSA with the required information. This IRS Data Retrieval Tool allows applicants to skip certain required verification steps, which have proven a barrier to completing the FAFSA process for low-income students. However, because eligibility is currently based on income information from the year immediately preceding enrollment, early financial aid application deadlines, particularly for first-time applicants, mean that tax data are not yet available. As a result, students must determine how to fill in the financial questions on the FAFSA and subsequently, must take the additional steps to submit tax documents to complete the federal verification process.

There is clear evidence that the current FAFSA process creates barriers for students. The benefits of simplifying the formula to rely solely on a few pieces of data from federal income tax forms would disproportionately help low-income students in overcoming these barriers. Importantly, several studies have found that simplifying the formula in this way would have little impact on eligibility for low-income students and the distribution of Pell Grant funds. In fact, the vast majority of families for whom additional data are necessary to evaluate assets or complex sources of income would not likely be eligible to receive a Pell Grant.

Although the online application and IRS Data Retrieval Tool have simplified the federal application process, there is opportunity to design a more effective system. We recommend the following improvements:

1. Create a more transparent federal eligibility determination by limiting the required financial data to just two elements: Adjusted Gross Income (AGI) and number of exemptions (family size)— information readily available from the IRS.
2. Allow applicants whose parents or who themselves are not required to file a federal tax form to qualify for the maximum Pell Grant award without requiring them to provide financial data on the FAFSA.
3. Base eligibility on "prior-prior" year (PPY) tax data (data from the year before the year currently used to determine federal aid eligibility).
4. Allow students who have experienced unusual changes in their family circumstances—for example, the death of a parent or working spouse—to appeal the original eligibility determination.

2 H. Novak and L. McKinney, *The Consequences of Leaving Money on the Table: Examining Persistence among Students Who Do Not File a FAFSA*, **The Journal of Student Financial Aid** Vol. 1 Number 3, National Association of Student Financial Aid Administrators (NASFAA), 2011.

A More Transparent Federal Eligibility Determination

The perceived, and often real, difficulty in completing the FAFSA and the federal verification requirements are not the only problem with the financial aid system. The complexity of the formula used to determine eligibility for federal financial aid is confusing and opaque. It is difficult for students and families to estimate the amount of student aid for which they will be eligible because of the number of data elements that go into the formula and because of the underlying calculations that are applied to the data. To estimate the amount of a student's Pell Grant under the current system, it is necessary to know with some degree of certainty the student's expected family contribution (EFC). The EFC (Federal Methodology) formula changes each year, as key allowances, such as the Income Protection Allowance, are updated. As a result, most first-year students do not learn about their financial aid eligibility until after they have been admitted to a postsecondary institution.

We believe that the eligibility formula needs to be simplified to help students from low- and moderate-income backgrounds understand early in their college preparation years how much financial aid they are likely to receive. Our specific proposals are detailed below:

1. For most students, Pell Grant eligibility should be based on Adjusted Gross Income (AGI) and family size (number of exemptions).
   - Parents' tax information would be required for dependent students; student's and spouse's tax information would be used for independent students.
   - The eligibility system would not take into account certain data used in the current EFC formula: the number of siblings or family members in college, family assets, or in the case of dependent filers, student income and assets. (Non-tax filers would not be required to provide financial data; they would automatically qualify for the maximum Pell award.)

2. There are tax filers with more complex financial circumstances for whom using AGI and number of exemptions does not make sense. For this population, using only these two data elements could result in a Pell Grant eligibility determination that does not reflect the student's or parents' financial strength. However, because relatively few applicants demonstrate such circumstances, requiring additional financial data and more complex eligibility determination for *all* filers is not justified. To solve this problem, we propose using IRS triggers to identify those filers based on key data elements such as a negative AGI or the tax schedules they file (Schedules B, C, D, E, and F). For these tax filers, the Department of Education could access more detailed IRS information to determine Pell Grant eligibility. With more detailed IRS information, it would be possible to adjust the AGI for tax filers whose reported AGI is negative but who do not fit the definition of low-income. (Currently, negative AGI is treated as zero in the FAFSA processing system.)
   - Based on earlier modeling done by the Urban-Brookings Tax Policy Center, 17% of FAFSA filers or their families completed the specified tax schedules. There may be additional filters that would limit the number of filers for whom more detailed information would be used to determine eligibility.
   - The Urban-Brookings Tax Policy Center also found that in 2007-08, among students with negative family AGI, 86% filed at least one supplementary tax schedule and 42% filed at least two.

