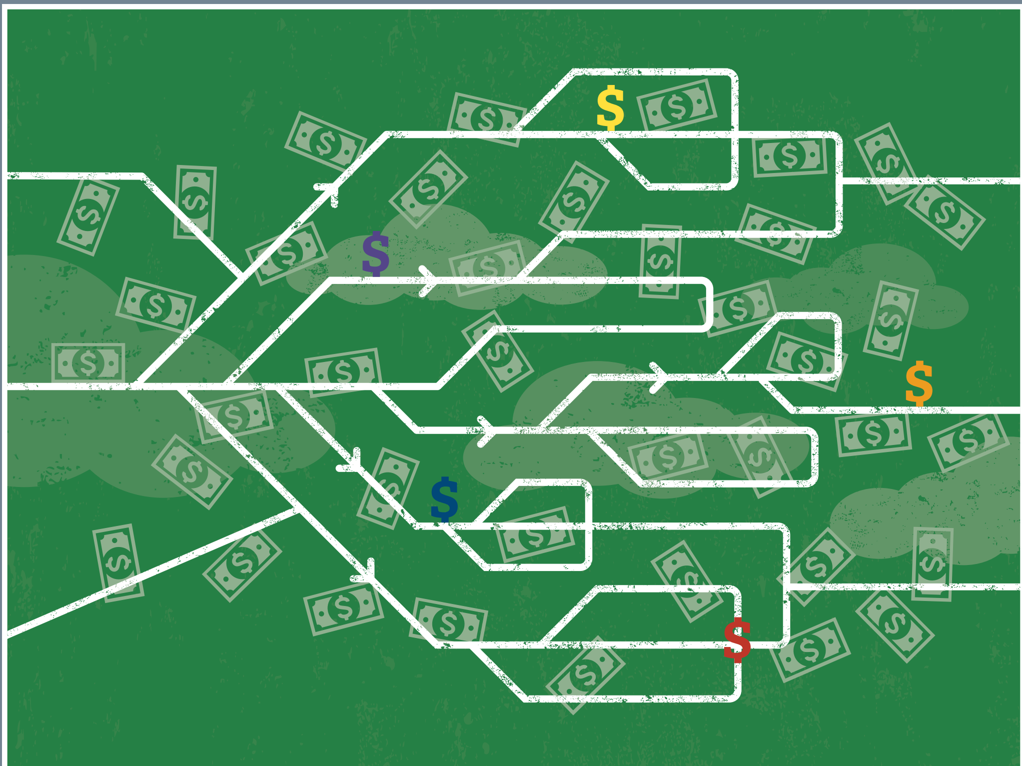
# Undergraduate Financial Aid in the United States



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# Section 3

# Overview of Undergraduate Financial Aid

## WHO PROVIDES AID?

What form should subsidies for higher education take? Governments subsidize college via two primary channels: 1) by directly funding public institutions, which then charge students reduced or even free tuition; and 2) by providing financial aid to individual students, which they then use at any eligible institution. The focus of this paper is financial aid. But these two channels are not mutually exclusive, generating a spectrum of alternative models of higher education finance. Significant variation exists across the United States, though from an international perspective the United States is an example of a high-tuition, high-aid system, while many European countries use a low-tuition, low-aid model.

To students and families, direct government subsidies to institutions are often invisible, and they are not always included alongside discussions of financial aid policy. Yet even in the United States, direct appropriations from state and local governments are one of the largest sources of support for undergraduates. And because of the potential for interactions between financial aid and direct appropriations—decreasing support via one channel, for example, may necessitate increases in the other—it is important to consider these two channels together.

Table 1 provides an overview of the current landscape of support for undergraduates, as well as trends over the past twenty-five years. The federal government is currently the largest source of student support by far, providing $122.7 billion in grants, loans, work-study, and tax benefits in 2014–2015. State and local governments provide the next largest source of total support, primarily through institutional appropriations ($75.3 billion in 2013–2014) but also through direct grants to students ($10 billion). Institutions themselves provide another $39.8 billion in grants, and private organizations and employers provide $11.3 billion in grant aid. (Not shown in this table is an additional $8.6 billion in nonfederal loans, primarily private loans. Since these loans confer no special advantages relative to other types of consumer credit, they are not considered here as a form of student aid.)

