

## Testimony: Net Price Calculators and Financial Aid Award Letters

The panelists have been asked to answer four questions about net price calculators and financial aid award letters. I will address each of these questions one at a time.

### 1. What data do students and parents need about college expenses and financial aid, and when?

- In middle school?
- During the college search process and before applying for admission?
- After admission to one or more colleges?

Students and their families need clear, accurate and complete information about college costs, financial aid and the bottom-line cost of education to help them make *informed decisions* about affordability. The information should permit a meaningful and consistent apples-to-apples comparison of costs among different colleges. Such comparisons should be based on a true bottom-line cost of education, such as the out-of-pocket cost.

The out-of-pocket cost is defined as the difference between the total cost of attendance and total gift aid. Gift aid includes grants, scholarships, tuition waivers and housing waivers, but not loans or student employment. The out-of-pocket cost measures the amount of money the family must pay or borrow to cover college costs.

Families also need information about policies that can affect the calculation of the out-of-pocket cost, such as the college's policies concerning displacement of outside scholarships and whether the college practices front-loading of grants.

The information about college costs should be complete, including all direct and indirect costs. Allowances for various discretionary cost components, such as textbooks, transportation and housing, should be realistic and based on actual average costs for similarly situated students.

The information about financial aid should provide clarity concerning the types, amounts and sources of financial aid awards. The type of each award should be clearly identified, distinguishing between grants, scholarships, student employment, education loans and tuition installment plans.

In addition to a snapshot of current one-year costs and financial aid, families need estimates of the *entire* cost of the educational program from start to finish. They need to understand the amount or percentage by which the college cost components and the financial aid awards will change with each subsequent year of enrollment. They need to know the total out-of-pocket costs from matriculation to graduation. They need projections of cumulative debt at graduation, including estimates of the monthly loan payments and the total payments over the life of the loans.

This information should be made available to families at key decision points, such as

- during the college search process and the initial selection of colleges, before the student applies for admission; and
- during the final choice of a college after the student has been accepted by the colleges.

Providing families with this information may influence their behavior. Affordability is not the only reason to choose a college, but it is an important criterion that affects access, choice, retention and completion. It also affects the amount of debt at graduation and whether the student graduates with excessive debt.

Confusion about affordability and the real cost of college leads to some students dropping out of college or graduating with unaffordable amounts of debt.

Middle-school students, on the other hand, do not need precise information about college costs. Instead, they need general information about affordability and the availability of need-based student aid, especially gift aid. The goal of early awareness efforts should focus on demonstrating that college is a possibility, so that students pursue more challenging high school courses and obtain adequate preparation for a college education. This will improve the flow of qualified students from high school to college.

**2. What lessons can be drawn from the history and current status of financial aid award letters?**

- In practice, do financial aid award letters meet the needs of students and parents?
- If not, what are the major shortcomings -- from a student and parent perspective?
- What improvements can be made and are these improvements likely to be made?

Current standards for financial aid award letters are implemented as recommended best practices. These voluntary standards have not adequately addressed the needs of students and their families, despite existing for more than a decade.

In a December 2010 survey conducted by Fastweb, 84% of college freshmen and their parents said that financial aid award letters should be standardized to make them easier to understand and to compare. More than half (51%) said that it was difficult to compare financial aid award letters of different colleges.

There are numerous flaws in current financial aid award letters from a student and parent perspective:

- Cost information in current financial aid award letters is often incomplete or absent. Even when a financial aid award letter includes some cost-of-attendance information, the cost information may be limited to just tuition or fail to provide a detailed breakdown. It is often unclear what costs are included in the cost of attendance and what costs are not. Variable costs that are under a family's discretionary control – such as textbook costs, travel and transportation costs, personal expenses and off-campus housing costs – are often significantly underestimated.
- Families sometimes misinterpret the expected family contribution (EFC) as a limit on their portion of college costs. Actual costs are often higher due to unmet need and the inclusion of loans in the need-based financial aid package.
- Many financial aid award letters lack a clear distinction between loans (which must be repaid) and gift aid (which does not need to be repaid). The different types of aid are often mixed together, contributing to confusion over the differences. Many financial aid award letters use an alphabet soup of cryptic acronyms and abbreviations for loans and grants. It is hard for families to tell what is a loan and what is a grant. Many financial aid award letters treat loans as though they cut college costs. Most families do not consider loans to be financial aid.
- Loans often mask the existence of unmet need. While practices such as packaging PLUS may have valid public policy justifications (e.g., to increase awareness of lower-cost federal education loans), a lack of clarity concerning the nature of the loan sometimes confuses families into believing that the PLUS loan is a grant and that they are getting a free ride.
- The most important information about loans, such as interest rates, monthly payments and total payments, is often omitted or buried in an appendix.
- Loans are often listed according to artificial distinctions, such as the source of the loan or whether eligibility is based on financial need, and not according to the cost per dollar borrowed.

