



How College Financial Aid Works

by [Jim Belvin](#)

Introduction to How College Financial Aid Works

Next to buying a house, planning for college expenses can be one of the biggest financial projects that parents and their children undertake. Four years of college costs tens of thousands of dollars, and it is increasingly easy to break into the hundreds-of-thousands range, especially for advanced degrees. Parents, you've probably wondered just how you can manage to send your child to the college or university that he or she has dreamed about and earned the right to attend.



Photo courtesy Duke Photography

We all hear horror stories about how much college costs now and -- even worse -- how much it will cost in 10 or 20 years. Regardless of what you've heard, it's not too late to find a way to make paying for college manageable -- not easy, but manageable. Paying for college is a family affair -- parents and students work together to make college affordable. Obviously, the earlier you start, the easier it will be. However, it's never too late to make a difference.

There are three basic ways to pay for college. You can pay for it before your child enrolls, while he or she is enrolled in college or after graduation. Many people use a combination of the three. Think of the wide range of options as a smorgasbord from which you select the approaches that fit your family's payment strategy. In this article,

we'll examine how you can use college financial aid -- from scholarships to work/study jobs to student loans -- to help pay for that all-important education. Let's start planning!

What Is Financial Aid ?

There are a variety of financial aid tools available to students today, including scholarships, need-based awards, work-study employment and student loans. Let's discuss some of them:

Need-based Financial Aid

Well over 50 percent of today's college students receive need-based aid. **Need-based financial aid** eligibility is based on two simple issues -- cost of education and family ability to pay. The cost of education can vary significantly from institution to institution. Generally, these budgets include all reasonable costs (tuition, room, board) of attendance.

To apply for need-based financial aid, complete the **Free Application for Financial Aid (FAFSA)** and, if appropriate, the **College Scholarship Service's PROFILE**. These documents are used to determine what amount, if any, a family (and that means the parent and student) can provide toward the annual cost of attendance. Required amounts of family contributions may vary somewhat from institution to institution, but the formulas in place ensure that most expected contributions are similar.

The formulas consider a variety of family circumstances when determining eligibility. (The College Board Web site has some great [financial aid calculators](#) you can use!) Consequently, there is no real cut-off point or maximum income a family can have and still qualify for assistance. You may be surprised to learn that an increasing number of families with significant incomes now qualify for assistance. Every student, regardless of financial situation, should consider applying for need-based aid and see what happens.

How Do I Apply for Need-Based Aid?

There are two need-based aid applications being used nationally, the Free Application for Federal Student Aid (FAFSA) and the College Scholarship Service's (The College Board) PROFILE. The FAFSA, as the application for all federal funds, is required by all institutions. Many institutions will require complete copies of your most recent [tax](#) and W-2 forms. The PROFILE, which is generally viewed as the application for private or institutional funds, is required by many but not all institutions. If you are applying to a college whose aid awards include significant levels of institutional funding, there is a good chance that the school will require both forms. If you are unsure as to which form(s) is required, check with the school or simply file both forms. You want to assure yourself access to all available funding, so don't take any chances.

The FAFSA and the PROFILE are essentially 1040 line-item referenced financial statements. If you have completed your most recent taxes, use the numbers from these to complete your applications. If your tax forms aren't available, estimate. You can correct any errors when your tax forms are complete, so don't miss an application deadline

because you haven't finished with your taxes. In addition to collecting income and asset information, each form also collects demographic data including family size, parent age, number of students in college and other related information. You are also invited to provide each school with information on any extenuating circumstances that affect your family's ability to support educational expenses. Take advantage of the opportunity to provide this information by writing directly to the college you're considering. Don't be shy -- others will not be.

Formulas and Applying

Both the Department of Education and the College Scholarship Service apply "need analysis" formulas to the information your financial aid applications supply. These formulas, which were designed by congress and by the educational community, differ in important ways, but each estimates what amount your family can provide toward educational expenses in the upcoming year. If you are interested in reviewing these formulas, check the [Department of Education](#) and [College Scholarship Service \(College Board\)](#) Web sites. You can also find these formulas outlined in a variety of commercial publications available on newsstands.

Both the FAFSA and the PROFILE are available through guidance counselors' offices and both can be completed online. Either way, each form takes about an hour to 90 minutes to complete. You must complete and submit each form once every year. With each form, list all of the colleges to which you intend to apply. The Department of Education and the College Scholarship Service will take care of the rest by sending copies of your form to the institutions you have listed.