The table illustrates how the division of labor in higher education finance has shifted over time. The federal government has always been the largest provider of direct aid to students, but this investment has nearly quintupled over

## Table 1. Support for Undergraduates (in Billions, 2014 Dollars) by Source, over Time

| Aid Source | 1990–1991 | 2000–2001 | 2010–2011 | 2014–2015 (Prelim.) |
|---|---|---|---|---|
| STATE & LOCAL APPROPRIATIONS* | $70.7 | $84.7 | $79.7 | $75.3 |
| TOTAL FEDERAL, STATE, INSTITUTIONAL & OTHER AID** | $42.4 | $81.5 | $200.6 | $183.8 |
| ALL FEDERAL AID | $26.9 | $53.0 | $148.3 | $122.7 |
| All Federal Grants | $11.7 | $14.2 | $51.8 | $44.6 |
| Pell Grants | $9.0 | $11.0 | $39.0 | $30.3 |
| FSEOG | $0.8 | $0.9 | $0.8 | $0.7 |
| LEAP | $0.1 | $0.1 | $0.1 | $0.0 |
| Academic Competitiveness Grants | $0.0 | $0.0 | $0.6 | $0.0 |
| SMART Grants | $0.0 | $0.0 | $0.5 | $0.0 |
| Veterans and Military | $1.8 | $2.3 | $10.9 | $13.6 |
| Federal Work-Study | $1.1 | $1.1 | $0.9 | $0.9 |
| All Federal Loans | $14.1 | $32.7 | $77.5 | $62.1 |
| Perkins Loans | $1.4 | $1.3 | $0.7 | $1.0 |
| Subsidized Stafford | $11.2 | $15.7 | $31.6 | $24.7 |
| Unsubsidized Stafford | $0.0 | $10.6 | $33.5 | $25.9 |
| ParentPLUS | $1.5 | $5.1 | $11.6 | $10.6 |
| Education Tax Benefits | $0.0 | $5.0 | $18.0 | $15.2 |
| STATE GRANTS | $3.7 | $6.3 | $10.0 | $10.0 |
| INSTITUTIONAL GRANTS | $8.9 | $16.7 | $32.8 | $39.8 |
| PRIVATE & EMPLOYER GRANTS | $2.9 | $5.5 | $9.6 | $11.3 |
| **TOTAL FALL FTE ENROLLMENT** | **8,624,253** | **9,667,063** | **13,660,597** | **12,942,183** |

**Source:** State and local appropriations from National Center for Education Statistics (2015). Aid amounts and undergraduate FTE counts from The College Board, *Trends in Student Aid 2015* (New York: The College Board, 2015), Table 1A and Table 3 (online data). *Appropriations may include graduate education; 2014–2015 number is not yet available so is estimated at 2013–2014 amount. **Total aid excludes nonfederal loans, which total $8.6 billion in 2014–2015.

the past twenty-five years (even after adjusting for inflation, and regardless of whether student loans are included or excluded from consideration). Meanwhile, state and local appropriations have barely budged in real terms—increasing by just 6 percent since 1990, even as undergraduate enrollment rose by 50 percent (if state grants are included, total state and local funding still has

increased by only 15 percent). Not surprisingly, in periods when state/local funding (per student) at public institutions declines, tuition and fees at public institutions tend to rise in response.[14] This in turn increases the policy pressure for expanding financial aid, especially in core programs such as Pell Grants and federal tax benefits, to soften the blow.

## WHAT ARE THE MAIN TYPES OF AID AND THEIR KEY FEATURES?

Financial aid for college students takes a multitude of forms. This section provides an overview of the largest federal programs, as well as illustrative examples of other types of programs. Table 2 provides average and maximum award amounts and numbers of students served through each type of program.

The federal programs established in Title IV of the Higher Education Act of 1965 are known collectively as "Title IV aid" and include the precursors to Pell Grants, Stafford Loans, and Federal Work-Study. Title IV aid also includes a variety of smaller programs: Perkins Loans; Federal Supplemental Educational Opportunity Grants (SEOG); the Leveraging Educational Assistance Partnership (LEAP) program; Academic Competitiveness Grants (ACG); and National Science and Mathematics Access to Retain Talent (SMART) grants. Students must file a Free Application for Federal Student Aid (FAFSA) to apply for any Title IV aid. Veterans' benefits and tax benefits for college are two sources of federal aid that exist outside the Title IV system—and have grown rapidly in recent years. Embedded within the state, institutional, and private/employer grant categories are hundreds of separate programs with distinct characteristics.