3. As recommended by the Rethinking Pell Grants study group, the Pell Grant award schedule should be restructured to ensure that it targets grants more effectively to low- and moderate-income students. Under the current formula, when the maximum award increases, students from higher income families become eligible for a grant. The Pell award table should be structured so that only students from families with incomes below a specified level are eligible for a Pell Grant. The eligibility levels could be calibrated to the poverty line and adjusted to be more generous if program funding permits. However, in no case should the income cutoffs be less generous than those modeled under the Rethinking Pell Grants study group's proposal, which awarded the maximum award to students with family income at or below 100% of the poverty line and limited eligibility to students with family incomes lower than 200% of the poverty line. Tying eligibility to the poverty line, which is indexed for inflation annually, would mean that Pell Grant awards for students at different income levels would rise as prices in the economy rise. Detailed information about how such an award table could be constructed can be found in ***Rethinking Pell Grants***[3].

   – The Urban-Brookings Tax Policy Center modeled the effects of the Rethinking Pell Grants proposal on Pell Grant distribution. The results were quite positive, indicating that even if all eligible dependent non-FAFSA filers received grants based on the restructured award schedule, the cost of the program would not change significantly for dependent students. However, the number of dependent recipients would increase (3,596,780 under the Rethinking Pell Grants proposal compared to 3,045,290 in 2012-13).

   – Because there would be no adjustment for multiple family members in college, all current recipients with AGIs above 200% of the poverty level would lose Pell Grant eligibility.

   – There would be more recipients with AGIs below $40,000 and fewer with higher AGIs. There would be more dollars going to students with AGIs below $30,000 and fewer going to those with higher AGIs.

   – Most of those who file the FAFSA but do not receive Pell Grants would remain ineligible, but about 4% of FAFSA filers now ineligible for Pell would become eligible.

4. To increase the predictability of Pell awards, the maximum award should be adjusted each year by the increase in the CPI plus 1%.

5. By moving to a very simple Pell eligibility determination based on AGI and family size, award look-up tables would allow low- and moderate-income students to predict their Pell Grant awards well in advance of applying for aid. Look-up tables could be easily accessible on school, college, and government web sites. (The look-up tables would make it clear that applicants or their parents who file specified tax schedules or report negative AGI could not rely on these Pell Grant estimates.)

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3 **Rethinking Pell Grants** is a project convened by the College Board and funded by the Bill & Melinda Gates Foundation and the Lumina Foundation. Detailed information and background research on the recommendations of the Rethinking Pell Grants Study Group can be found at http://advocacy.collegeboard.org/college-affordability-financial-aid/rethinking-pell-grants.

Use of Prior-Prior Year Data

Currently eligibility is based on income information from the year immediately preceding enrollment. The timing of available income data is particularly acute for first-time applicants. For example, a freshman applying for assistance for the fall of 2014 must provide 2013 income and tax data in the spring of 2014, often long before their required filings to the IRS. Relying on "prior-prior year" (PPY) data would ensure that the majority of tax filers could populate FAFSA financial fields with accurate IRS data. In addition, students would be able to apply earlier for financial aid, potentially as early as the spring of their junior year in high school. This would allow them to receive information about their financial aid eligibility earlier, enabling them to plan ahead and make more appropriate college choices. Importantly, required verification would be eliminated for most applicants, removing a barrier to application completion and freeing up aid administrators to work directly with students and their families and to handle appeals.

In 2013 the National Association of Student Financial Aid Administrators (NASFAA) conducted a study of the impact of using PPY data on determining eligibility for federal student aid and on Pell Grant awards. Based on five years of data from more than 70,000 student records, NASFAA concluded that the U.S. Department of Education (ED) should use the authority granted under the Higher Education Opportunity Act to fully implement a PPY system because of the benefits to the neediest students of simplifying the process. Recognizing that such a change would not benefit all groups of students equally—the study found that independent students without dependents did not fare as well under a PPY system as other students—the organization also recommended that ED ensure that the system take into account the most current financial circumstances of applicants who had experienced significant changes from their PPY income to their income at the point of enrollment.

