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Federal Student Aid: Need Analysis Formulas and Expected Family Contribution

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Summary

This report describes the need analysis formulas used to calculate the Expected Family Contribution (EFC) for federal student aid applicants. The formulas are codified in Title IV of the Higher Education Act (HEA), as amended. The Free Application for Federal Student Aid (FAFSA) is the data collection instrument through which students submit the information that is used to calculate the EFC.

The HEA has three EFC formulas: one for dependent students and one each for independent students with and without dependents. A student's dependency status is determined by the student's age and other characteristics. The dependent student formula considers the financial resources of the student and the student's parents. The independent student formulas consider the financial resources of the student and, if applicable, the student's spouse.

The financial resources considered by the EFC formulas are divided into income and assets. The EFC formulas' definition of a family's income is fairly inclusive and includes many forms of taxable and nontaxable income. The EFC formulas' definition of assets includes balances of qualified bank accounts, investments, business equity, and real estate. There are substantial exemptions in the calculation of assets, including a family's primary residence, retirement accounts, and a family-owned small business.

The EFC formulas provide a number of allowances against income and assets (also known as "protections"). Only income and assets in excess of these allowances ("available" income and assets) are considered when calculating the EFC. If the family's income is below the allowance level, the family will have no available income and therefore no contribution from income. Similarly, if the family is required to report assets and the amount of assets is below the asset protection allowance, the family will have no available assets and therefore no contribution from assets.

Assessment of available income and/or assets is the calculation of the actual EFC or components thereof. The assessment rate is the portion of available income or available assets that contribute to the EFC. For example, the assessment rate for available income of an independent student without dependents is 50%, meaning that each dollar of income in excess of the income allowances increases the family's expected contribution by 50 cents. Assessment rates vary by dependency status and type of financial resource (i.e., income or assets). Generally speaking, additional available income is assessed at a higher rate than additional available assets.

In cases where an applicant's income is below statutorily-specified levels, the family may be eligible for a simplified needs test (SNT) in which the family is not required to report information on assets. Thus, the EFC of applicants who are eligible for the SNT is based entirely on the family's income. In cases where an applicant qualifies for the SNT and meets certain additional income criteria, the applicant may be eligible for an "automatic zero" EFC.

The HEA contains provisions that allow for adjustments for families in specified circumstances. For example, a family with multiple students enrolled in postsecondary education has its EFC divided among the enrolled students. The HEA also contains provisions that allow an individual school's financial aid administrator to exercise professional judgment and adjust certain data used to calculate the EFC to reflect unusual circumstances like job loss, atypically high medical expenses, or other exceptional situations.

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Introduction

Title IV of the Higher Education Act (HEA) authorizes a group of federal student aid programs.[1] Eligibility for many of these aid programs is contingent on student need. Student need is defined as the difference between a school's cost of attendance (COA) and the student's expected family contribution (EFC). A student's EFC is determined by a group of formulas in Part F of Title IV. The formulas define the applicable family unit and establish a process to calculate the EFC for the upcoming award year on the basis of the income and assets of the student and, if applicable, the student's parents or spouse.[2]

The EFC formulas in the HEA are also known as the "federal methodology."[3] This report will discuss the EFC formulas and how current law and the Department of Education (ED) consider the financial resources and other characteristics of a student's family in calculating the EFC.[4] This report will not discuss the application of the EFC in determining and packaging student aid.

The next section of this report will discuss how ED collects and processes information from prospective students using the Free Application for Federal Student Aid (FAFSA). The following section will discuss how the information from the FAFSA is used to determine the student's dependency status and applicable EFC formula. The subsequent sections will describe how each of these formulas translates the financial characteristics of a student's family into an EFC.

Collection and Processing of Student Information

The FAFSA is the data collection instrument for information used to calculate the EFC.[5] The EFC is calculated on the basis of information provided on the FAFSA by the student on income, assets, and other characteristics. Students who do not meet the "independent student" criteria in statute must report information on their parents. Students who are married must report information on their spouses.