Divorced?

The custodial parent must complete both the FAFSA and PROFILE. Some schools that require the PROFILE will also require that the non-custodial parent complete a Divorced and Separated Form. This document will be included in the PROFILE and should be submitted directly to the college or university. If it is inappropriate for the non-custodial parent to complete the form, or if he or she refuses, write to the school to request an exception to this policy. If the custodial parent has remarried, the stepparent must also complete the FAFSA. There are no exceptions. PROFILE schools will often require information on stepparents as well.

A Financial Aid Example

As we already explained, need analysis and packaging policies can and do vary from institution to institution. Here is an example of what might happen (where I work) at [Duke University](#):

We ask the family to complete and submit the PROFILE and FAFSA no later than February 1. (We require tax forms, but those aren't due until May 1.) We also invite them

to submit letters that explain any extenuating circumstances that might affect their family's ability to support educational expenses.

At Duke, students are admitted without reference to their need for financial aid. This policy of "need-blind admissions" means that we do not determine an applicant's aid eligibility until after the student has been admitted. As soon as we are notified of a student's admission, we pull together the application materials, determine aid eligibility and prepare awards for those who are eligible. Who will be eligible? The formula we use considers a wide variety of circumstances -- there is no one answer. However, here is an example of a fairly typical applicant's award:

The Smiths are a family of four. Both parents work, and Melissa, the Duke applicant, will be the only one in college next year. Family income is roughly \$60,000, and their assets are pretty standard relative to their income. They own their own home and have offered no unusual circumstances.

In this case, the parents' contribution would likely range from \$8,000 to \$12,000. Melissa's contribution in this example is \$2,000, with \$1,900 coming from summer earnings and \$100 coming from Melissa's savings. The cost of attending Duke for next year will be approximately \$34,000. For illustration purposes, let's assume that the parents contribute \$12,000. So here are the numbers (all figures are in U.S. dollars):

Cost of Attendance	\$34,000
Parent Contribution	- 12,000
Student Contribution	- 2,000

Demonstrated Need	\$20,000

In addition to guaranteeing need-blind admissions, Duke meets 100 percent of each student's demonstrated need. Here is how this works:

Demonstrated Need	\$20,000
Work Study	+ 1,800
Loans	+ 4,600
Grants	+ 13,600

Total Award	\$20,000

The number of siblings in school at the same time is important. Parent contributions generally go down by 40 to 50 percent if more than one child is in school. Remember,

this is just one example, and your results are likely to be different. For specific details, contact your prospective institution's aid office.

What Happens If I Qualify?

If you demonstrate need, you are eligible for need-based financial aid. Demonstrated need is a simple concept -- it is each institution's cost of education minus the designated family contribution. So the "formula" looks something like this:

$$\text{Cost} - \text{Family Contribution} = \text{Aid Eligibility}$$

If your aid award includes federal dollars (and most do), your total aid may not exceed your demonstrated need. Some institutions will meet 100 percent of your demonstrated need; others will meet only a portion of that need. The brochure from each school will outline its policy on meeting need.

Regardless of the portion of need that a school meets, almost all package aid offers three types of assistance:

- **Work-study**
- **Deferred interest and payment**
- **Federal loans and grants**

The portion of each fund in the package varies from one college to another. While free-and-clear grants are everyone's favorite type of financial aid, don't discount work and loan opportunities.

Federal law requires that you re-apply for need-based financial aid each year. There are no exceptions. Applications are generally available in early December of each year. Mark your calendar to re-apply in December. You don't want to receive your fall bill and discover that you failed to apply for aid. At that point, it may be too late!

In most cases, a school will tell you of your financial aid eligibility at the time that admission is offered. Colleges and universities know that you are concerned about costs and most will not ask you to commit to them until they commit to you.

What If I Don't?

If you don't qualify for aid in the first year, apply again in the second year. Circumstances change and so does aid eligibility. You may be surprised to find that you receive aid in the second year. And if your circumstances change mid-way through an academic year, most institutions are willing to meet some or all of your newly demonstrated need.

Scholarships: Merit-based

Citizenship Requirements

To qualify for federal need-based aid, the student must be either a United States citizen or eligible non-citizen. Generally, you are an eligible non-citizen if you have an Alien Registration Receipt Card (I-1551), a conditional permanent residence (I551C), or are an eligible-non citizen with an Arrival-Departure Record (I-94). (For details, check page 2 of the Free Application for Federal Student Aid.) Although foreign students are not eligible for federal student aid, many institutions offer scholarships. If you are a foreign student in need of assistance, check with the college or university to which you expect to apply.