Policy-makers and students should recognize that one dollar of one type of aid is not always directly comparable to one dollar of another type of aid. The most valuable (and most costly) types of aid are grants and tax benefits, because they are nonrepayable and generally require no work obligation, though some grants may include academic performance requirements or may be conditioned on prior work (like veterans' benefits). Student loans, because they eventually require repayment, are not as valuable to students (or as costly for the government) per dollar of aid. Similarly, since work-study programs require students to work, one dollar of work-study support is not the same as one dollar of aid that comes with no strings attached. Finally, different types of aid require different types of applications and often have different rules for maintaining eligibility, both of which can affect their value to students. The aid application process is discussed in more detail below.

14. College Board, *Trends in College Pricing 2015* (New York: The College Board, 2015); Sandy Baum, "Declining State Expenditures on Public Universities Are in Fact Driving Tuition Increases," *Urban Wire* (April 5, 2015), http://www.urban.org/urban-wire/declining-state-expenditures-public-universities-are-fact-driving-tuition-increases.

# Table 2. Students Served, Average and Maximum Award Amounts by Type, 2014–2015

| | Students Receiving | | Annual Award Amounts | |
|---|---|---|---|---|
| | Number (Millions) | Percent of Undergrads | Maximum | Average among Recipients |
| **Federal Title IV Aid** | | | | |
| Pell Grants | 8.248 | 35% | $5,775 | $3,670 |
| Stafford - Subsidized* | 6.556 | 27% | $5,500 | $3,750 |
| Stafford - Unsubsidized* | 6.230 | 26% | $7,500 | $6,660 |
| **Campus-Based Title IV Programs** | | | | |
| FSEOG | 1.470 | 6% | $4,000 | $500 |
| Federal Work-Study** | 0.638 | 3% | n/a | $1,500 |
| Perkins Loan | 0.550 | 2% | $4,000 | $2,210 |
| **Other Federal Aid** | | | | |
| Education Tax Benefits | 13.956 | 59% | $2,500 | $1,310 |
| Veterans' Benefits** | 0.890 | 4% | n/a | $14,110 |
| **State Grants** | 3.433 | 14% | varies | $2,644 |
| **Institutional Grants** | 4.633 | 19% | varies | $6,418 |
| Total Undergraduate Enrollment (12-month headcount) | | 23,856,278 | | |

**Source:** Unless otherwise noted, numbers of recipients and average amounts from The College Board, *Trends in Student Aid 2015* (New York: The College Board, 2015), Figure 7. For state and institutional grants, numbers of recipients and average amounts are estimated using NPSAS: 2012 data via NCES QuickStats. Numbers of recipients for Stafford Loans are for undergraduates only and are taken from U.S. Department of Education, Student Aid Data Center (2016). Total undergraduate enrollment from the Integrated Postsecondary Education Data System (IPEDS). *Loan limits listed are for dependent third-year students and higher; the unsubsidized loan maximum is reduced by students' subsidized loan eligibility. Independent students are eligible for an additional $4,000-$5,000 in unsubsidized loans per year. **These programs do not have statutory maxima. Veterans' Benefits include tuition/fee reimbursement up to in-state public institution levels, plus monthly housing allowances. Perkins Loans, FSEOG, and Federal Work-Study are determined by individual institutions but cannot exceed students' unmet need.

### *Pell Grants*

The federal Pell Grant program is the single largest source of grant aid, providing $30.3 billion in grants of up to $5,775 per year to over 9 million students annually in 2014–2015. Students can use their grant at any eligible institution and receive the same amount regardless of where they go. Although the eligibility formula is complex, family income is the main component: those with family income below $30,000 typically receive the maximum award, while only about

5 percent of those with family incomes above $70,000 receive any award.[15] If the award exceeds tuition and fees, students can use the extra amount for books, food, or other living expenses.