Information from the FAFSA is shared with state agencies and institutions of higher education to help determine federal and non-federal aid.[6] Some questions gather information that is relevant to state and institutional aid programs but not relevant to federal aid programs. Responses to these questions do not affect the EFC and corresponding federal aid.[7]

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[1] These federal student aid programs are often collectively referred to as "Title IV programs." The HEA is a broad-reaching law that touches on many aspects of higher education. For an overview of the law, see CRS Report R43351, *The Higher Education Act (HEA): A Primer*, by Alexandra Hegji.

[2] While the EFC assesses how much a student and his or her family is expected to contribute toward educational expenses, there is not a requirement that they actually contribute that amount. As such, non-need-based federal student aid (such as certain types of unsubsidized loans) may be used to substitute for the EFC.

[3] The term "federal methodology" distinguishes the formula in the HEA from separate methodologies that may be used by states or institutions. State and institutional methodologies may or may not be based on the federal methodology.

[4] **Appendix B** provides historical background on the role and determination of student need in federal student aid.

[5] The statutory authorization for the FAFSA is in Section 483 of the HEA (20 U.S.C. 1090).

[6] See Section 483(a)(10) of the HEA (20 U.S.C. 1090[a][10]).

[7] For example, the FAFSA asks the highest level of education completed by each of the student's parents. This question allows states and institutions to target aid to first-generation college students. No federal Title IV programs target funds on the basis of the student's parents' educational attainment.

Individual Filing of the FAFSA

The vast majority of student aid applicants complete the FAFSA online, though it is also possible to complete a paper form.[8] The online FAFSA is designed to prompt applicants only for necessary data. For example, if an applicant's initial responses indicate that he or she meets the criteria to be classified as an "independent" student, the online form will not ask questions about the student's parents. This "skip logic" simplifies the application process by allowing users to only provide necessary information.

Applicants who file the FAFSA online and who have already completed their tax returns for the applicable reference year have the option of using the Internal Revenue Service Data Retrieval Tool (IRS-DRT). The tool provides tax data to the applicants that they can then choose to import into the FAFSA. Some FAFSA items do not have tax form equivalents and therefore must be completed manually, even if the applicant uses the IRS-DRT.

Processing of the FAFSA

After an applicant submits a FAFSA, the form is processed by the Central Processing System (CPS). The CPS uses the applicant's responses to calculate an EFC and checks the application's data against several existing databases (such as the Social Security Administration) to verify the student's identity and eligibility for federal student aid. The CPS also checks the FAFSA for possible inconsistencies or mistakes that require correction.

After processing the FAFSA data, the CPS produces two types of output documents. The Student Aid Report (SAR) provides the student with his or her EFC and other information. Institutional Student Information Records (ISIRs) are provided to institutions that the student specified on his or her FAFSA. The ISIR provides the student's EFC and other data from the FAFSA that can influence institutional need-based aid.[9]

Availability of the FAFSA and Reference Year

The FAFSA becomes available on October 1 of the year prior to the applicable award year (AY). For example, the FAFSA for AY2018-2019 became available October 1, 2017. The FAFSA is completed using income and tax information from the year that is two years prior to the applicable award year. To continue the same example, the FAFSA for AY2018-2019 is completed using income and tax information from calendar year 2016.

Prior to AY2017-2018, the FAFSA became available on January 1 of the award year and was completed using income and tax information from the year prior to the award year. For example, the FAFSA for AY2015-2016 became available on January 1, 2015, and was completed using income and tax information from calendar year 2014.

The move to make the FAFSA available earlier and shift from using the prior year's income and tax information to using information from the "prior-prior year" was accomplished through ED's exercise of an authority specified in the HEA.[10] ED stated that the shift will allow students to

[8] The online FAFSA can be completed and submitted at https://fafsa.ed.gov/. The paper FAFSA for award year 2018-2019 (AY2018-2019) is available at https://fafsa.ed.gov/fotw1819/pdf/PdfFafsa18-19.pdf.