There are many and diverse scholarships out there for students today. Let's look at the kind that's based on merit.

Almost all parents expect that their child will win a **merit-based scholarship**. Many will, but, unfortunately, there are simply not enough to go around. That aside, students should apply for any for which he or she may be eligible. There are only four things you need to know about merit scholarships:

- You need to know which schools offer merit scholarships -- not all do. You can find this out by requesting brochures from each school that interests you or your young person.
- You need to know how and when to apply for each scholarship. Deadlines are critical. Don't miss out on scholarships because your application was late. The school's brochures will provide you with all the information you need to apply on a timely basis.
- Parents and students need to keep merit scholarships in perspective. Regardless of what you might hear, merit scholarships are not, by themselves, reason to attend a particular school. A merit scholarship may serve to underline the reasons for choosing a particular school, but remember, academic and social interests and goals should drive this decision.
- There are many different kinds of merit scholarships. Many are based on academic merit, but others are based on leadership, artistic or musical ability, dance and even such specialized activities as cheerleading.

Scholarships: Local and National

There are two kinds of local scholarships: the "Who-are-you-what's-your- heritage-where-are-you-from-who-do-you-know?" scholarships, and the competitive merit awards. For the first type of local scholarship, students are selected because of their religion, their ethnicity, their parents' professional affiliations or the companies that employ their parents.

The second group features scholarships for which students can compete locally. These include PTA scholarships and civic awards (such as those provided by the Kiwanis Club, the Exchange Club and the Jaycees). The first group of scholarships generally requires only an application, while merit scholarships usually require a paper, speech, project or other form of competition.

Someone in your community is going to receive these scholarships. There are four places where you can find out about these awards:

- **The kitchen table at your home** - Sit down as a family and consider your various family connections. Consider your religious affiliation. Parents, perhaps you are a member of a club or fraternal organization that offers scholarships for which your child may apply. Many corporations provide scholarships to the

children of employees. Perhaps your company does. If you have an affiliation that could lead to a scholarship, follow up on it!

- **The high school guidance counselor's office** - Students should stop by regularly and read the counselor's bulletin board. You may be surprised by what you find.
- **The local library** - The library bulletin board and resource section can provide you with very real scholarship opportunities.
- **The Internet** - The Internet is a rich source of scholarship opportunities -- both local and national. Focus your search engine on "scholarships" and check out some Web sites. Some good ones are [The College Board](#), [SallieMae.com](#), [USAGroup](#) and [Fastweb.com](#). These sites offer excellent advice on paying for college and often list national scholarships for which you may apply. As a rule, you should avoid working with any scholarship or financial aid search firm that charges a fee for its services. Almost without exception, any scholarship funds available for a fee are also available for free.

National Scholarships

Many national organizations, corporations included, offer valuable scholarships. Again, the World Wide Web is a good place to start your search for these.

Making a Student Independent

Many believe that aid eligibility will be based solely on the student's financial situation if he or she can be declared legally independent. This was true at one point. Congress, however, changed the rules in 1992. Now students may become independent **only** if they meet the following criteria:

- The applicant is 24 or older.
- The applicant is a graduate student.
- The applicant is a veteran.
- The applicant is married.
- The applicant is an orphan or a ward of the court.

What If I Have to Get a Job?

Most students can earn between \$1,500 and \$2,000 by working during the academic year. Student jobs (sometimes called work-study) generally require students to work between 10 and 15 hours a week. This may sound like a lot, but it isn't -- high school students often work more than that each week.

Working while in college offers the student more than just the chance to make money. College jobs allow students to work with faculty and administrators who can often serve as mentors. And students can often find jobs that relate to their academic work (lab work, research, etc.). Just as importantly, campus jobs often provide students with the opportunity to examine various career options. At the very least, potential employers appreciate the fact that students worked while they were in college.

Although working while in college is important, it's not for everyone. Working, like the rest of one's college experiences, must be kept in perspective. Working should be a complement rather than a hindrance to the student's academic activities. Try it -- if it doesn't work or if academic problems occur, talk with your academic dean. Immediately!

