Paying for College: Finding a Strategy That Works

Reprinted from Newsweek

It's a classic good news/bad news moment: that fat envelope in the mailbox signifies that your child's first-choice school said yes. Then there's the deflating next moment, when the bill falls out of the welcome package. For years, the financial news hasn't been good for campus-bound students and their families. Colleges have been raising their fees mercilessly, seemingly oblivious to the declines in family incomes and 529 savings-account balances. Tuition, room and board, fees, and the occasional pizza add up to more than $50,000 a year at the pricier schools, and average more than $37,000 a year at private colleges and $14,000 at public universities.

But there is some good news, too. Federal aid is expanding, and more of it is coming in the form of grants, which don't have to be repaid. Undergraduate students received an average of $8,896 in aid, including $4,656 in grants, in the 2007–08 school year. Since then, both the federal government and some college-specific programs have thrown more money into the mix. Many schools are increasing the amount they'll pay to keep their freshman classes full during the worst recession in 30 years.

You have to know how the system works to make sure your kid gets the money he needs to pay those big bursar's bills. Here's how to afford college now.

Position yourself for financial aid early.
Colleges add up all of their costs for a year of attendance, and then subtract the amount they expect the family to pay. The schools fill the gap with a mix of grants, loans, and student jobs. To maximize the aid your family receives, you have to understand how the family contribution is calculated. Some items, such as student savings accounts, high family income, or big capital gains can hurt your aid eligibility. You can get a rough idea of your expected family contribution by using the calculator at FinAid, an educational Web site (finaid.org/calculators/finaidestimate.phtml), or one provided by the Department of Education at fafsa4caster.ed.gov. You can lower your expected family contribution for freshman year with careful money management in the year before your child graduates from high school (i.e., the year ends in December, graduation is the following June). Colleges base their aid decisions on income from that year, so families who can shift income out of that year by postponing year-end bonuses or delaying the sale of winning investments until January (or later) of graduation year may be able to increase their aid eligibility. This strategy also works if you shift income sooner, and take profits by Dec. 31 of your child's junior year in high school. Money saved in a student's name can be transferred to a 529 college savings plan (which barely hurts their aid eligibility) or spent on extras like summer camp and computers. You'll have to keep this up for four years; schools reassess aid-worthiness annually.

Apply strategically.
Think about money before you choose the schools you will apply to, and don't assume that you'll save the most by going to a state school. The Ivy League schools and other top privates have sworn off most loans and promised to meet full need with grants. Private schools with big endowments can afford more generous aid packages and, in the last year, they have been spending a lot to make sure they have a full freshman class. "This year we saw a lot of want-based aid," says Seth Allen, dean of admissions and financial aid at Grinnell College, which didn't match the generous offers of its competitors. But many schools do, so apply to schools that compete with each other for the same type and tier of students.

Apply for aid.
The earlier you file your application, the better your award is likely to be; schools spend their money fast, notes private adviser Philip Malinoski of Higher Ed Strategies (higheredstrategies.com). By the end of January of your child's senior year of high school, fill out and file the Free Application for Federal Student Aid (fafsa.ed.gov), even if you have to guesstimate numbers and revise them later. Give yourself time and keep the aspirin handy: filling out a FAFSA is about as much fun as doing your 1040 on April 15. The Obama administration has pledged a new, simplified FAFSA by January 2010, but early reports say it still has as many as 120 questions. Also fill out the College Board's Profile form (profileonline.collegeboard.com), which is used by many private schools when they calculate their own aid awards. Finally, touch base with the financial-aid offices at all of the colleges that your child is applying to, and find out if they have any forms of their own for you to complete.

Do all of that, even if you think you make too much. Even families with six-figure incomes can qualify for aid from expensive schools.

Review the offers.
Your aid offer will be sent on April 1, and is likely to consist of grants, loans, and student on-campus work, as follows.

Grants.
Pell Grants are federal grants awarded strictly on the basis of need, and recipients typically come from families earning less than $50,000. For the 2009–10 school year, the maximum award is $5,350. Other federal grant programs include the Federal Supplemental Educational Opportunity Grant (up to $4,000, awarded to students with exceptional financial need) and several grant programs for students with good grades in competitive high-school programs or particular fields of study, such as math or teaching. Colleges also have their own pools of grant money.

Loans.
Stafford loans are the main form of federally funded aid now, and if your expected family contribution is below the school's estimated costs, you'll be able to qualify for as much as $3,500 of subsidized loans for freshman year at 5.6 percent interest for the 2009–10 school year. (In subsequent years, that amount is $4,500 for your sophomore year and $5,500 for each of the next two years, and those interest rates are scheduled to decline over the next two years.) When a Stafford loan is subsidized, the federal government picks up the interest until you leave school. You can also borrow an extra $2,000 a year in unsubsidized Stafford loans; they are charging 6.8 percent interest, and interest accumulates while you are in school. Parents can fill any remaining gaps with the redundantly named Parent Loan for Undergraduate Student (PLUS) at 8.5 percent. Where will these loans come from? More will come directly from the Department of Education, as many private lenders have gotten out of the business. But every college financial-aid office has a list of lenders it works with, and you can also hunt for lenders at the Web site simpletuition.com.

Work study.
Typically, an on-campus job for the student will round out the aid package.

Negotiate the package.
Financial-aid officers call April "haggle month" because that is when parents typically beg for more money and fewer loans. You are most likely to win a better deal if you can demonstrate that your financial circumstances have worsened since you filed the FAFSA. Showing better offers from competing schools can help, too. Even if the school refuses to revise its offer, you are permitted to take some of the package (the grants and the Stafford loans) and turn down other portions of it (the PLUS loans and work-study jobs), if you can find other forms of funding. A student may earn more at an off-campus job than she can taking the work-study job.

Fill the gaps with alternative sources.
Some schools are managing their enrollment by "gapping" some students—not entirely filling the difference between the family's contribution and the school's cost. That forces the student to come up with more cash on their own or go elsewhere. But private loans, available from many banks and student lenders like Sallie Mae, are expensive and can saddle your student with debts that limit his post college choices. Parents must typically cosign them to keep the interest rates at manageable levels, but even then the rates start at about 8 percent and can run as high as 17 or 18 percent if the family's credit score is poor. Students may be able to avoid extra loans by searching for private scholarships at fastweb.com, saving their summer earnings, or working on- or off-campus while they are in school. Other options involve using a home-equity line of credit or gifts from Grandma. Grandparents who want to help their grandchildren pay for school can have the biggest (and least aid-jeopardizing) impact if they simply deposit their gift in the 529 college savings plan held by the parents—or let the kids borrow money and then help them pay it off after they've earned that diploma—and before they have a look at those grad-school bills.