[9] For more information on the SAR and ISIR, see p. AVG-5 of the Student Aid Handbook at https://ifap.ed.gov/fsahandbook/1516FSAHbkActiveIndexMaster.html.

[10] The authority for ED to make this change is established in Section 480(a)(1)(B) of the HEA (20 U.S.C. 1087vv[a][1][B]).

apply for aid earlier and better align the financial aid application process with the college application timeline.[11] The change in timing may also increase the likelihood that families will be able to import tax information to the FAFSA using the IRT-DRT because it is likely that applicable family members will have filed taxes for the applicable year by the time the FAFSA becomes available.

Determination of Dependency Status and Eligibility for the Simplified Needs Test

Data from the FAFSA are used to determine a student's dependency status and the applicable formula within that dependency status. This is typically a two-step process.

The first step is determining the student's dependency status. If the student meets the criteria to be classified as independent, the EFC calculation will only consider the financial resources of the student and, if applicable, the student's spouse. If the student does not meet the criteria for an independent student, the student is classified as dependent and the EFC formula will consider the financial resources of both the student and the student's parents.[12]

The second step is determining the applicant's eligibility for a simplified needs test (SNT). If the applicant is eligible for the SNT, the student's EFC will be determined on the basis of a reduced number of income-based factors and assets will not be considered in EFC calculations. Some applicants who are eligible for the SNT may be further eligible for an "automatic zero" EFC. If an applicant is not eligible for the SNT, the EFC will be determined on the basis of the full formula, which considers both income and assets.

Determining Dependency Status

The HEA has different formulas for each of three dependency statuses:

- dependent students;
- independent students without dependents; and
- independent students with dependents.[13]

As noted previously, the formula for dependent students considers the financial resources of the students' parents while the formulas for independent students do not. In cases where a student is married, the financial resources of the student's spouse are always considered.

[11] See Department of Education, "Changes Impacting the 2017-2018 FAFSA," https://financialaidtoolkit.ed.gov/resources/fafsa-changes-17-18-faq.pdf.

[12] Notably, a student who is married is automatically classified as independent of his or her parents. As such, there is no circumstance in which the EFC formula would consider the financial resources of both the student's parents and the student's spouse.

[13] Statute labels the two groups of independent students as "independent students without dependents other than a spouse" and "independent students with dependents other than a spouse." The definition of a dependent of a student in Section 480(k)(2) of the HEA (20 U.S.C. 1087vv[k][2]) specifies that, for purposes of federal student aid, a spouse cannot be a dependent of an independent student. Since a spouse cannot be a dependent, the "other than a spouse" designation in each dependency status is somewhat unnecessary. In the interest of brevity, this report will refer to "independent students without dependents" and "independent students with dependents."

Criteria for Independent Student

The HEA specifies that a student who does not meet the criteria for an independent student is treated as a dependent student. An independent student is defined as a student who meets *any* of the following criteria:[14]

- is 24 years of age or older by December 31 of the award year;[15]
- is an orphan, in foster care, or a ward of the court; or was an orphan, in foster care, or a ward of the court at any time when the individual was 13 years of age or older;
- is, or was immediately prior to attaining the age of majority, an emancipated minor or in legal guardianship as determined by a court of competent jurisdiction in the individual's state of legal residence;
- is a veteran of the Armed Forces of the United States or is currently serving on active duty in the Armed Forces for other than training purposes;
- is a graduate or professional student;
- is a married individual;
- has legal dependents other than a spouse; or
- has been verified, by a qualified authority during the school year in which the application is submitted, as either an unaccompanied youth who is a homeless child or youth, or as unaccompanied, at risk of homelessness, and self-supporting.