Summer employment - Although resting up from the rigors of the academic year or lounging around at the beach are much more fun than working, summer jobs can make a college education much easier to finance. The average student can make from \$1,500 to as much as \$6,000 by working during the summer. And internships and other forms of summer employment provide a student with another chance to look at a variety of careers. If the student receives a need-based aid award, a summer savings expectation will be included in your family contribution.

Internships and cooperative education programs - Internships and cooperative education programs provide students with wonderful opportunities to earn while they learn. Internships are generally available during the summer. Co-op programs, generally available during the academic year, often extend the period of enrollment beyond the normal four-year plan. This is something to consider since these programs often allow the student to work with potential employers while they are in school. This can be an invaluable experience and can sometimes lead to full-time employment after graduation. Check with your prospective college's career service office for details on both internships and co-op programs.

Cost of Education

As a general rule, the cost of education for an academic year includes tuition, fees, room and board, books, academic supplies, personal expenses and, in many cases, travel between campus and home. When considering a school's financial aid, be sure you understand what their educational costs include. Is the room on campus? Is it a single or a double? How many meals are included in the board plan? Do fees include insurance? If you aren't sure, contact the school and ask.

Reserve Officer Training Corps (ROTC)

Many parents who were in school in the '60s will remember that Reserve Officer Training Corps (ROTC) programs fell into disfavor with a lot of people. Well, that was then, this is now. Today, ROTC programs are back and they are very popular. ROTC programs are not for everyone, but they might be right for you or your student.

Offered by the Army, Air Force and Navy (not at every school, so check the brochure), ROTC programs provide participants with funds for tuition (sometimes full, sometimes partial), books, fees and a monthly stipend of as much as \$150. Students are expected to take a few military science classes, participate in drills and attend summer camp programs. Following graduation, ROTC students are required to spend some period of time on active or reserve duty.

As you consider ROTC programs, don't forget about the free clothing -- hats and shoes, nice travel bags (all in military colors, of course) -- summer vacations, and the fact that you don't have to look for a job following graduation. The possibility of subsidized graduate work can be an additional benefit.

What About Loans?

This is where we get to the "paying for college after graduation" part -- and that means borrowing. Borrowing should always be a last-resort method of paying for college. That said, borrowing can and should be used to close the gap between the resources available to your family and the cost of the institution your student deserves.

For many families, the **equity in the home** represents the largest "savings" account. If your home has equity value, you should consider using it to pay for college. Although not always true, home-equity-loan interest rates are often lower than those charged by commercial loan sources. Additionally, home-equity-loan interest is tax deductible, which further lowers the cost of attendance. Equally as important as low interest is the fact that home-equity payments can be extended over a longer period than just the four years of enrollment.

Tax Credits

Created by congress, the **Hope Scholarship** provides a tax credit based on the family's income and the tuition the family pays. Qualified families may claim up to \$1,500 as a tax credit. In addition, the **Lifetime Learning Tax Credit** is available to individuals who file a tax return and owe taxes. Depending upon your income, your family may claim a tax credit of up to \$1,000 per tax year (increasing to \$2,000 in 2003). For details on your eligibility, check with your college's financial aid office or the IRS.

There are, of course, student loans and parent loans -- both of which are becoming more important all the time as families try to pay the rising costs of higher education.

Student Loans

Federal loans are the most accessible and affordable loan resources now available to students. There are two federal programs available nationally, the **Stafford** and **Perkins** programs. Both provide interest-subsidized, payment-deferred loans that borrowers can repay after their enrollment ends. Interest -- capped at 8.25 percent for Stafford and 5 percent for Perkins -- begins to accrue only after the borrower begins to repay the loan. To qualify for interest-subsidized Stafford or Perkins student loans, the student must demonstrate need by completing the FAFSA. Although several different repayment plans are available, most students repay these funds over a 10-year period.

Although students may borrow as much as \$4,000 in Perkins funds each year, actual offers differ from institution to institution, based on availability and school policy. Stafford borrowers may borrow \$2,625 in the first year, \$3,500 in the second year and \$5,500 in the third and fourth years. Additional Stafford and Perkins loans, with higher annual borrowing limits, are available to graduate and professional students.

Perkins and Stafford are the loans most often included in student aid awards. For students who demonstrate need, interest payments are deferred until the student is no longer enrolled at least half-time.

Perkins loan funds include both federal and institutional funds and reside on campus. If you are offered a Perkins loan, you need only to sign the promissory note.

