

**U.S. Department of Education – Report to Congress on Efforts to Simplify the
Free Application for Federal Student Aid (FAFSA)
January 16, 2009**

BACKGROUND

On August 14, 2008, President Bush signed the Higher Education Opportunity Act (HEOA) (Pub. L. No. 110-315) into law, amending the Higher Education Act of 1965 (HEA). Section 483(f)(2) of the HEA, as amended by the HEOA, requires the Secretary of Education (Secretary) to submit to Congress a report on some of the Secretary's efforts to simplify the Free Application for Federal Student Aid (FAFSA). Specifically, the report must provide the following information:

- How the expected family contribution of a student can be calculated using substantially less income and asset information than was used on March 31, 2008;
- The extent to which the reduced income and asset information will result in a redistribution of Federal grants and subsidized loans under Title IV of the HEA, State aid, or institutional aid, or in a change in the composition of the group of recipients of such aid and the amount of such redistribution;
- How the alternative approaches for calculating the expected family contribution will rely mainly, in the case of students and parents who file income tax returns, on information available on the 1040, 1040EZ and 1040A tax forms, and include formulas for adjusting income or asset information to produce similar results to the existing approach with less data;
- How the Internal Revenue Service (IRS) can provide to the Secretary income and other data needed to compute an expected family contribution for taxpayers and dependents of taxpayers and when in the application cycle the data can be made available;
- Whether data provided by the IRS can be used to prepopulate the electronic version of the FAFSA with student and parent taxpayer data or generate an expected family contribution (EFC) without additional action on the part of the student and taxpayer;
- The extent to which the use of income data from two years prior to a student's planned enrollment date will change the expected family contribution computed in accordance with part F of Title IV of the HEA (need analysis formula), and potential adjustments to the need analysis formula that will minimize the change; and
- The extent to which the data elements collected on the FAFSA on March 31, 2008, that are needed to determine eligibility for student aid or to administer the Federal student financial aid programs, but are not needed to compute an expected family contribution, such as information regarding the student's citizenship or permanent residency status, registration for selective service, or driver's license number, can be reduced without adverse effects.

The process and analysis used to prepare this report builds on work already done by the U.S. Department of Education (Department) on simplifying the FAFSA process. The Department consulted with financial aid professionals, academic researchers, and students and families. These consultations led the Department to analyze whether the determination of a student's eligibility for, and amount of, federal student aid could be based on just two data items – the family's IRS Adjusted Gross Income (AGI) and the number of IRS exemptions. For reasons more fully explained below under the "Congressional Inquiry" section of this report, the Department determined that the use of those two items would be a simpler method of determining a student's eligibility than the current approach.

The use of these two data items would transform the calculation of a student's eligibility from one that attempts to determine the family's "ability to pay" to one that simply identifies the most needy families for receipt of federal subsidized aid. This shift is consistent with the "Automatic Zero-EFC" and "Simplified Needs Test" EFC calculations currently required by the HEA, which identify applicants from low-income families and provide them with a determination of eligibility based primarily on family income.

Replacing the more than 45 questions on income and assets that are now required to determine eligibility with just these two data items (AGI and IRS exemptions) would dramatically simplify the FAFSA form. As discussed in greater detail later in this report, this reduction in required data elements would simplify the entire financial aid application process and provide the opportunity for students and families to have more specific and reliable information on the types and amounts of federal student aid they would be eligible to receive. This is in contrast to the current system, which provides a family with only an "expected family contribution," which is nothing more than the amount they are not eligible to receive. However, this approach to the student financial aid process cannot be implemented by administrative changes to the FAFSA form. As explained below, it will require statutory changes to the HEA.

Free Application for Federal Student Aid (FAFSA)

The HEA requires the Secretary to produce, distribute and process--free of charge--a single common financial reporting form (the FAFSA) to determine a student's eligibility for aid under Title IV of the HEA. The HEA also requires the Secretary to develop and maintain an electronic version of the form. Currently, the paper FAFSA is six pages long with more than 100 questions and an additional four pages of instructions. The data items included on the FAFSA are, in large part, dictated by the requirements of the need analysis formula contained in the HEA (Part F of Title IV) and include a number of questions related to income (both taxable and untaxed), assets, family size, number in college, student's and parent's age and marital status, and student's grade level. Most of this information is used to calculate the student's expected family contribution (EFC). The EFC then determines the student's eligibility for financial aid (see *application process below*). To calculate a full-time student's eligibility for a Pell grant, the EFC is subtracted from the annual maximum Pell grant award. To determine eligibility for other subsidized aid, the EFC is used with the cost of attendance and other aid to calculate how much additional aid the student may receive.