A student who does not meet any of the above criteria is considered a dependent student for the purposes of the EFC formula.[16] Notably, a student's financial independence does not, by itself, make the student independent for federal student aid purposes. Similarly, whether or not a parent declares a student as a dependent on the parent's tax return has no effect on the student's dependency status for the purposes of the FAFSA and federal student aid.

Independent Student with Dependents

The EFC formula has separate treatments for independent students with and without dependents. Thus, once a student meets the criteria for an independent student, it must be determined if the independent student has dependents. Dependents of the student are defined as "the student's dependent children and other persons (except the student's spouse) who live with and receive more than one-half of their support from the student and will continue to receive more than half of their support from the student during the award year."[17]

[14] For complete legislative language related to independent student criteria, see Section 480(d) of the HEA (20 U.S.C. 1087vv[d]).

[15] The award year runs from July 1 to June 30. The FAFSA for a given year presents this criterion in terms of a birthdate. For example, the AY2018-2019 FAFSA asks if a student was born prior to January 1, 1995.

[16] In very limited cases, a school's financial aid administrator may be able to perform a "dependency override" and classify as independent a student who does not meet any of the statutory criteria for an independent student. For more information, see the "Professional Judgment and Students with Unusual Circumstances " section later in this report.

[17] See Section 480(k)(2) of the HEA (20 U.S.C. 1087vv[k][2]).

Whose Financial Resources are Considered When Calculating the EFC?

- If the student meets any of the independent student criteria, the student is considered to be an independent student and the EFC formula considers the financial resources of the student and, if applicable, the student's spouse. For married independent students, the EFC formula considers the income and assets of the student and the student's spouse collectively and generally does not distinguish who the income or assets are associated with.
- If the student does not meet any of the independent student criteria, the student is considered to be a dependent student and the EFC formula considers the financial resources of both the student and the student's parents. For dependent students, the EFC formula has distinct treatments for income and assets depending on whether they are associated with the student or the student's parents.

Determining Eligibility for the Simplified Needs Test[18]

The full EFC formulas consider a range of data elements related to income and assets and make a number of intermediate calculations to determine a student's EFC. Not all students, however, are subject to the full formulas. Applicants with certain characteristics and incomes below a specified level are eligible for a simplified needs test (SNT) or an automatic zero EFC. The SNT does not consider an applicant's assets when calculating the EFC. Applicants who are eligible for the SNT and fill out the FAFSA online are typically not prompted to enter asset information. This reduces the number of questions these students must answer when completing the FAFSA.[19]

To be eligible for the SNT, the applicant must have an adjusted gross income (AGI) of less than $50,000 and meet other criteria. For dependent students, the AGI limit applies only to the student's parents. For independent students, the AGI limit applies to the combined AGI of the student and the student's spouse, if any.

In addition to meeting the AGI limit, an applicant must meet at least one further qualification from a list of criteria. For dependent students, these criteria generally apply to the student's parents. For independent students, these criteria apply to the student and the student's spouse, if any. The statutory criteria are the following:[20]

- *Files a qualified tax form*. Dependent students are eligible if their parents file, or are eligible to file, a 1040A or 1040EZ tax form. Independent students are eligible if they file either a 1040A or 1040EZ. A 1040 form is also a qualified tax form for both dependent students' parents and independent students if the 1040 form is filed only to claim a qualified education tax credit.[21] An applicant who files the 1040 and claims other deductions or credits is not eligible for the SNT.
- *Is not required to file a tax return*. Dependent students are eligible if their parents are not required to file a tax return. Independent students are eligible if neither the student nor the student's spouse, if any, is required to file a tax return.
- *Is a dislocated worker*. Dependent students are eligible if one parent is a dislocated worker. Independent students are eligible if the student or the student's

[18] The simplified needs test is established in Section 479 of the HEA (20 U.S.C. 1087ss). ED has issued clarified eligibility criteria on this issue through the FAFSA and other guidance.

[19] Some states require asset information for all applicants to determine eligibility for state-based aid. Because states get data from the FAFSA, students who are residents of these states may be required to provide asset information even though such information is not necessary for federal aid purposes.