- Most financial aid award letters do not include information about the student's current cumulative education debt (including both principal and interest) and the corresponding monthly loan payments and total loan payments. Similarly, most financial aid award letters do not include a projection of cumulative debt at graduation and the corresponding monthly loan payments and total loan payments.
- There are no standards concerning the formatting, organization and content of financial aid award letters, such as what information should be prominently displayed on the first page of a financial aid award letter. This forces families to hunt for the information they need (and use calculations to derive some of the most important information) instead of being able to compare financial aid award letters from different colleges side-by-side and line-by-line.
- Very few financial aid award letters report a true bottom-line cost, such as the out-of-pocket cost (which is defined as the difference between the total cost of attendance and total gift aid). Instead, some financial aid award letters report a net cost, which is defined as the difference between the cost of attendance and all need-based student aid. This treats loans as though they reduce the family's costs. Most financial aid award letters report neither a net cost nor an out-of-pocket cost figure.

These problems persist unabated despite the existing voluntary standards and are likely to get worse as college budgets get squeezed. There are fundamental conflicts between a college's pecuniary interests and the best interests of students and their families, regardless of whether the college is public, non-profit or for-profit. College financial aid policies are often driven by a need to minimize the discount rate.

These problems can be addressed by adopting a *mandatory* standard for financial aid award letters and net price calculators. The ability to compare financial aid award letters and net prices of different colleges depends on universal adoption of the same standard by all colleges. Otherwise such comparisons will not be made on an apples-to-apples basis and the cost differences will not be meaningful.

I have prepared a 37-page proposal for standardizing financial aid award letters and net price calculators. The proposal includes 39 optional and 59 mandatory standards that address all of the problems discussed in this testimony. I have shared a copy of the report and a four-page summary with the Advisory Committee on Student Financial Assistance (ACSFA). I will distribute copies to the financial aid community and the general public via the FinAid.org web site. It is my hope that the report will stimulate discussion about standardizing financial aid award letters and ultimately lead to a mandatory standard. In the meantime, colleges may use the report as a road map toward improving their financial aid award letters and net price calculators.

### **3. Will net price calculators provide students and parents the data needed to make informed decisions?**

- How do net price calculators relate to financial aid award letters - in content and form?
- Will net price calculators likely suffer from the same shortcomings as do financial aid award letters?
- Are net price calculators likely to suffer from additional (unique) shortcomings?

Net price calculators are likely to suffer from the same problems as financial aid award letters because there are no existing mandatory standards for net price calculators, other than the definition of net price, and even that definition has problems.

While the Higher Education Opportunity Act of 2008 defined cost of attendance as the average annual cost of tuition and fees, room and board, books, supplies and transportation for first-time, full-time undergraduate students, it did not specify which year would apply. Net price calculators are often used in the fall, before colleges have set the tuition rates and student aid budget for the next year. It is unclear

whether a college should use the previous year's costs, the current year's costs or a projection of next year's costs, or when or how frequently the calculator should be updated. The lack of a standard for this aspect of net price calculators will limit their accuracy and usefulness in estimating the actual cost to the family and comparing costs among different colleges.

Families must currently search for net price calculators on each college's web site, as there is no centralized repository of net price calculators. Families must reenter their financial information on each college's calculator. User interfaces and output formats are not standardized.

The accuracy and precision of the net price calculations may vary considerably from student to student and college to college. Some colleges may use net price calculators that are not customized to the individual family circumstances, leading to a lack of comparability. The net price calculations might not correlate well with the college's packaging philosophy, resulting in net price figures that fail to correspond to the college's own financial aid award letters. There is no third party monitoring of the accuracy of the net price estimates.

**4. To what extent can financial aid award letters and net price calculators be standardized and integrated?**

- In practice, how closely related are net price calculators and financial aid award letters likely to be?
- What steps might be taken to ensure that these two tools are standardized and integrated?
- Who should take the lead in doing so and how should that process proceed?

Net price calculators and financial aid award letters should use the same standards as much as possible. The content and form of the results of a net price calculator should match and be predictive of the final financial aid award letter and the actual cost to the family as much as possible to help families make informed decisions concerning college selection and choice. These standards must be mandatory to ensure a consistent universal basis for comparing financial aid award letters and net price calculations from different colleges.

My 37-page report demonstrates that financial aid award letters and net price calculators can be standardized by providing a detailed proposal for such a standard. The report also includes a mockup of the first page of a standardized financial aid award letter that incorporates many aspects of the proposal.