One of the appealing features of the Pell Grant program relative to other types of grants is the wide variety of students it supports to attend a wide range of programs. The only academic qualification to initially receive a Pell Grant is to be a high school graduate who has not already earned a bachelor's degree. The program is not limited to full-time enrollees (as some state grants are), nor does it require students to attend a particular institution. Finally, students need not enroll in a traditional academic program. Vocational degrees and certificates are also covered if they are credit-bearing programs at accredited institutions.[16] Pell Grants thus provide more funds for vocational training (or retraining) than does the Department of Labor. More than half of all Pell recipients are classified as independent, meaning they are either age twenty-four or older, married, veterans, or have dependents of their own. Nearly one-quarter of Pell recipients are over age thirty.[17]

### *Subsidized and Unsubsidized Stafford Loans*

The Stafford Loan program provides two types of loans for undergraduates: subsidized loans, which do not accrue interest while students are enrolled and are available only for those with financial need; and unsubsidized loans, which accrue interest but are available regardless of financial need. Both types offer interest rates, forbearance protections, and flexible repayment options that make them substantially more appealing than private sources of credit. Loan amounts are capped annually at levels that vary depending on students' class level and whether they are dependent or independent students.[18] Cumulatively, dependent students cannot borrow more than $31,000 for undergraduate study through the Stafford program. Independent students may borrow up to $57,500 in total Stafford loans.

The Stafford Loan program has undergone important changes over the years. Originally, the federal government did not provide loans directly but rather guaranteed the loans provided under the program by private lenders. In 2010, the guaranteed student loan program was eliminated, and since then

15. Author's calculations using 2014–2015 Federal Pell Grant Program End of Year Report, Table 070.

16. Noncredit trade and certificate programs are not currently eligible for Title IV financial aid, including Pell Grants. Some community colleges offer both credit/credential-bearing (eligible) and noncredit (ineligible) programs in vocational fields.

17. College Board, *Trends in Student Aid 2015* (New York: The College Board, 2015), 35.

18. For 2015–2016, the maximum subsidized Stafford Loan was $3,500 for dependent first-year undergraduates and $5,500 for third-years and beyond. Students can also take out additional unsubsidized loans. The maximum combined amount of subsidized and unsubsidized Stafford Loans is $5,500 for dependent first-years and $7,500 for third-years and up. Independent students have the same subsidized annual limits but higher combined annual limits, from $9,500 for first-years to $12,500 for third-years and higher.

all Stafford Loans have been issued directly by the federal government under the Direct Stafford Loan program.[19] Students' options for repaying Stafford Loans have also expanded. Although the default, mortgage-style ten-year repayment schedule remains the most common (used by 52 percent of borrowers in repayment), students can now opt into one of several income-based repayment programs that allow payments to vary with income and offer loan forgiveness to students with debt remaining after the end of a set repayment period (e.g., twenty or twenty-five years). Designing an effective and appealing income-based repayment option has proved challenging, as evidenced by the fact that five such options currently exist, implemented in succession.[20] Nonetheless, the number of borrowers in these income-based plans has more than doubled since 2013, from under 2 million to over 5 million in 2016 (growing from 12 percent to 24 percent of borrowers).[21]

*"Campus-Based" Title IV Aid Programs*

Perkins Loans (to be discontinued as of September 2017), Federal Supplemental Educational Opportunity Grants (FSEOG), and Federal Work-Study (FWS) are collectively referred to as the "campus-based" Title IV aid programs, because the federal government allocates funds for these programs directly to institutions, which provide some matching funds but have wide discretion on how the funds are distributed and managed at the campus level.[22] Of the three programs, only FSEOG awards must be directed toward undergraduates with exceptional financial need.[23] FWS awards may be distributed according to any prioritization strategy, as long as recipients have documented financial need. Since need is simply the difference between the full cost of attendance (including books, transportation, and living expenses) and other aid received, even

19. Direct lending was piloted in 1992, and the two methods of providing Stafford Loans coexisted over time until the financial crisis of 2008, after which many private lenders struggled to generate the liquidity required to continue offering student loans.

20. Income-based plans include an "income-sensitive" repayment plan, an "income-contingent" repayment plan, an "income-based" repayment plan, a "pay as you earn" repayment plan, and, most recently, the "revised pay as you earn" (REPAYE) plan. Not all borrowers are eligible for all plans. The REPAYE plan is both the most generous in terms of how payments are calculated (10 percent of discretionary income for up to twenty or twenty-five years), and in terms of which students may opt into the program (any Direct Loan borrower may opt into it).

21. Author's calculations using direct loan portfolio data from U.S. Department of Education, https://studentaid.ed.gov/sa/about/data-center/student/portfolio. These figures include only direct loans in repayment, deferment, or forbearance, representing $696 billion of the $1.2 trillion federal student loan portfolio.

22. When the Higher Education Act of 1965 was implemented, most federal aid flowed to institutions rather than directly to students (in the early years, aid flowed first to regional boards, and institutions had to apply for funds). The campus-based programs are vestiges of that early framework.