[20] See Section 479(b) of the HEA (20 U.S.C. 1087ss[b]) for full legislative language.

[21] Qualified tax credits are those under Section 25A of the Internal Revenue Code.

spouse is a dislocated worker. A dislocated worker is a worker who has involuntarily lost his or her job and meets other criteria.[22]

- *Received a qualified means-tested benefit in the prior 24 months*. Qualified benefits include Supplemental Security Income (SSI); the Supplemental Nutrition Assistance Program (SNAP, formerly known as food stamps); free and reduced price school lunch; Temporary Assistance for Needy Families (TANF); the special supplemental nutrition program for women, infants, and children (WIC); and other programs identified by the Secretary.[23] ED has used this secretarial discretion to add Medicaid to the qualified means-tested benefits.[24]

Automatic Zero EFC[25]

Some applicants who are eligible for the SNT may be further eligible for an automatic zero EFC. This means that, regardless of other financial characteristics, the student qualifies for a zero EFC. A zero EFC entitles the student to receive the maximum amount of need-based federal student aid, given the student's cost of attendance and enrollment rate. The automatic zero EFC is only available to dependent students and independent students with dependents; it is not available to independent students without dependents.

In AY2018-2019, a dependent student is eligible for the automatic zero EFC if the applicant is eligible for the SNT and the student's parents' AGI was below $25,000. An independent student with dependents is eligible for the automatic zero EFC if the student is eligible for the SNT and the AGI of the student and the student's spouse (if applicable) was below $25,000.

The automatic zero EFC is not the only way that an applicant may be eligible for a zero EFC. It is possible that a student may have a zero EFC as a result of the SNT or a full EFC formula.

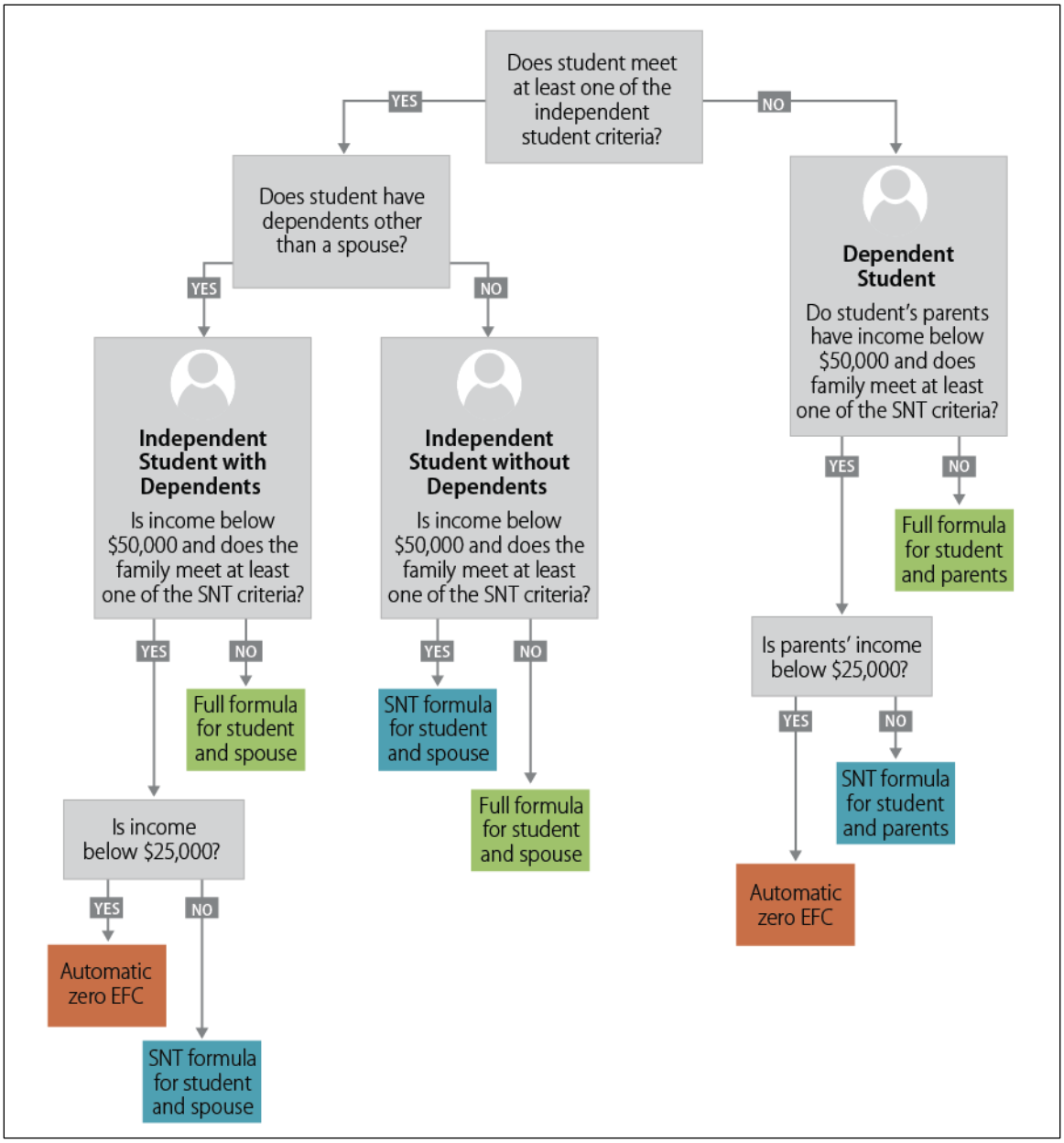
[22] The HEA follows the definition of a dislocated worker in the Workforce Innovation and Opportunity Act (WIOA). WIOA defines a dislocated worker as an individual who has been laid off, demonstrates labor force attachment (usually through eligibility for unemployment compensation), and is unlikely to return to the same industry or occupation. See 29 U.S.C. 3102(15).

