

The Need for Standardized and Required Disclosures Concerning College Costs and Financial Aid

*Testimony Presented at the U.S. Department of Education Public Meeting on
Recommendations for Improvement of Student Financial Aid Offer Forms
and Development of Model Financial Aid Offer Forms*

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Thank you for inviting me to discuss and offer recommendations for improvements in student financial aid offer forms, more commonly known as financial aid award letters, and the development of a model financial aid award letter.

My name is Mark Kantrowitz. I am publisher of Fastweb and FinAid, the most popular web sites about planning and paying for college. Fastweb is a free scholarship matching service and FinAid is a free encyclopedic guide to student financial aid information, advice and tools. More than 50 million students and parents have used Fastweb's services over the last 16 years, with 9 million currently active users of the site. My role is focused on content development and thought leadership. I try to act as a catalyst for positive change affecting student financial aid and higher education, with a special emphasis on improvements in access, choice, retention and completion.

PROBLEMS WITH CURRENT FINANCIAL AID AWARD LETTERS

Financial aid award letters should be focused primarily on the needs of students and their families. Students and their families need and want clear, correct, complete and comparable college cost and financial aid disclosures. Financial aid award letters do not currently satisfy these needs.

Paying for a college education is one of the few major life cycle expenses without standardized statutory disclosures concerning costs and discounts. Cost disclosures are required for automobiles, real estate, credit cards, mortgages, retirement plans, investments and private student loans. These disclosure requirements were established by federal and state laws, not by voluntary industry best practices. For example, the Monroney Window Sticker was established by the Automobile Information Disclosure Act of 1958, the Schumer Box for credit cards was established by the Truth in Lending Act of 1968 (TILA), the Good Faith Estimate and HUD-1 settlement statements were established by the Real Estate Settlement Procedures Act of 1974 (RESPA), interest and fee disclosures were established by the Truth in Savings Act of 1991, retirement plan and pension disclosures were established by the Employee Retirement Income Security Act of 1974 (ERISA) and the Seller's Property Disclosure Statement was established by various state real estate disclosure acts. Private student loan disclosure requirements were recently added to the Truth in Lending Act of 1968 by the Higher Education Opportunity Act of 2008.

Voluntary best practices are inadequate. Problems with financial aid award letters have persisted despite publication of an Award Letter Evaluation Tool by NASFAA in 2001 as a voluntary set of best practices.

Additional attention was drawn to the issue in 2007 through an op-ed in Inside Higher Ed in June 2007,¹ the creation of the FinancialAidLetter.com web site in June 2007 and a report published by Consumers Union in July 2007.² The 2007 NACAC Counseling Trends Survey also reported that approximately 61% of high school guidance counselors wanted more tools for helping families interpret and better understand financial aid award letters, a greater percentage than for any other resource. These efforts culminated in the inclusion of section 484 in the Higher Education Opportunity Act of 2008 (P.L. 110-315), which requires the U.S. Department of Education to make recommendations concerning financial aid award letters and to produce a model financial aid award letter.

In November and December 2010 Fastweb conducted a survey of 391,892 college freshmen and sophomores and 187,669 parents of college freshmen and sophomores concerning financial aid award letters. The results are statistically significant with a 7.17% confidence interval at the 95% confidence level. The survey found a variety of serious problems with financial aid award letters:

- Many financial aid award letters have missing or unrealistic cost of attendance figures. Nearly a third (29%) of award letters omit the cost of attendance entirely. Of those that do provide a cost of attendance figure, almost three fifths (58%) do not provide a detailed breakdown of costs. Almost three quarters (73%) of families feel that transportation allowances are unrealistic. More than three fifths (62%) feel that allowances for books and supplies are unrealistic.
- Almost seven eighths (84%) of students and parents feel that financial aid award letters should be standardized to make them easier to understand and compare. Half (51%) feel that it is difficult to compare financial aid award letters from different colleges.
- Most financial aid award letters lack a figure for the bottom line cost of college. More than half (55%) of the financial aid award letters do not mention a net cost figure and nearly two-thirds (64%) of the financial aid award letters do not mention an out-of-pocket cost. The net cost is the difference between the total cost of attendance and the financial aid package. The out-of-pocket cost is the difference between the total cost of attendance and just gift aid. Gift aid is money that does not need to be repaid, such as grants, scholarships, tuition waivers and housing waivers.
- Students and parents reported that financial aid award letters included misleading information about financial aid. A fifth (21%) said that the award letter did not distinguish between grants and loans. A fifth (21%) said the award letter used Parent PLUS loans to meet financial need, masking unmet need.
- Three fifths (61%) of students and parents said the financial aid award letter did not include basic information about loan terms other than loan amounts. Less than a third (29%) of financial aid award letters mentioned interest rates, a fifth (21%) mentioned the loan term in years, 14% mentioned the total loan payments, 13% mentioned the monthly loan payment and 12% mentioned the total interest paid.