The current FAFSA and EFC formulas have long been questioned by financial aid professionals, academics, families, and others with regard to the complexity, relevance, and fairness of the formulas. In a report entitled *A Test of Leadership – Charting the Future of U.S. Higher Education (Sept. 2006)*, the Secretary's bipartisan Commission on the Future of Higher Education found that the current Federal financial aid system "is confusing, complex, inefficient, duplicative, and frequently does not direct aid to students who truly need it." (P. 3). The Commission recommended that the entire financial aid system be restructured and the current

FAFSA be replaced “with a much shorter and simpler application.” (P. 3). The Commission further stated that “[t]he application process should be substantially streamlined by analyzing student need through a simple criterion such as family income.” (P. 19).

The Department’s Advisory Committee on Student Financial Assistance issued similar findings. In its 2005 report entitled *The Student Aid Gauntlet: Making Access to College Simple and Certain*, the Advisory Committee found that “students and families are often still baffled by [the financial aid] process and cringe at the sight of application forms.” (P. 12). The report further notes that the financial aid application process can “undermine educational aspirations, plans, enrollment, and persistence.” (P. 12).

Congress also recognizes the need for simplification. One Member stated that “[i]t shouldn’t be easier to get a loan from the Export-Import Bank than to get financial aid to attend college.”¹ Moreover, in enacting the HEOA, Congress required the Secretary to take a number of actions to improve the financial aid process. Specifically, Congress directed the Secretary to:

- Work to make the FAFSA more consumer-friendly and to make questions on the FAFSA easy for students and families to read and understand;
- Develop a simplified form for students from low-income backgrounds;
- Examine how, and in what manner, the IRS can provide income and other data from pre-existing tax forms in order to determine a student’s federal student aid eligibility; and
- Establish a pilot program for dependent students that would inform them by the fall of their senior year of high school of possible federal aid award amounts based on data from the prior tax year - known as the “prior-prior” year.

The Financial Aid Application Process

The financial aid application process today requires completion of the FAFSA on or after January 1 of each calendar year for which the student will be entering (or continuing) postsecondary education. For example, a student may complete and submit a FAFSA on or after January 1, 2009 for the 2009-2010 academic year, which begins in August or September 2009 at most schools.

Most students begin their FAFSA process in February and March. However, there are many, including first-generation college students, non-traditional students, and students from underrepresented backgrounds, who, for a variety of reasons, do not begin the FAFSA process until much later. Some do not begin the process until just before, or even after, they actually begin their course of study.

When completing the FAFSA, students and their families may be required to respond to the more than 100 questions, 45 of which are specifically used to calculate the statutorily defined EFC. The expected family contribution, notwithstanding its name, is effectively an index that is used to determine the applicant’s eligibility for, and amount of, federal aid (grants, subsidized loans, and work-study). The completion of the on-line version of the FAFSA is a somewhat less daunting task as a result of its use of “skip-logic” to allow some questions to be passed over. However, the completion of the FAFSA -- whether on-line or in paper form -- nevertheless is

¹ Press Release, Office of Congressman Rahm Emanuel, “Emanuel Plan to Simplify College Financial Aid Form To Be Voted on Tomorrow” (July 30, 2008).

challenging for many students and families. In its 2007 report entitled *Going to the Source: A Practical Way to Simplify the FAFSA*, the Institute for College Access and Success stated, “[t]he financial aid application process, whether in its paper or online form, is long, confusing, intimidating in tone, and requires a great deal of personal and family financial information that can be especially difficult for students from low-income families to collect.” (P. 4).