[23] According to Section 479 the HEA (20 U.S.C. 1087ss), dependent students are eligible if the student or the student's parent received a qualified benefit. Independent students are eligible if the student or the student's spouse received a benefit. Subregulatory guidance has expanded this policy to include any person in the applicant family's household. For example, see questions 97-101 on the AY2018-2019 FAFSA at https://fafsa.ed.gov/fotw1819/pdf/PdfFafsa18-19.pdf.

[24] See question 97 on the AY2018-2019 FAFSA.

[25] The "automatic zero" criteria are established in Section 479(c) of the HEA (20 U.S.C. 1087ss[c]). The income levels in statute are updated annually per Section 478 (20 U.S.C. 1087rr).

Figure 1. Determination of Dependency Status and Applicable EFC Formula



Source: CRS analysis of Part F of Title IV of the Higher Education Act

Notes: Full criteria for the simplified needs test are in Section 479 of the HEA (20 U.S.C. 1087ss). Automatic zero income threshold is based on AY2018-2019 levels and may be updated in subsequent years.

General Framework and Common Components of the EFC Formulas

As noted previously, the EFC formulas consider the income and assets of the student and, if applicable, the income and assets of the student's parents or spouse. In the simplest terms, the EFC is a specified portion of the applicant's "available" income and assets in excess of allowable "protections." To calculate available income (or assets) it is necessary to calculate total income (or assets) and then subtract the allowable protections.

Figure 2 illustrates the major steps in the calculation of the EFC for each dependency status. There is some variation in the steps based on dependency status:

- For dependent students, separate contributions are calculated on the basis of the student's financial resources and the financial resources of the student's parents. These contributions are then added together for the final EFC.
- For parents of dependent students (but not dependent students themselves) and independent students with dependents, there is an intermediate calculation of "adjusted available income" (AAI). AAI is the sum of available income and the contribution from assets. The AAI is used as the base to calculate the parents' or independent student's final contribution.
- For dependent students and independent students without dependents, contributions from income and assets are calculated separately and then added together. There is no AAI step for these students.