23. Perkins Loans, which offer a fixed interest rate of 5 percent on loans up to $4,000 per year (with interest subsidized during enrollment), may be directed toward graduate or undergraduate students with exceptional need.

relatively high-income undergraduates can qualify for FWS if they attend sufficiently expensive institutions.

Unlike other Title IV aid, whether a given student is awarded aid under one of these programs can vary dramatically by institution, because awards of this type depend both on the amount of available funding at each institution as well as the targeting strategy in place at the institution. The amount of funding available, in turn, depends upon an archaic institutional allocation formula of which the main component is essentially to provide institutions with whatever they got last year.[24] The formula thus advantages high-cost institutions that began participating in these programs early in their history. Public institutions receive less per student than private institutions, and many community colleges receive no funds under these programs. The inequitable distribution of campus-based allocations has been a policy concern for several decades, but efforts to modify the allocation formula have had limited effect.[25] Unease around the allocation formula may be one reason funding for these programs has withered while other aid programs have grown. The Perkins Loan program is scheduled to end in September 2017, while FSEOG and FWS have both shrunk by about 20 percent since 2000–2001.

### *Education Tax Benefits*

The delivery of aid for undergraduates through the tax system has increased over time, from nothing in 1990 to $15.2 billion in 2014–2015. More undergraduates now receive tax benefits for college than receive Pell Grants, though the value of the tax benefits is smaller on average. The American Opportunity Tax Credit (AOTC) is the largest tax benefit, providing a credit of up to $2,500 for education expenses (including course materials in addition to tuition and required fees).[26] The AOTC is available for up to four years of undergraduate education for students enrolled at least half-time. The Lifelong Learning Tax Credit (LLTC) enables part-time students in any type of program to receive a credit equal to 20 percent of tuition and required fees, up to $2,000.[27]

While only one LLTC may be claimed per household, the AOTC can be claimed per student enrolled. Moreover, up to $1,000 of the AOTC is refundable. The refundability of the credit and the allowance of expenses for course materials greatly enhances the value of the AOTC for low-income students who may have limited tax liability and tuition and fees covered by other sources of aid. Because filers can claim only one benefit per student and the AOTC is both more generous and has a higher phase-out range, the LLTC is currently mainly

24. This is called the "base guarantee." For more details, see David P. Smole, *Campus-Based Student Financial Aid Programs under the Higher Education Act*, Congressional Research Service RL31618 (Washington, D.C.: Government Printing Office, 2006).

25. Robert Kelchen, "Campus-Based Financial Aid Programs Trends and Alternative Allocation Strategies," *Educational Policy* (September 22, 2015), doi:10.1177/0895904815604213.

26. The AOTC covers 100 percent of the first $2,000 in expenses and 25 percent of the next $2,000.

27. See IRS Publication 970 for details: https://www.irs.gov/publications/p970/ch03.html.

relevant for postgraduate education or for undergraduates enrolled less than half-time. While the AOTC and the LLTC are the largest tax benefits for undergraduates, other tax benefits for college include the tuition and fees deduction and the deduction for student loan interest payments.[28]

*Veterans' Benefits*

GI Bills have played an important role in promoting college attainment among military veterans throughout the twentieth century. From 1985 to 2009, the main source of education aid for veterans was the Montgomery GI Bill (MGIB).[29] Although the MGIB is still available, many service members now benefit from a substantially more generous program implemented under the Veterans Educational Assistance Act of 2008 (often called the Post 9/11 GI Bill). This program provides eligible service members a tuition benefit equal to the maximum tuition and fees charged by any public institution in the individual's state of residence, plus a generous housing allowance.[30] Although just 4 percent of undergraduates receive these benefits, the average benefit is so high among those who qualify that total federal expenditures on veterans' education benefits in 2015 were larger than Pell Grants were before 9/11 (in inflation-adjusted dollars; see Table 1). Veterans' benefits can be used for an even wider range of educational programs than is supported by the Title IV aid programs (including on-the-job training and apprenticeships), and the programs it supports are not necessarily bound by Title IV regulations.