Once the EFC is calculated, a Student Aid Report (SAR) is generated and sent to the student, to institutions selected by the student, and the student’s state of legal residence. The SAR is a full report of the information reported on the student’s FAFSA application, including the EFC as calculated under the statutory formulas. However, the SAR contains no specific information on the student’s eligibility for, or amount of, a federal grant(s), loan(s) or work-study aid. Therefore, even after completing a lengthy and often confusing application, the student and family have no more information on their ability to finance the student’s education than before the application was completed. In most cases, a student does not learn of the types or amounts of financial aid he or she is eligible to receive until notified by the postsecondary schools listed on the FAFSA. For most first-time students, this notification, at the earliest, occurs in mid-to late-spring preceding the start of the academic year and may be after those same schools require students to make a commitment to attend. Continuing students often do not know their eligibility for federal aid until late spring or the summer preceding the start of the next school year.

This process and timeline is too often a barrier to students who wish to participate in postsecondary education, especially students from low-income families, first-generation college students, and those who do not have access to counselors or mentors to assist them through the process. The volume and type of data required on the FAFSA can be intimidating and daunting for students and families. For instance, the 2007 report from the Institute for College Access and Success stated that “[s]ome of the questions, such as those asking for checking account balances, create the inaccurate impression that parents and students will have to spend their last pennies before any aid is made available.” (P. 4).

Simplification

Following the recommendation of the Secretary’s Commission on the Future of Higher Education to restructure the aid system and shorten and simplify the application form, and in conjunction with the Department’s own analysis, the Secretary developed a set of principles for reform of the federal student aid process. These principles include requesting information on the FAFSA that is easily obtainable and verifiable and that is necessary to determine eligibility and award levels. Additional principles include that the application process and the form would: (1) ensure that federal student aid is targeted to the neediest students; (2) be independent of other aid; and (3) be predictable, portable, and distributed through fewer federal programs to ensure a consistent application process.

On October 1, 2008, at Harvard University, the Secretary unveiled a prototype of a simple two-page FAFSA (attachment A), which presented one possible way to reduce the burden of the application process and improve access to federal aid. The prototype has fewer than 30 questions with only two related to financial information – Adjusted Gross Income and number of IRS exemptions. Both of these items are easily obtainable, understandable, and completely verifiable. A version of this prototype FAFSA, or others like it, would simplify the process, and meet the objectives of a simplified, transparent, and targeted federal student aid program, process, and application. This concept is more fully explained in the response to item I below.

Congressional Inquiry

The information on financial aid simplification requested by Congress in section 483(f)(2) of the HEA follows:

I. How the EFC of a student can be calculated using substantially less income and asset information than was used on March 31, 2008.

To reduce the amount of information needed to determine a student's eligibility for federal student aid, the statutory need analysis formula must be changed as well as how the results of those calculations are used. The Department's analysis of several years of applicant and recipient data makes it clear that the eligibility of students from low-income backgrounds for subsidized federal student aid (grants, subsidized loans, and work-study) can be determined using significantly less data than what is currently required. Specifically, eligibility for subsidized federal aid, targeted to the neediest students, can be determined using only the family's IRS Adjusted Gross Income and the number of IRS exemptions claimed. Therefore, the FAFSA would no longer need to contain the current numerous questions about other taxable income, untaxed income, or assets.

Ultimately, policymakers would determine how AGI and IRS exemptions can be used to establish the criteria for eligibility for subsidized federal aid.

The College Board in its report entitled *Fulfilling the Commitment: Recommendations for Reforming Federal Student Aid (September 2008)* suggests that the maximum Pell eligibility rise with poverty level, with a maximum Pell grant award at 150 percent of the poverty level, and a phase down to zero at 250 percent of the poverty level. While the College Board's report recommends one approach, there are alternative thresholds that could be considered by policymakers in determining eligibility for federal student aid.

II. The extent to which the reduced income and asset information mentioned above will result in a redistribution of federal grants and subsidized loans under Title IV of the HEA, State aid, or institutional aid, or in a change in the composition of the group of recipients of such aid, and the amount of such redistribution.

The extent of any impact of a reduction in data elements will be determined when policymakers set the criteria for eligibility to achieve specific policy and funding objectives. The setting of the criteria for eligibility will directly determine the amount of aid and its recipient distribution.

States and institutions will need to determine the extent to which a revised federal eligibility determination will be sufficient to meet their funding and policy objectives. If states and institutions determine that the Federal process does not provide the information they need, there are a variety of means, including using data sharing technologies, whereby states and institutions can obtain additional information without disrupting or complicating the simplified federal process.