For parents of dependent students with more than one child in college, the parental contribution is divided by the number of students in college before being added to the contribution of the student for the final EFC. Similarly, independent students from families with more than one college student have their final contributions divided by the number of family members in college.

Table 1 provides brief descriptions of the major factors used in the EFC formulas. This table is followed by a more thorough description of the EFC formula for each dependency status. Detailed descriptions of the factors used in the EFC formulas are in **Appendix A** of this report.

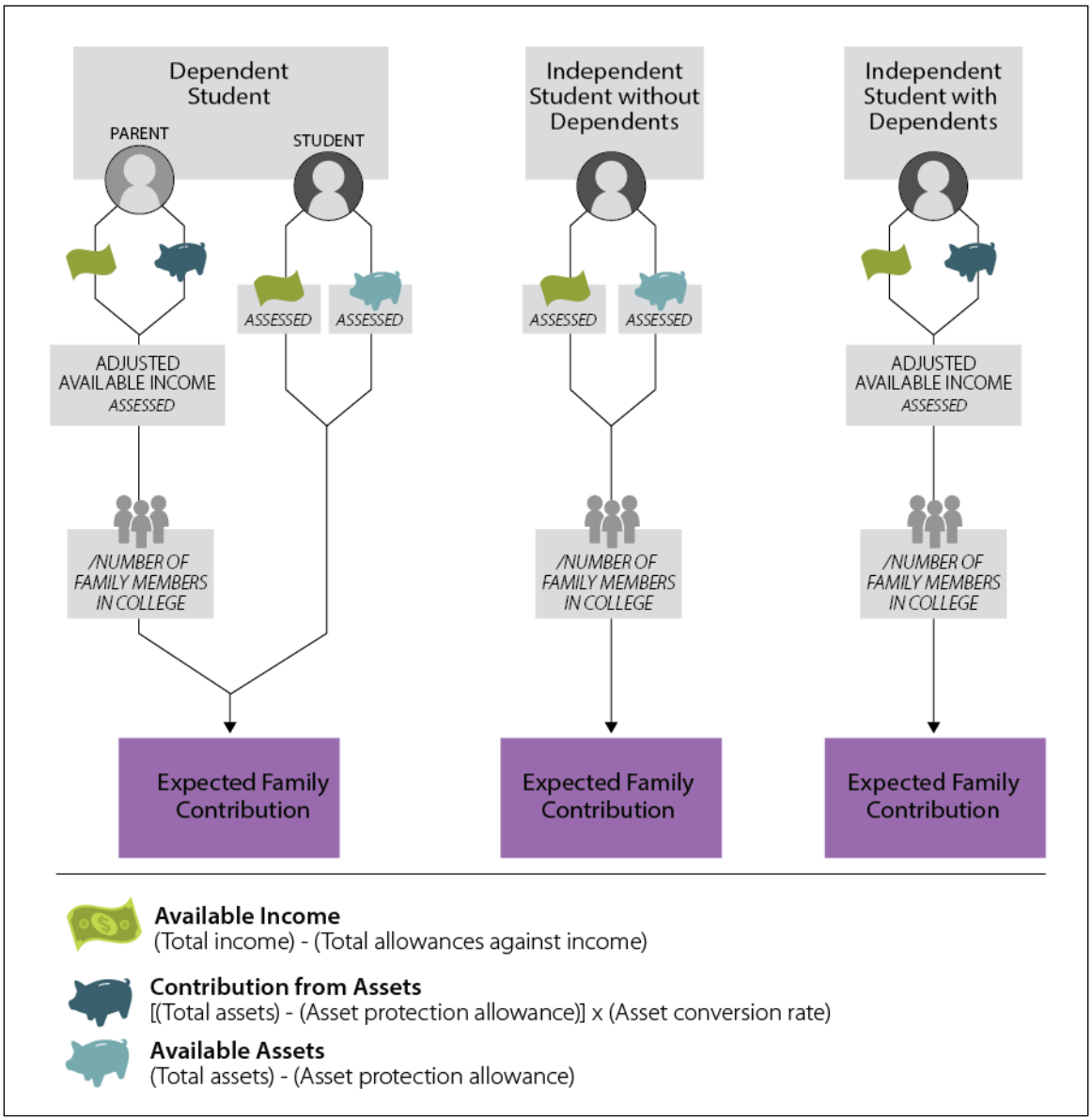
Notably, there is no difference in *what* financial resources are considered for students and relevant family members of each dependency status, though there are differences in *how* these financial resources are treated. For example, total income has the same definition across dependency statuses, but the process to determine how much of an applicant's income contributes to the EFC varies across dependency statuses.

