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SAVING FOR COLLEGE 101:
HOW YOUR SAVINGS CAN AFFECT FINANCIAL AID

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HOW YOUR SAVINGS CAN AFFECT FINANCIAL AID

If you're like many parents, you may be wondering whether saving too much for college will decrease your child's chances of receiving need-based federal financial aid.

THE EFC CALCULATION

A critical component of the Free Application for Federal Student Aid (FASFA) is the Expected Family Contribution (EFC). The EFC, or amount you are expected to contribute toward your child's education costs, is calculated by factoring in the following financial resources:

- 20% of the student's assets, such as money, investments, business interests and real estate
- 50% of the student's income (after certain allowances)
- 2.6 - 5.6% of the parents' assets, such as money, investments, business interests, and real estate, based on a sliding income scale (after certain allowances)
- 22 - 47% of the parents' income, based on a sliding income scale (after certain allowances)

YOUR ASSETS AND THE EFC

Let's examine how specific types of assets affect the EFC formula.

Retirement Accounts

Retirement acounts, such as IRAs and 401(k)s, whether yours or your child's, are not counted at all in determining the EFC for federal financial aid. Be careful, however, about taking money out of your IRA (or any retirement account) to pay for college.

Though the tax law permits penalty-free withdrawals from a traditional or Roth IRA to pay for qualified college costs, doing so could jeopardize financial aid in the following year. The entire withdrawal, including principal and earnings, counts as income on the following year's aid application.

Different Types of Equity

The equity in your primary home, a family-owned business, insurance policies, and annuities is also excluded from your assets when determining the EFC.

Student Assets

Assets that belong to the student result in a greater reduction in financial aid. UGMA and UTMA accounts are counted as student assets. In addition, they may increase the student's income tax return. Often, the income tax benefit of setting aside investment assets in a child's name is offset by the reduction in the child's financial aid package.

529 Plans & Coverdell Educational Savings Accounts (ESAs)

These vehicles may be two of the better options to save for college without jeopardizing financial aid. They offer special advantages when it comes to aid eligibility.

- If a parent owns the 529 account or ESA, up to 5.6% of the value is included in the EFC as a parent asset.
- If a grandparent owns the account, none of the value is included. Distributions made from grandparent-owned 529 plans, however, will be considered untaxed income to the student for purposes of the following year's FASFA asset reporting. This means that 50% of the value of the distribution will be counted as student income.
- A 529 account or ESA owned by a dependent student, or by a custodian for the student, is to be reported on the FAFSA as a parental asset.
- Withdrawals from 529 plans and ESAs are also treated advantageously. When used to pay for college, such withdrawals are excluded from your federal income tax return and don't need to be added back in when reporting family income on the FAFSA. This is unless the withdrawals come from a grandparent-owned plan, as described above.

Of course, some colleges calculate financial need using a different formula when offering their own grants and tuition discounts.

Consult your professional tax preparer, financial advisor or laywer to determine the best savings plan for you and your family.

MEET THE EXPERT:

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**The fees, expenses and features of 529 plans can vary from state to state. 529 plans involve investment risk, including the possible loss of funds. There is no guarantee a college-funding goal will be met. Earnings must be used to pay for qualified higher education expenses to be federally tax-free. The earnings portion of a nonqualified withdrawal will be subject to ordinary income tax at the recipient's marginal rate and subject to a 10% penalty. By investing in a plan outside your state of residence, you may lose any state tax benefits. 529 plans are subject to enrollment, maintenance and administration/management fees and expenses. This material has been provided for general informational purposes only and does not constitute either tax or legal advice. Although we go to great lengths to make sure our information is accurate and useful, we recommend you consult a tax preparer, professional tax advisor, or lawyer. CRR, LLP has partnered with Axial Financial Group—an independent financial services firm that provides wealth management services. Kristen Zavaski is a financial consultant located at Axial Financial Group, 5 Burlington Woods, Suite 102, Burlington, MA 01803. Securities and advisory services offered through Commonwealth Financial Network®, member FINRA/SIPC, a Registered Investment Adviser. CRR, LLP (also represented as CRR, CRR CPA), Axial Financial Group, and Commonwealth Financial Network are separate and unrelated entities.*