Meeting the Data Needs of States and Institutions

While many states and institutions support the goal of a simpler application and eligibility determination, there are concerns that less data will result in increased eligibility for their own need-based aid programs that in most cases are inadequate to meet the needs of current students. In addition, many worry about the ability to target their limited need-based aid equitably if they have less information with which to evaluate family financial strength.

To support the needs of these states and institutions, we recommend that more detailed IRS financial data be used to drive an economically sound need analysis formula that will help users evaluate the financial strength of applicants whose family income makes them ineligible for Pell Grants. Only data captured by the IRS would be used to calculate the EFC; as a result, number of family members in college, as well as dependent student income and assets, would be ignored in the formula. At a minimum, all data elements reported on pages 1 and 2 of the IRS tax return would be reported to states and institutions that require more detailed information. To ensure that this requirement does not add complexity for students and families, these data would be from the "prior-prior" year and would be made available by the IRS using a modified version of the Data Retrieval Tool. Ideally, the need analysis formula would be developed and updated by the U.S.

Department of Education in collaboration with representatives of state higher education agencies and institutions. Legislation would not be necessary, and economists would serve as expert consultants to the need analysis oversight committee.

In support of the Rethinking Pell Grants study group's proposal to make such a need analysis system available, the Urban-Brookings Tax Policy Center simulated the results of using more detailed IRS data to determine the family contribution. The modeled formula defined income as AGI minus capital gains plus losses (capital, business, farm, other). It did not allow for negative AGI. It imputed assets by assuming that reported interest and dividends represented 5 percent rates of return. Allowances and assessment rates were similar to, but not identical to those used in the existing Federal Methodology (FM). The simulation results made it clear that it would be possible to develop a formula that would yield a distribution of expected contributions similar to current policy[4].

Several simulation results suggest that a formula that uses more detailed IRS data would produce EFCs more reflective of family financial capacity. For example:

– Subtracting capital and other gains from income and adding back losses would increase significantly the average parent contributions (PCs) of the small number of filers with negative AGI (PCs for this group averaged $6,657 compared to $2,500 under FM). For independent applicants with negative AGI, the average contribution under the simulated formula was $2,176 compared to $101 under the current FM.

– Dependent applicants with family income of $125,000 or less would pay somewhat less under the simulated formula: $6,949 on average compared to $7,576 under FM. Independent applicants would pay about $300 more ($4,727 compared to $4,454). Of course, adjustments to the formula could achieve results more in line with current FM if this were the desired outcome.

– Applicants who reported family income higher than $125,000 would be required to pay more under the simulated formula: on average $41,497 compared to $37,765 for parents of dependent students; $37,174 compared to $30,411 for independent students.

Early Communications

Many students, especially those from low-income backgrounds, do not get information early enough about postsecondary opportunities and the financial aid for which they may be eligible. Students and families often overestimate the cost of attending college, basing any information they might have on published prices rather than net prices. As a result, they do not believe that college is a possible future pathway toward a career and do not take the steps necessary to prepare academically. By middle school, students begin to make critical choices about their academic future. To help them make the most informed choices possible, they and their parents need specific information, presented in simple language, about postsecondary options and financial aid eligibility.

While GEAR UP and TRIO Programs provide early information to a targeted group of low-income

4 Details of the simulation can be found in Rethinking Pell Grants at http://advocacy.collegeboard.org/college-affordability-financial-aid/rethinking-pell-grants

students, many students are not served by these programs. In addition, school counselor-student ratios, reported to be 471:1 in public secondary schools in 2010-11, make it difficult if not impossible for students to receive important guidance about applying to and paying for college. The problem is more daunting for older adults who do not have access to programs such as GEAR UP or to school counselors to help them make informed choices about education programs or institutions.

The College Board completed a research study in 2012, partnering with the College Foundation of North Carolina (CFNC), to determine the impact of providing to lower-income parents of middle school students, clear and simple information about how to pay for college. The study found that clear information specific to the family's circumstances made a substantial difference in their understanding of financial aid eligibility and college prices. In particular, parents in the randomly assigned test group demonstrated significantly greater understanding of college costs, net price, and grant eligibility than did parents in the control group.

To ensure that all students and families are aware of the importance of postsecondary education and the associated benefits, we recommend that the federal government provide college information annually, customized to the family's financial circumstances. The process should be automated, taking advantage of the IRS/U.S. Department of Education (ED) partnership, and should begin when the child begins school at age five. Families would check a new box on the IRS form each year, giving permission to the IRS to release information to ED, which would send information about the importance of college, paying for college, and financial aid eligibility. Families who receive public benefits would receive similar information through their providers.