Stafford loans are slightly more complicated. You must complete a specific loan application and submit it to the lender. Banks or state lending agencies generally provide Stafford loan funds. If the school offering you the loan is a **Direct Loan school** (about 25 percent are), funds will come directly from the institution.

Students who are unable to demonstrate need through the FAFSA may still borrow from the Stafford student loan program. These funds are, however, unsubsidized and require that the borrower be responsible for interest from the point funds are disbursed. This can be paid while the borrower is in school or capitalized and paid at the time principal payments become due.

Because of the **interest subsidy** we mentioned, you should first consider federal loans. At the same time, be on the lookout for local and institutional loans, which can sometimes offer even better terms than federal programs. As with local scholarships, check with fraternal organizations and churches or synagogues. Finally, an increasing number of colleges and universities are offering institutional loans at very reasonable rates.

Regardless of who you borrow from, federal loan repayment schedules are amortized over time, with a maximum standard repayment period of 10 years (under some circumstances, other repayment periods are available). The repayment period is increasingly important. If you make your payments on a timely basis, you can reduce the interest rate you are charged -- sometimes substantially. The message here is: **Pay on time and you can save money**. If you have problems, contact your lender, who can offer you a variety of repayment options, even if you do have difficulties.

Parent Loans

A growing number of parent loans are available nationally. The federally supported **Parent Loan to Undergraduate Students** (PLUS) offers low interest (not interest-subsidized) loans for which repayment begins 60 days after funds are disbursed. And, of course, there are many private parent loans offered under a variety of terms and interest rates -- some allowing repayment over as long as 20 years.

Almost all parent loans require some type of **credit check**. The PLUS loan credit check is the most liberal, requiring only that parents have had no credit problems within 60 days of application. The credit check for private parent loans is more stringent and generally requires that the applicant's debt-to-income ratio meet a specified standard.

The good news about most parent loans is that the applicant can borrow up to their student's cost of education minus any available financial aid. Parent loans should be viewed as cash flow loans or as a way to close the gap between the cost of the school of choice and those other resources your family has identified.

Study Abroad

Studying abroad can be one of the most important experiences a student can enjoy as an undergraduate. At most institutions, need-based aid and merit scholarships may be applied to study-abroad costs. Like campus financial aid, need-based study-abroad assistance will be based on family ability to pay and the cost of education. Although standard expenses (room and board, tuition, etc.) will be included in a study-abroad budget, it is wise to double check that with your campus financial aid office.

Some Words of Wisdom

- Start saving for college NOW. This is good advice for parents and students because the more you save, the less you have to borrow.
- It's not the college's sticker price that matters. All that really matters is the **net cost** of education. In most cases, there is a difference between the family's out-of-pocket expense and the college's sticker price.
- Use time to its fullest advantage. For most families, college is the second largest expense they will ever incur. Most families pay for their homes over as many as 30 years -- consider paying for college over six to eight years, or longer.
- As your student creates the list of schools to which he or she will apply, don't eliminate a school just because it's expensive. A great deal of assistance is available, and you may be surprised at how much you or your student receives.
- Parents, get your child involved early in paying for college. By saving during high school and by working during college, students can make an important contribution toward supporting their educational costs. And it's the responsible thing to do!
- As a family, create a strategy that fits your particular set of circumstances. Remember -- there is no best way to pay for college.
- Keep educational costs in perspective. College costs may be going up, but there's good news, too. Recent studies indicate that those who earn a bachelor's degree on average will have lifetime earnings of approximately 60 percent more than those who stop at a high school diploma. The return on your investment can be extraordinary.

Here are a few final thoughts:

- If you create a family strategy through which you can start planning early, if you take advantage of the wide variety of programs available during college, and if you are willing to borrow when necessary and reasonable, then the college you deserve can be available.
- Why not view the financial aid officer at your college as a resource? These professionals will be pleased to help you think through the maze of payment

options available for your consideration. They are also good at helping students budget their expenses while in college. Maybe, just maybe, the aid officer can help you find a grant to replace the loan for which you might otherwise have to apply.

- **Parents!** - Remember, if you don't do all you can to ensure that your child is well-educated, he or she may come back home and live with you!

Lots More Information

About the Author

Jim Belvin is the director of financial aid at Duke University in Durham, NC. He has served in various leadership capacities in several professional organizations, including the National Association of Financial Aid Administrators. A trustee of The College Board, he also sits on advisory boards for the Sallie Mae Fund and the USA Group. He is a popular speaker on the topic of college financial aid and an advocate for strong student assistance programs.



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