*State Grants*

The main source of state support for higher education is through direct appropriations to public institutions, which keep tuition lower than it would be otherwise. But over time, states have shifted toward providing support directly to students via need- and merit-based financial aid. State grants have nearly tripled since 1990–1991 (see Table 1). Most state grant programs are relatively small-scale and provide an average of just $771 per full-time-equivalent (FTE) student. But dozens of states now offer broad-based merit aid programs that award up to full tuition and fees at state public universities to students who meet modest academic criteria, such as a high school grade point average (GPA) of 3.0 and an above-average ACT or SAT score. These programs have grown faster than exclusively need-based state grants, and as of 2013–2014 slightly

28. Other tax benefits for education (not included in the totals in Tables 1 and 2) include the parental personal exemption for students aged nineteen to twenty-three and the exclusion of scholarship and fellowship income. For more information on tax benefits for college, see Susan Dynarski and Judith Scott-Clayton, "Tax Benefits for College Attendance," Working Paper 22127 (Cambridge, Mass.: National Bureau of Economic Research, 2015).

29. Andrew Barr, "Fighting for Education: The Effect of the Post-9/11 GI Bill on Degree Attainment," working paper prepared for Society of Labor Economics annual meeting, April 2016, http://www.sole-jole.org/16512.pdf.

30. Ranging from $800 per month in rural areas to $2,700 per month in New York City. See ibid. for additional details.

more than half of all state aid had at least some merit criteria, while 47 percent was exclusively need-based.[31] South Carolina—the state with the highest level of state grant aid per FTE undergraduate ($1,890)—allocates 83 percent of its funds via merit-based scholarships.[32]

### *Institutional Grants*

As shown in Table 1, institutional grants are the second largest single source of financial aid for undergraduates (second only to federal student loans), providing an average of $3,077 per FTE undergraduate. Just under one-quarter of all aid to undergraduates, or about one-third of all aid other than federal loans, comes in the form of institutional aid. Institutional grants can serve a variety of purposes, from supporting low-income students to simply optimizing enrollments. Just under half (46 percent) of all institutional grant aid is distributed purely based on merit, with the rest having at least some need-based component.[33]

Institutional grants are most common and largest at private not-for-profit four-year colleges: average institutional grants are almost ten times higher at these schools than at public four-year institutions ($7,601 per enrollee versus $865) and 57 times higher than the average at public two-year colleges ($133 per enrollee).[34] The role of institutional aid has also grown over time, more than quadrupling in size between 1990–1991 and 2014–2015. In recent years, this has helped blunt the impact of rising tuition, particularly at private four-year colleges. While published prices have risen steadily, increases in institutional aid as well as Pell Grants meant that net tuition and fees at these institutions in 2015–2016 were still slightly below their peak from 2007–2008.[35]

### *Place-Based Local "Promise" Programs*

Locally based "promise" programs have sprouted around the country with a mix of public and private funding. This new model for financial aid provision combines the simplicity, personal responsibility, and locally based features of state merit aid programs with more forgiving academic criteria. In some cases, the only merit requirement for eligibility is to graduate from a public high

31. National Association of State Student Grant and Aid Programs, *45th Annual Survey Report on State-Sponsored Student Financial Aid 2013–2014 Academic Year* (Washington, D.C.: National Association of State Student Grant and Aid Programs, 2015).

32. College Board, *Trends in Student Aid 2015.* South Carolina has three merit scholarships—the Palmetto, LIFE, and HOPE—for different tiers of high school performance.

33. Author's calculations using National Postsecondary Student Aid Survey (NPSAS): 2012 data on undergraduates, tabulated using NCES QuickStats. Students at private four-year institutions are much more likely than those at public four-year institutions to receive a merit-based grant (37 percent versus 9 percent), even though the percentage of dollars distributed based on merit is similar at both institution types.

34. Author's calculations using NPSAS: 2012.

35. College Board, *Trends in College Pricing 2015.*

school within a certain area. One of the first such programs was the Kalamazoo Promise, which in 2005 began offering full in-state college tuition to graduates of the Kalamazoo Public Schools in Michigan who had been enrolled in the district for at least four years.[36] Similarly, in 2008, local business and civic leaders provided funding to establish the "Knox Achieves" program in Knox County, Tennessee, which guarantees free community college tuition and fees to high school seniors who sign up, apply for financial aid, and meet with a mentor.[37] The program expanded to twenty-two counties in 2011 and became the model for a statewide "Tennessee Promise" program that rolled out in September 2015. Since the launch of the Kalamazoo Promise, thirty-one communities have implemented promise programs across the country, though with varying benefits, eligibility criteria, and funding sources.[38] These programs have also been cited as models for the Obama administration's College Promise proposal to make the first two years of community college free (this proposal is discussed in more detail in Section 4).