Sending all families such information long before their children are old enough for college will encourage low- and moderate-income families to view college as affordable and provide more affluent parents with information to encourage pre-college planning and saving. Information would become more detailed when the child entered high school.

The annual communication could include the following information:

- Individual and societal benefits of postsecondary education
- Importance of academic preparation
- Available postsecondary options
- Prices of public institutions in the family's state of residence—both average published and net prices
- Pell Grant amount for which the child would be eligible if enrolled in college now
- Information about state need-based grant aid and if possible, estimated eligibility
- Advantages of wise borrowing
- Importance of college savings
- Eligibility for tax benefits

Opportunity for Further Simplification

Beyond the recommendations outlined, there is considerable interest among consortium members in eliminating the requirement for low-income students to reapply for financial aid each year because many continuing students miss state and institutional application deadlines and fail to complete the verification process. To deal with this problem, economists Sandy Baum and Judith Scott-Clayton recommended in their paper on Pell Grant reform (funded by the Hamilton Project) that eligibility be based on the three most recent years of IRS data, limiting the extent to which aid eligibility is affected by short-term income fluctuations. Under their proposal, eligibility would be fixed at the point of initial application, and students would not need to reapply each year. Income information would be accessed via the IRS Data Retrieval Tool so as not to complicate the process for students.

Unfortunately, because accessing the most recent three years of income data would require significant changes to the IRS Data Retrieval Tool, it is unlikely that such a change could be implemented in the near future. As a result, we are not recommending elimination of the reapplication requirement because income from a single year may not reflect the student's long-term financial situation. However, we believe that the approach described by Baum and Scott-Clayton offers interesting possibilities for further simplification of the application process, and we recommend that it be explored by ED in partnership with the IRS. As part of that effort, we recommend a pilot study to determine whether the requirement to reapply for federal student aid each year could be eliminated in the future.

Conclusion

Students from low-income backgrounds face numerous barriers in pursuing postsecondary goals and often the largest is financial. The proposals we set forth in this paper aim to eliminate many of the barriers to ensure that students are aware at an early age of the financial aid available to them and can follow a simple, transparent path to access it. We believe that our recommended approach will not only increase postsecondary opportunities for those students who are interested and prepared, but will help them to complete their credential or degree to increase their chances for a bright future.

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EXECUTIVE SUMMARY

The Gates Foundation provided funding to support four consortia in developing consensus recommendations related to common ideas and themes presented in the 2012-13 Reimagining Aid Design and Delivery (RADD) project. The College Board joined six organizations to focus on increasing simplification and transparency in the financial aid system. The goals of the RADD 2.0 consortium on simplification and transparency are:

– Continue to raise awareness about federal financial aid simplification and transparency issues.

– Inform the debate on the desirable outcomes and possible unintended consequences of reforms.

– Drive towards policy coherence on financial aid simplification and transparency.

The College Board supports the following strategies to simplify the financial aid system and increase transparency for the families accessing it:

– For most students, Pell Grant eligibility should be based on Adjusted Gross Income (AGI) and family size (number of exemptions). By moving to a very simple Pell eligibility determination, award look-up tables would allow low- and moderate-income students to predict their Pell Grant awards well in advance of applying for aid.

– "Prior prior" year income data should be used to determine aid eligibility in order to streamline the financial aid application process. Relying on "prior-prior" year data would ensure that the majority of tax filers could file their FAFSA with accurate IRS data in a more timely way (many FAFSA applicants can't access IRS data because they haven't yet filed current-year taxes). In addition, students would be able to apply earlier for financial aid, potentially as early as the spring of their junior year in high school.

– To support the needs of states and higher education institutions, we recommend that more detailed IRS financial data be used to drive an economically sound need analysis formula that will evaluate the financial strength of applicants whose family income makes them ineligible for Pell Grants.

– To ensure that all students and families are aware of the importance of postsecondary education and the associated benefits, we recommend that the federal government develop an early-awareness effort to provide college information annually, customized to the family's financial circumstances. The process should be automated, taking advantage of the IRS/U.S. Department of Education partnership, and should begin when the child starts school at age five.