III. The extent to which the Department’s alternative approach for calculating the EFC (i) relies mainly, in the case of students and parents who file income tax returns, on information available on the 1040, 1040EZ, and 1040A tax forms; and (ii) includes formulas for adjusting income or asset information to produce similar results to the existing approach with less data.

As previously discussed, an alternative approach to the current system could rely on limited data accessible from the completed IRS forms 1040, 1040EZ, or 1040A. The AGI and number of exemptions claimed, for example, can be obtained from page one of a federal income tax return. For an independent student, the information would be from the student’s (and spouse’s, if applicable) federal tax return. For a dependent student, the information would be taken from the parent’s tax return. In addition to being understandable and obtainable by the family, these two data items can be verified by either a manual or electronic verification process. In cases where the student or parent did not, and will not, file a tax return, the student would report the amounts comparable to what would be included as AGI and number of exemptions.

An alternative approach would allow legislators to produce results similar to those in the current process or to achieve alternative results to meet desired policy objectives for the distribution of aid while greatly simplifying the process. As noted earlier, the approach suggested in this report can be implemented in a way that leaves these important decisions to legislators.

IV. The manner in which the Internal Revenue Service can provide to the Secretary income and other data needed to compute an EFC for taxpayers and dependents of taxpayers, and when in the application cycle the data can be made available.

Under the approach presented in this report – using only AGI and IRS exemptions – it is possible that, under a set of data matching protocols, the IRS could provide those items either in “real or near-real time” at the time the student is filing his or her electronic FAFSA or soon after the FAFSA is filed as part of a verification process.

The Department is currently working with the Internal Revenue Service to implement a “consent based” approach for sharing data where the applicant (and parents for a dependent student) would provide consent to the IRS for the release of information to the Department. This work is currently being conducted in the context of reducing “improper payments” (an improper payment occurs when, for instance, a student or family receives too much or too little aid because they entered incorrect information on the FAFSA) and not to provide a mechanism for the pre-population of the FAFSA. The Department is also looking into how a simplified approach with a focus on data pre-population could be implemented in the future.

There are, however, a number of significant policy, timing, and operational challenges to be addressed. The biggest challenge with any process (including the current process) that determines eligibility based on information from a family’s tax return is the significant calendar differences between the IRS tax return filing requirements and the application process for student aid. For example, to the extent that early filing of the FAFSA is desirable, at least as early as the fall preceeding the upcoming award year, there would be no data available since the tax year would not have yet ended. Even within the current process (FAFSA application process beginning on January 1), it is unlikely that tax return information would be available for the majority of financial aid applicants who complete their FAFSA weeks, and in some cases months, before the general tax-filing deadline of April 15.

Use of “prior-prior” tax year information would address most of these calendar issues. However, additional analysis needs to be performed to determine if use of prior-prior tax year information is practicable and, if so, for which groups of students.

V. How the data provided by the Internal Revenue Service can be used to (i) pre-populate the electronic version of the FAFSA with student and parent taxpayer data; or (ii) generate an EFC without additional action on the part of the student and taxpayer.

In addition, to the calendar and legislative issues discussed above, there are other timing issues that would influence any attempt to “pre-populate” a student’s FAFSA with data from the IRS. As stated earlier, many families complete and submit their FAFSA before they file their tax returns, thereby leaving the IRS with no up-to-date information available for matching or pre-populating a FAFSA.

The Department continues to explore with the IRS a framework for data matching. However there are technological challenges that must be resolved before a comprehensive system for pre-population could be established. It should be noted that, under the current criteria, using only IRS data to pre-populate the FAFSA, a student and family would still be required to provide additional information, as the IRS does not maintain all necessary data. Additionally, as noted above, the Department is looking into how a simplified approach with a focus on data pre-population could be implemented in the future.

While the Department’s sample FAFSA would ask fewer questions, and many of those answers could be obtained through the IRS, some questions are not part of the IRS process and will require the applicant’s responses. However, given what would be a significant reduction in the number of questions on a simplified FAFSA, this should pose little burden to the student.

VI. How the use of income data from two years prior to a student’s planned enrollment date will change the EFC computed in accordance with Part F of Title IV, and the potential adjustments to the need analysis formula, if any, that would minimize these changes.