## AID APPLICATION, ELIGIBILITY, AND ACCOUNTABILITY

Aid that flows to individual students typically requires an application to determine whether students meet the specified income and/or merit-based eligibility requirements. Another set of eligibility requirements applies to institutions and is used to determine where students may use their aid. For both students and institutions, certain financial and performance criteria must be maintained over time in order to continue receiving federal aid.

### *Student Eligibility and the FAFSA Process*

The Title IV aid programs—Pell Grants, Stafford Loans, and the campus-based aid programs—all require students to file a FAFSA. This form, which can be completed online several months prior to college entry, is also required for many

36. See Timothy J. Bartik and Marta Lachowska, "The Short-Term Effects of the Kalamazoo Promise Scholarship on Student Outcomes," *Research in Labor Economics* 38 (2013): 37–76; Timothy J. Bartik, Brad Hershbein, and Marta Lachowska, "Longer-Term Effects of the Kalamazoo Promise Scholarship on College Enrollment, Persistence, and Completion," paper presented at American Education Finance and Policy Annual Conference, Washington, D.C., February 2015.

37. See Celeste K. Carruthers and William F. Fox, "Aid for All: College Coaching, Financial Aid, and Postsecondary Persistence in Tennessee," *Economics of Education Review* 51 (2016): 97–112.

38. Lindsay Page and Judith Scott-Clayton, "Improving College Access in the United States: Barriers and Policy Responses," *Economics of Education Review* 51 (2016): 4–22.

state and institutional aid programs.[39] The FAFSA collects detailed information about the student's (and parents', where applicable) household structure, income, assets, and various other benefits and expenditures (such as education tax credits claimed, child support paid or received, and other money received or paid on the student's behalf). From this information, the U.S. Department of Education computes an expected family contribution (EFC), an estimate of how much the family can pay out of pocket for college. The formula itself is incredibly complex, but the main determinants of the EFC are dependent/independent status, family income, family size, and number of students currently enrolled in college.[40]

Once the EFC is computed, "need" is defined as the difference between the cost of attendance (such as tuition, fees, books, living expenses) and the family contribution. The EFC is provided to both students and the schools to which they have applied. Financial aid offices at each institution then use the EFC to "package" each student's financial aid awards, including aid from all sources.[41] Students then receive a letter from each institution informing them of their annual aid package. Although online FAFSA applicants immediately receive estimates of their EFC and Pell eligibility, until they receive their institutional aid letters they do not have complete information on what college will cost for them.

The complexity of the FAFSA application process is well documented. Despite attempts to simplify the form in recent years, it still contains more than a hundred questions about income, assets, and expenses. Moreover, the FAFSA may not be the only aid application students need to fill out. While most states and public institutions rely on FAFSA elements for their own need-based aid programs, many private not-for-profit institutions also require the College Board's CSS/Financial Aid PROFILE®.[42] This longer, more detailed application includes additional questions about family circumstance, income, assets, and liabilities that have little consequence for determining federal and state aid eligibility but help institutions more precisely target their own aid to families throughout the income distribution.

39. Until recently, students could not file a FAFSA before January 1 of the year of enrollment, since the form relied upon information from the prior tax year (for instance, 2014 for a 2015–2016 enrollee). Beginning with the 2016–2017 cycle, the FAFSA will collect information from the prior-prior tax year (2014 for a 2016–2017 enrollee). The goal of this recent change is to enable students to apply for and learn their aid eligibility several months earlier than was possible in the past (October instead of January).

40. Six formulae are used, depending upon whether the applicant is dependent or independent, with or without dependents of their own, and whether income is low enough to qualify students for a simplified formula.

41. While calculating eligibility for various programs can require intricate formulas, Pell awards are generally equal to the Pell maximum minus the EFC, while subsidized loans are equal to the cost of attendance minus the EFC and other aid received, up to the relevant loan maximum. Pell awards are prorated for less-than-full-time enrollment. Stafford Loans are not prorated though less-than-full-time enrollment may affect eligibility by reducing the cost of attendance.