The most problematic of these practices understate the college costs, overstate the generosity of the financial aid package and obscure or misrepresent the true bottom-line cost of college. Cost of attendance information is often incomplete or absent. Many colleges report just tuition and other direct costs that are billed by the college, omitting information about indirect costs.³ Allowances for books & supplies,

¹ Mark Kantrowitz, *Standardize Financial Aid Award Letters*, Inside Higher Ed, June 22, 2007.
www.insidehighered.com/views/2007/06/22/kantrowitz

² Consumers Union, *Helping Families Finance College: Improved Student Loan Disclosures and Counseling*, July 2007.
www.consumersunion.org/pdf/CU-College.pdf

³ Some colleges report only tuition, not tuition and fees, because increases in tuition are lower than increases in tuition and fees.

transportation and personal expenses are often underestimated. Financial aid award letters include misleading information about the amount, type and source of financial aid and use cryptic terminology to describe awards. Financial aid award letters do not clearly distinguish loans from grants and often characterize loans as reducing the bottom-line cost. For example, a March 2011 article in the New York Times included an excerpt from an actual college financial aid award letter which stated “*Your parents may further reduce 2011-12 educational expenses by applying for the Parent Loan for Undergraduate Students (PLUS).*”⁴ Such misrepresentations are widespread. Loans do not reduce college costs. They often increase costs by charging interest.

Many current financial aid award letters may violate state plain language and false advertising statutes. They may also violate the new federal substantial misrepresentation regulations concerning the nature of an institution's financial charges.⁵

Similar problems are prevalent among net price calculators despite the goal of helping students and their families understand bottom-line college costs. Some colleges confuse families as to the true cost of college by highlighting a net cost figure and de-emphasizing the net price figure. Net price calculators also create new problems. Net price calculators are used in the fall before colleges set the next year's costs and financial aid budget, making them less predictive of future college costs. There is also a tradeoff between the accuracy and simplicity of a net price calculator. As a result, the net price calculator may yield results that are much different than the final financial aid award letter or actual college costs. At best, net price calculators offer a ballpark estimate that is unreliable for precise comparisons of different colleges. Net price calculators may be suitable for determining whether a college's costs are inside or outside the ballpark, but not for distinguishing between center field and home plate.

These persistent problems, despite the existence of a *voluntary* set of best practices, demonstrate the need for a *mandatory* standard for financial aid award letters. The design of cost and financial aid disclosures must be focused primarily on what's in the consumer's best interests. The needs of students and their families must come first.

The lack of clear and accurate information causes consumer confusion about affordability and the real cost of college. This leads some students to decide against enrolling in college, some students to drop out of college when they run out of money and other students to graduate with unaffordable amounts of debt. Affordability is not the only reason to choose a college, but it is an important criterion that affects access, choice, retention and completion. Making financial aid award letters more accurate and easier to understand might improve access and completion at minimal cost to the taxpayer. Making financial aid award letters easier to compare might also help drive down college costs through increased competition.

RECOMMENDATIONS FOR STANDARDIZING FINANCIAL AID AWARD LETTERS

Some of the following recommendations for standardizing financial aid award letters are based on my testimony on the same topic during a hearing of the Advisory Committee on Student Financial Assistance in March 2011. That report proposed a detailed set of 39 optional and 59 mandatory standards for financial aid award letters.⁶ These recommendations are easy to implement, mostly requiring a minimal retooling of financial aid award letter templates in administrative software systems. These recommendations have been implemented in award letter analysis and comparison tools available on the FinAid web site.⁷

⁴ Ron Lieber, *Balancing Debt Against College Choice*, New York Times, March 23, 2011. www.nytimes.com/2011/03/24/your-money/24TEENS.html

⁵ 34 CFR 668.71 and 34 CFR 668.73.

⁶ Mark Kantrowitz, *Proposal for Standardization of Financial Aid Award Letters and Net Price Calculators*, March 17, 2011. www.finaid.org/educators/20110317awardletters.pdf

⁷ www.finaid.org/calculators/awardletter.phtml and www.finaid.org/calculators/awardletteradvanced.phtml

An updated version of the model financial aid award letter from this report is appended to this testimony.

The following recommendations fall into several broad categories, all intended to enable students and their families to make informed decisions about college affordability.

- **Definitions**
- **Content**
- **Accuracy and Clarity**
- **Comparability**
- **Format and Organization**
- **Analysis and Interpretation**
- **Timing**
- **Consumer Input**

Definitions

The standard for financial aid award letters should establish unambiguous uniform definitions for many of the terms used in financial aid award letters. It should also specify standards for calculating the values of items that are listed in the financial aid award letter.