To respond fully to this issue, the Department needs to conduct additional data analysis. However, it is likely, based on preliminary observations, that using “prior-prior” income data (as explained on page 3 of this report) would not significantly impact a targeted set of FAFSA filers, such as dependent students from low-income families. It is not clear, however, how the use of “prior-prior” year information would affect the eligibility of other groups of students, particularly single, independent students.

As noted, policymakers would have a wide range of options for determining how to establish the criteria for eligibility. Modeling of different alternatives, including the use of “prior-prior” year data, as opposed to prior year data, would provide policymakers with valuable information to help determine if, when, and for whom the use of “prior-prior” year income data would be appropriate.

VII. The extent to which the data elements collected on the FAFSA on March 31, 2008 that are needed to determine eligibility for student aid or to administer the federal student aid programs, but are not needed to compute an EFC, can be reduced without adverse effects.

As noted above, the sample FAFSA form would address this question directly. The only questions on the envisioned simplified application would be those that are specifically related to determining that the student is an eligible student (e.g. citizenship, high school graduation information) and those that are needed to determine the types and amounts of federal aid the student will be eligible to receive. For example, the alternative application presented by the Department in this report includes fewer than 30 questions.

Additional Policy Discussion

As this and other simplification proposals are discussed, there are additional issues to consider as follows:

Exclusion of Untaxed Income – The current need analysis formula, while including some sources of untaxed income, excludes others. For example, child support received by a single parent is currently counted as untaxed income, while veteran’s educational benefits and welfare benefits are not. In fact, Congress has recently eliminated several untaxed income items, including income tax credits and certain social security benefits, from the formula via the College Cost Reduction and Access Act (CCRAA). The Department’s simplified approach further reduces the categories of untaxed income that are included in the needs analysis formula.

Exclusion of Assets – Federal student aid applicants (and their parents) report the net value of their assets on the FAFSA. Applicants are instructed to report asset values that represent market values as of the day they file the FAFSA. Based on Department data, more than 90 percent of current Pell grant recipients would be unaffected by the removal of assets from the EFC formula and, thus, from the form. Within the EFC calculation, however, all asset classes are not treated equally. The asset questions on the current FAFSA ask about liquid assets (cash and checking and savings accounts, which likely will not be available for the student’s educational expenses months later), as well as the values of stocks, bonds, other investments, retirement accounts, and real estate equity (excluding the family home). While the net worth of farms and businesses may be considered, most of this asset class is not included because of a set of complex statutory exclusions. Additionally, the formula uses a complex calculation to determine what portion of all other assets is available to pay postsecondary education expenses. For example, the formula includes “protections” based on age and marital status. Finally, because date-specific asset values are largely unverifiable, the reporting or non-reporting of assets is a principal area of the EFC calculation subject to mis-reporting or abuse.

Since assets do not significantly impact the Pell grant eligible population, and the use of untaxed income distorts income distinctions, an option using two verifiable income elements – AGI and IRS tax exemptions – to determine student aid eligibility meets the earlier-stated goals and principles of simplification. In addition to dramatically simplifying the student aid process and significantly reducing burden on families and institutions, using only these two income data elements will result in eligibility determinations for federal student aid that are predictable and verifiable and will better target aid.

Conclusion

The Department's analysis indicates that reducing the income data on the FAFSA to AGI and IRS exemptions would not significantly impact the eligibility of low-income students. The combination of using less information with a different eligibility formula provides the opportunity to improve the information provided to students and families regarding their application for federal student aid. Instead of informing them of what they are expected to pay, the simplified application process would allow the federal government to immediately (in real-time for on-line filers) inform students of the types and amounts of federal student aid the student is eligible to receive.

We are hopeful that, with this specific information in hand, students and families would be able to work together with their States, institutions, and private groups to put together a financing package to better meet the challenges of paying for college.

We know that 40 percent of college students, nearly eight million, never even apply for federal aid, even though most of them would be eligible for assistance. The reduction in required data discussed in this report will significantly reduce the burden now experienced by students and families in completing the FAFSA. Simplification is not just about changing the FAFSA form; it is also about creating a new eligibility calculation that is simpler, understandable, and more easily verifiable. This cannot be accomplished without changes to current law.

These suggested changes, along with the flexibilities provided to policymakers, could achieve the objectives many interested parties seek.