42. CSS originally stood for College Scholarship Service.

Students must file a FAFSA annually, so aid eligibility may fluctuate from year to year. Some students lose aid simply because they fail to reapply.[43] Students also may lose aid due to academic performance—and not just in "merit-based" programs: even need-based programs have minimum performance standards. For example, all Title IV federal student aid recipients must maintain "Satisfactory Academic Progress" (SAP). While SAP standards can vary by institution, they commonly require that students maintain at least a 2.0 cumulative GPA and complete at least two-thirds of the credits they attempt. More than one in five first-year Pell recipients fails to meet the GPA criterion alone, with higher rates at public institutions. Estimates suggest perhaps 40 percent of first-year aid recipients at community colleges may be at risk of losing eligibility due to performance.[44]

### *Institutional-Level Eligibility*

To ensure that students use federal student aid at legitimate postsecondary institutions, institutions must also apply to become Title IV eligible. Students cannot receive Pell Grants, Stafford Loans, or campus-based federal aid if they attend an ineligible institution. To become eligible, institutions must be authorized in their home state, have existed for at least two years, and be accredited by an approved accrediting agency.[45] They also must agree to report annually on an extensive set of topics, including institutional characteristics, enrollment, tuition and fee charges, financial aid disbursements, student persistence and completion, and institutional revenues and expenditures. No more than 90 percent of an institution's revenue can come from Title IV aid—a limitation approached by some for-profit institutions.[46] Revenue from other federal sources, such as veterans' benefits, does not count toward this limit.

Federal mechanisms for monitoring quality and enforcing minimum standards have been an active area of policy-making in recent years. For example, for institutions to maintain eligibility, the default rate among students who take out federal student loans cannot exceed a set threshold in three consecutive years. The loan default rate used to be measured just two years after students entered

43. Kelli Bird and Benjamin L. Castleman, "Here Today, Gone Tomorrow? Investigating Rates and Patterns of Financial Aid Renewal among College Freshmen," *Research in Higher Education* 57 (4) (2016): 395–422; Benjamin L. Castleman, Benjamin L. Page, and Lindsay C. Page, "Freshman Year Financial Aid Nudges: An Experiment to Increase FAFSA Renewal and College Persistence," *Journal of Human Resources* 51 (2) (2016): 389–415.

44. Lauren Schudde and Judith Scott-Clayton, "Pell Grants as Performance-Based Aid? An Examination of Satisfactory Academic Progress Requirements in the Nation's Largest Need-Based Aid Program," CAPSEE Working Paper (New York: Center for the Analysis of Postsecondary Education and Employment, 2014), forthcoming in *Research in Higher Education*.

45. For a summary of Title IV requirements, see Stephanie Riegg Cellini and Claudia Goldin, "Does Federal Student Aid Raise Tuition? New Evidence on For-Profit Colleges," *American Economic Journal: Economic Policy* 6 (4) (2014): 174–206.

46. The average is 70 percent at for-profit institutions. TICAS, "Q&A on the For-Profit College '90–10 Rule,'" January 25, 2016, http://ticas.org/sites/default/files/pub_files/90-10_qa_0.pdf.

repayment, but in 2009 this window was extended to three years.[47] In addition, the Department of Education established a new "gainful employment" requirement that went into effect in 2015. Under the new rule, which applies to nearly all programs at for-profit institutions and vocational certificate programs at community colleges, programs can lose Title IV eligibility if its graduates have annual loan payments exceeding a certain percentage of their income.[48]

Policy-makers have also raised questions in recent years about both the rigor and objectivity of the accreditation process. Accreditors rarely decline to accredit institutions that they evaluate—even those with poor student outcomes, shaky finances, and accusations of fraud and abuse. The federal panel that oversees accreditors made news in June 2016—because the action was so rare—when they voted to no longer recognize the Accrediting Council for Independent Colleges and Schools, which accredits many for-profit colleges.[49]

47. Prior to 2009, the cohort default rate was based on a two-year window and a 25 percent threshold, meaning that no more than 25 percent of borrowers who entered repayment in one year had defaulted by the end of the next year. In 2009, the window was extended to three years—which more than doubled estimated default rates at for-profit institutions—and the threshold raised to 30 percent. See FinAid.org, "Cohort Default Rates," http://www.finaid.org/loans/cohortdefaultrates.phtml (accessed August 19, 2016), for a history of relevant regulations.

48. Loan payments are considered excessive if they exceed 12 percent of total earnings and are greater than 30 percent of discretionary earnings. See *Federal Register* 79 (211) (October 31, 2014), https://ifap.ed.gov/fregisters/attachments/FR103114Final.pdf.

49. Paul Fain, "Accreditor on Life Support," *Inside Higher Ed* (June 24, 2016), https://www.insidehighered.com/news/2016/06/24/federal-panel-votes-terminate-acics-and-tightens-screws-other-accreditors.