For example, some of the definitions related to the bottom line cost of college do not really measure the true cost of college. The *out-of-pocket cost* is a good definition of the bottom line cost of college, the amount of money that the family must earn, save or borrow to cover college costs. It is the difference between the total cost of attendance and total gift aid. This is in contrast with the *net cost*, which focuses on cash flow. The net cost is the difference between the cost of attendance and the financial aid package, which usually includes student employment and loans in addition to gift aid. The net cost is a marketing concept, designed to convince families that they can afford the college even when they can't. It is not a true measure of how much college will really cost since it treats loans as though they reduce the family's costs.

Financial Need = Cost of Attendance – EFC

Financial Aid = Gift Aid + Self-Help Aid

Gift Aid = Grants, Scholarships, Tuition Waivers and other awards of money that do not need to be repaid

Self-Help Aid = Loans and Student Employment

Loans = Money that must be repaid, usually with interest

Unmet Need = Financial Need – Financial Aid

Net Cost = Cost of Attendance – Financial Aid

Out-of-Pocket Cost = Cost of Attendance – Gift Aid

Content: Cost and Financial Aid Information

The standard for financial aid award letters should specify what items should be included in a financial aid award letter. At minimum, a financial aid award letter should include the total cost of attendance, total gift aid, total self-help aid and important derived values⁸ such as the out-of-pocket cost.

The total cost of attendance should include all direct and indirect costs, regardless of whether they are billed by the college or incidental. The financial aid award letter should also include a breakdown of the cost of attendance into the major cost components, such as tuition and required fees, room and board, books and supplies, transportation and personal expenses.

⁸ Derived values are calculated based on other values. For example, the out-of-pocket cost is the difference between the total cost of attendance and total gift aid. The most important derived values analyze and rate aspects of affordability, such as the bottom line cost of college or the total cost of an education loan.

Gift aid should be discussed within the context of a college cost disclosure because it functions as a discount that affects the bottom line cost of college.

The financial aid award letter should include all of the individual financial aid awards available to the student and classify them according to type.

Accuracy and Clarity

The standard for financial aid award letters should require the financial aid award letter to disclose clear and correct information about college costs and financial aid, to minimize the potential for consumer confusion. Financial aid award letters should also be complete, so that all relevant and important information is included.⁹ Omitting all or some cost information and presenting inaccurate estimates of cost allowances makes it more difficult for families to evaluate a college's affordability.

Financial aid award letters sometimes include *estimates* of tuition and fees instead of *actual* figures. The actual charges that appear on the bursar's bill in late summer may be much different. This problem is more prevalent at public colleges and universities. This makes it more difficult for students and families to compare and evaluate college costs.

Cost allowances for other items should be based on recent actual average costs for similarly-situated students, updated frequently to ensure that the amounts accurately reflect the actual costs students will experience.

Award letters should provide clarity concerning the types, amounts and sources of financial aid. Financial aid award letters should clearly distinguish between the various types of financial aid, especially grants and loans. Loans should never be characterized as reducing college costs, since they have to be repaid, usually with interest. Loans are not a form of gift aid.

Financial aid award letters should emphasize that cost figures are for only one year, not the student's entire educational program. Ideally, financial aid award letters should include information about how costs and financial aid will change from one year to the next, to help families plan for future college costs.

Comparability

Financial aid award letters should provide a standardized disclosure of costs and financial aid so that families can comparison shop. Accordingly, financial aid award letters should be comparable, allowing students and families to make meaningful and consistent apples-to-apples comparison of costs among different colleges. This requires standardization of the organization and format of the financial aid award letter in addition to standardization of the content of the financial aid award letter.

Analysis and Interpretation: The Bottom Line Cost

The financial aid award letter should include items that evaluate and summarize the overall financial impact on the family, such as an analysis of the bottom-line cost of college.

Financial aid award letters should prominently disclose the bottom-line cost. The out-of-pocket cost, which subtracts grants, scholarships and other forms of gift aid from the total cost of attendance, is a good measure of the true bottom-line cost of education. The out-of-pocket cost is the amount of money that the family must earn, save or borrow to cover college costs.

Colleges should be required to disclose any significant or relevant facts that might affect the family's decision concerning enrollment. In particular, financial aid award letters should disclose specific policies

⁹ Material information is important information that is relevant to the cost of college.

that affect the out-of-pocket cost, such as policies on front-loading of grants and the treatment of outside scholarships. They should also disclose policies that significantly affect college costs and eligibility for financial aid, such as policies concerning satisfactory academic progress (SAP), differential tuition, refunds, professional judgment, dependency overrides, enrollment status and gainful employment.

