



# Session 12

## Fundamentals of EFC Calculations, Part 1

Claire Micki Roemer

Greg Martin





# How is EFC Determined?

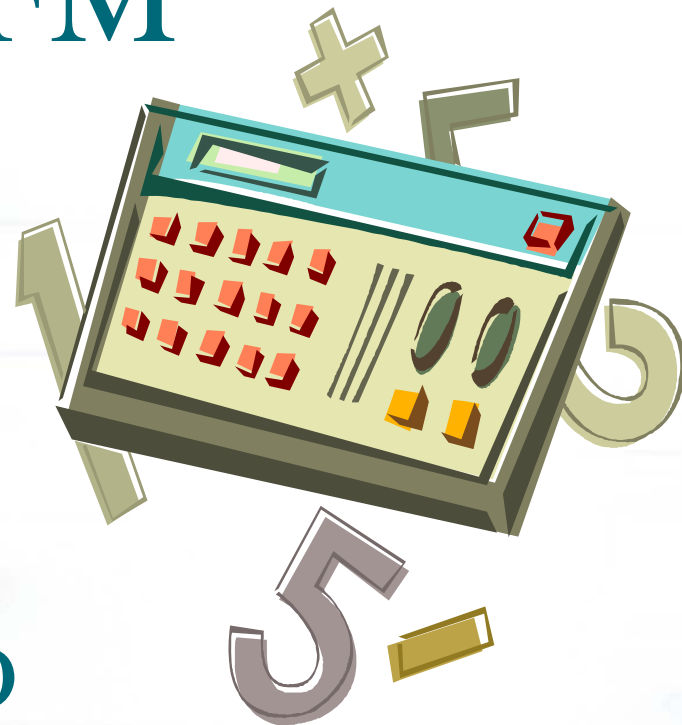
- Three Federal Methodology (FM) models
  - Dependent student
  - Independent student
  - Independent student with dependents other than a spouse





# How is EFC Determined?

- Three distinct FM formulas
  - Regular
  - Simplified
  - Automatic zero





# Factors that affect EFC

- Number in Household
  - Number in College
- Taxed and Untaxed income
  - Taxes paid
- Investments
- Age of the older parent
- Number of wage earners





# Principles of Need Analysis

- Family has primary responsibility to pay for educational costs
- Student and parents are expected to contribute to the extent they are able
- Family should be accepted in its present financial condition
- Families should be evaluated in an equitable and consistent manner





# Need Analysis Concepts

- Need-based funds are available to assist with educational costs that exceed the family's ability to pay
- FM assesses strength at the time of application
- Family resources are devoted first to basic subsistence





# Need Analysis Concepts

- Beyond basic needs, families can exercise discretion
- FM allowances protect family resources
  - Basic needs
  - Non-education related discretionary costs
- FM measures discretionary resources
  - Establishes a portion available for education





# Simplified Formula

- Assets not considered
  - Parents' AGI or earnings from work < \$50,000 **and**
  - Neither parents nor student required to file IRS form 1040







# Automatic Zero

- EFC is automatically zero if
  - Parents' AGI or income earned from work is \$15,000 or less **and**
  - Neither parents nor student required to file IRS form 1040





# Independent Students

- Independent Students without Dependents other than a spouse
  - Applies to single and married independent students
  - May NOT qualify for auto zero EFC
  - May qualify for simplified formula
    - Student (and spouse) AGI or earnings from work < \$50,000 and
    - Student (and spouse) not required to file IRS form 1040





# Independent Students

- Independent Students with Dependents other than a Spouse
  - Analysis looks much like that of parents of dependent students
  - EFC automatically zero if
    - Student's (and spouse's) AGI or income earned from work is \$15,000 or less and
    - Student (and spouse) not required to file IRS form 1040





# Independent Students

- May qualify for simplified formula
  - Student (and spouse) AGI or earnings from work < \$50,000 **and**
  - Student (and spouse) not required to file IRS form 1040





# Our Student

- Carol is a dependent student
  - Lives in OK with a family size of 6
    - Father works, mother works part time
    - Parents have total assets of \$30,100
    - First in her family to go to college





# Treatment of Income in FM

- Total Income:

Base year income from all taxable and untaxable sources

- Exclusions (FAFSA Worksheet C)

= Total Income





# Treatment of Income in FM

- Available Income

- Portion of income remaining for discretionary spending:

Total income

- Total Allowances

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Available Income (AI)





# Total Allowances

- Allowances for taxes
  - U. S. Income tax paid
  - Estimate of state and other taxes
    - State of residence
    - Amount of total income
  - FICA







# Total Allowances

- Income Protection Allowance-IPA
  - Estimates amount needed for basic needs
  - Based on BLS lower budget expenditures adjusted for CPI
  - Increases with each household member
  - Decreases with each member in college





# Total Allowances

- Employment expense allowance
  - Represents additional costs when both parents work
  - Applies to single parent working families





# Treatment of Assets in FM

- Assets defined
  - Cash, savings, checking
  - Investments and trusts
  - Real estate equity
  - Business/farm equity (non-family farms only)
    - Protects first 60% of equity up to \$100K
    - Decreases protection percentage after \$100K





# Treatment of Assets in FM

Cash, savings, checking

+ Net worth of real estate and  
investments

+ Adjusted net worth of business/farm

= Total Net Worth





# Treatment of Assets in FM

Total Net Worth

- Education Savings and Asset  
Protection Allowance

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Discretionary Net Worth





# Treatment of Assets in FM

- Education Savings and Asset Protection Allowance
  - Protects assets for retirement and future education costs
  - Applies  $>$  age 25
    - Increases with age
    - Adjusted for marital status
  - No protection for dependent students





# Treatment of Assets in FM

Discretionary Net Worth

X 12% (asset conversion rate)

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Contribution from Assets





# Adjusted Available Income

Parents' Available Income (+ / -)

+ Parents' Contribution from Assets (+ / 0)

Total Adjusted Available Income (+ / -)







# Determining Parents' Contribution

- As income increases, amount needed for basic household expenses decreases
  - Discretionary income increases
  - Income available for education

Adjusted Available Income (AAI)

X AAI contribution rate

Total Parents' Contribution from AAI





# Determining Parents' Contribution

- Total contribution from AAI is divided evenly among all household members in college

$$\frac{\text{Total PC from AAI}}{\text{Number in College}} = 9\text{-month PC}$$





# Determining Student's Contribution

Total of student taxed + untaxed income

- state and federal taxes
- \$2440 IPA
- allowance for parents' negative AAI

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Available income (AI)

X 50% assessment of AI

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Student contribution from AI



# Determining Student's Contribution

Cash, savings, checking

+ Net worth of real estate and investments

+ Adjusted net worth of business/farm

Total Net Worth

X 35%

Student contribution from assets



# Determining EFC

Parents' Contribution

+ Student's Contribution from AI

+ Student's Contribution from assets

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9 month EFC





We appreciate your feedback and comments. We can be reached at:

- Claire Micki Roemer
- Phone: 202-377-3452
- Fax: 202-275-4551
- Email: [claire.roemer@ed.gov](mailto:claire.roemer@ed.gov)
  
- Greg Martin
- Phone: 215-656-6452
- Email: [greg.martin@ed.gov](mailto:greg.martin@ed.gov)