Congress and the US Department of Education should take the lead in standardizing financial aid award letters and net price calculators. Section 484 of the Higher Education Opportunity Act of 2008 (P.L. 110-315, August 14, 2008) requires the US Department of Education to "convene a group of students, families of students, secondary school guidance counselors, representatives of institutions of higher education (including financial aid administrators, registrars and business officers), and nonprofit consumer groups" for the purpose of recommending improvements to "financial aid offer forms" within six months of enactment. The legislation also requires the US Department of Education to develop a standardized financial aid offer form and to provide recommendations to the House and Senate education committees within one year of enactment. The legislation also requires the US Department of Education to make the recommendations and standardized financial aid offer form widely available.

This seems like a good process for standardizing financial aid award letters. Unfortunately, none of these requirements have been completed more than two years after enactment. The US Department of Education should begin work on this Congressional requirement as soon as possible. Hopefully today's hearing will help jump start this process. My only suggestion for improving this process would be to incorporate a public comment period into the process before the US Department of Education reports to the House and Senate education committees.

**MODEL FINANCIAL AID AWARD LETTER (FIRST PAGE)**



**College of Blue Belle**  
 PO Box 2056  
 Cranberry Twp, PA 16066

Enrollment Status: Full-Time  
 Housing Status: On Campus  
 Period: Academic Year 2011-12  
 Today's Date: 3/17/2011

1-724-538-4500  
 1-724-538-4502 fax  
[www.peterbaldcattery.com](http://www.peterbaldcattery.com)

Cost of Attendance	\$23,450
Total Gift Aid	- \$13,300
<b>Out-of-Pocket Cost</b>	<b>\$10,150</b>

Gift Aid/Cost Ratio	57%
Gift Aid/Need Ratio	57%

Cost of Attendance	\$23,450
Federal EFC	\$0
Financial Need	\$23,450

	Fall Term	Spring Term	Full Year Total	Average Annual Increase
<b>Cost of Attendance</b>				
<b>Required Expenses</b>				
Tuition and Required Fees	\$5,000.00	\$5,000.00	\$10,000.00	5.6%
Room and Board	\$4,225.00	\$4,225.00	\$8,450.00	6.0%
Books and Supplies (Average)	<u>\$500.00</u>	<u>\$500.00</u>	<u>\$1,000.00</u>	6.9%
<b>Subtotal Required Expenses</b>	<b>\$9,725.00</b>	<b>\$9,725.00</b>	<b>\$19,450.00</b>	<b>5.8%</b>
<b>Discretionary Expenses</b>				
Travel and Transportation (Estimate)	\$750.00	\$750.00	\$1,500.00	3.2%
Health Insurance	\$500.00	\$500.00	\$1,000.00	13.1%
Miscellaneous / Personal (Estimate)	<u>\$750.00</u>	<u>\$750.00</u>	<u>\$1,500.00</u>	2.1%
<b>Subtotal Discretionary Expenses</b>	<b>\$2,000.00</b>	<b>\$2,000.00</b>	<b>\$4,000.00</b>	<b>5.1%</b>
<b>TOTAL COST OF ATTENDANCE</b>	<b>\$11,725.00</b>	<b>\$11,725.00</b>	<b>\$23,450.00</b>	<b>5.5%</b>

Gift Aid (Grants and Scholarships)	Source	Fall Term	Spring Term	Full Year Total	Average Annual Increase
Federal Pell Grant	Federal	\$2,775.00	\$2,775.00	\$5,550.00	0.8%
State Grant	State	\$125.00	\$125.00	\$250.00	-1.0%
University Merit Scholarship	College	\$2,500.00	\$2,500.00	\$5,000.00	0.0%
Private Scholarship	Private	<u>\$1,250.00</u>	<u>\$1,250.00</u>	<u>\$2,500.00</u>	0.0%
<b>TOTAL GIFT AID</b>		<b>\$6,650.00</b>	<b>\$6,650.00</b>	<b>\$13,300.00</b>	<b>0.3%</b>

**OUT-OF-POCKET COST** **\$5,075.00** **\$5,075.00** **\$10,150.00**

Options for Paying for Out-of-Pocket Cost	Rate	Fees	Duration	Full Year Total/Limit	Monthly Payment	Total Payments
<b>Student Employment</b>			10 hours/week			
Federal Work-Study	\$8.50/hour		for 30 weeks	\$2,550.00		
<b>Payment Plans</b>						
Tuition Installment Plan	\$1,128/month	\$100	9 months	\$10,250.00		
<b>Education Loans (Need-Based)</b>						
Perkins Loan	5.0%	0%	10 years	\$2,100.00	\$40.00	\$2,374.81
Subsidized Stafford Loan	3.4%	1%	10 years	\$5,500.00	\$55.17	\$6,620.94
<b>Education Loans (Non-Need)</b>						
Unsubsidized Stafford Loan	6.8%	1%	10 years	\$5,500.00	\$64.51	\$7,742.01
Parent PLUS Loan	7.9%	4%	10 years	\$10,150.00	\$127.72	\$15,326.52
Private Student Loan	10.0%	3%	15 years	\$10,150.00	\$112.45	\$20,239.26