Front-loading of grants makes a college appear to be more generous than it really is by providing a much lower out-of-pocket cost during the first year and possibly replacing grants with loans or work in subsequent years. While one could argue that front-loading of grants is good public policy because it reduces the debt of students who drop out and are most likely to default, such a result could also be obtained by modifying institutional refund policies to minimize the debt of students who drop out. Students and families need to know how costs and financial aid will change in subsequent years.

Each college has a different policy concerning the treatment of outside scholarships the student may win. This can affect the bottom line cost for a student who has won significant amounts of private scholarship money. These students need to know how much of the outside scholarships will reduce unmet need, how much will reduce the loan and work burden, and how much will reduce gift aid. Reductions in unmet need, loans and student employment have a more favorable impact on the out-of-pocket cost than reductions in gift aid.

Student Loans

Financial aid award letters can encourage students and families to reduce borrowing by providing clear information concerning student loans and the cost of borrowing. This will increase awareness of debt. Financial aid award letters should include more than just the loan amount near the name of the loan, but also the interest rates, monthly loan payments and total payments assuming a 10-year repayment term.

Financial aid award letters should include information about a student's cumulative education debt, including principal and interest. Financial aid award letters should include a projection of education debt at graduation and the corresponding monthly loan payments and the total of the monthly loan payments.

Student Employment

Financial aid award letters should provide realistic information about student employment. Are there enough jobs available for all the students awarded work-study funding? How likely is the student to be able to earn the full amount of a work-study award? How easy is it to find a job on campus? How many hours of work will be required to earn the full award amount? Will the work-study job be related to the student's major, or will it involve serving food to wealthier students in the college's cafeteria?

Format and Organization

Families are less likely to read longer financial aid award letters, but shorter financial aid award letters may be more confusing. Accordingly, it is important to streamline the first page of the financial aid award letter by prioritizing what information appears first and by minimizing extraneous verbiage and jargon. Tables may help increase the clarity and density of information.

The standard for financial aid award letters should specify that the most important information – such as the cost of attendance, gift aid and out-of-pocket cost – should be displayed prominently on the first page of the financial aid award letter. The first page of the financial aid award letter should also provide the expected family contribution (EFC) and financial need.

The organization and formatting of the first page of the financial aid award letter should permit a side-by-side or even line-by-line comparison of financial aid award letters from different colleges and universities.

The individual financial aid awards should be grouped separately according to type of aid to avoid confusion. Gift aid should be listed first and be separated from other types of financial aid by the calculation of the out-of-pocket cost.

The standard for financial aid award letters should be flexible enough to address the needs of various types of students, such as

- Dependent Students vs. Independent Students or Traditional vs. Non-Traditional Students¹⁰
- On-Campus vs. Off-Campus Housing
- Full-Time Enrollment vs. Part-Time Enrollment
- First-Time Students vs. Transfer Students

Most colleges use a single format for financial aid award letters for all the different types of students, albeit with different figures for each item, so it should be possible to develop a single standard template that addresses the needs of all students and their families. After all, all students need clear, accurate and complete information about college costs and financial aid. Likewise, differences in institutional resources and packaging philosophies should not prevent the development of a single set of standards for financial aid award letters.

Timing

The standard for financial aid award letters should address the timing of the receipt of financial aid award letters and the deadlines, if any, for responding to the financial aid award letter.

Currently, most new students must accept offers of admission by the May 1 National Candidate's Reply Date. Some students receive financial aid award letters too close to this deadline. Financial aid award letters should be received by students at least two weeks in advance of the May 1 deadline (and preferably a month in advance) to provide adequate time for the students to compare and evaluate financial aid awards and to decide where to enroll.

Get Student and Parent Input

The needs of students and their families should be the primary purpose and impetus for the development of a standardized financial aid award letter. Accordingly, the U.S. Department of Education should proactively solicit input from students and parents, not just college staff and public policy advocates.

The draft standard financial aid award letter should be designed and tested with focus groups and panels of consumers, including high school students, college students, parents and high school guidance counselors, as well as representatives of colleges and universities, similar to the processes used for private student loan disclosures and the FAFSA.

The U.S. Department of Education should solicit comments from students and their families, perhaps using the Facebook social comment plugin,¹¹ by posting a draft standard online and by sending email to a subset of FAFSA filers.

¹⁰ The term "non-traditional student" does not have the same meaning as "independent student." Non-traditional students may include first-generation college students, underrepresented minority students, older adult students, reentry students, students retraining in a new field, high school dropouts, orphans, foster care students, wards of the court, students with dependents, home-schooled students, part-time students, disabled students, international students, transfer students, working students, veterans, foster children, children of divorced parents, students abandoned by their parents and other types of at-risk students needing special assistance.

¹¹ <http://developers.facebook.com/docs/reference/plugins/comments/>