Which Year's Tax Information is Reported on the FAFSA?

Since AY2017-2018, ED has exercised an authority in law that allows a student's EFC to be calculated using income and tax information from the year that is two years prior to the award year. For example, when completing the FAFSA for AY2018-2019, students use tax information from calendar year 2016.

Figure 2. General Framework of EFC Calculation

For students subject to the full needs test



Source: CRS analysis of Part F of Title IV of the Higher Education Act.

Notes: For married independent students, the income and assets of the student's spouse are considered with the student's income and assets. Assessment rates vary for income and assets and by dependency status.

Table 1. Components of the Expected Family Contribution Formula

Factor or Components	Description
Total income =	
Adjusted gross income	Taken from tax return; non-filers report earnings from work
+ Untaxed income	Income that is not considered for federal taxation but is considered by the EFC formulas
- Excludable income	Income that is not considered by the EFC formulas
Available income =	
Total income	Defined above
- Income protection allowance	Standard allowance based on dependency status, family size, and number of students in college
- Federal income tax allowance	Allowance equal to actual federal income taxes
- Payroll tax allowance	Allowance equal to actual Social Security and Medicare taxes
- State and other tax allowance	Allowance calculated on the basis of total income and state of residence
- Employment expense allowance	Allowance for applicants from two-parent families in which both parents have earnings or applicants from single-parent families with earnings
Available assets =	
Total assets	Sum of cash, investments, and real estate; exemptions include retirement accounts, equity in a primary residence, and qualified small businesses
- Asset protection allowance	A protection amount based on the age and marital status of the student (or, if applicable, the student's parents or spouse)
Contribution from assets =	
Available assets	Defined above
x Asset conversion rate	The portion of available assets that may contributes to adjusted available income or EFC
Adjusted available income =	Intermediate calculation; only used for parents of dependent students and independent students with dependents
Available income	Defined above
+ Contribution from assets	Defined above
Contribution from available income / available assets / adjusted available income =	Amount contributed to the EFC from each financial resource
Available income / available assets / adjusted available income	Defined above
x Assessment rate	Percentage of applicable financial resource that contributes to the EFC

Source: CRS analysis of Part F of Title IV of the Higher Education Act.

Note: More detailed definitions for each term are in Appendix A.

Formula A: Calculation of EFC for Dependent Students[26]

The EFC formula for dependent students is different than the formulas for independent students in that it considers the financial resources of both the student and the student's parents. Under this formula, one contribution is calculated for the student's parents and a second contribution is calculated for the student. The sum of the two contributions is the applicant's EFC.

This section describes the full formula for dependent students. As noted previously, however, not all applicants are subject to the full formula. Dependent students with parental income and other characteristics that qualify for the simplified needs test are only subject to the income component of the EFC formula (not the assets component). Applicants who qualify for the simplified needs test with parental income that qualifies them for the automatic zero are not subject to the formula and receive a zero EFC.

Detailed definitions for terms in italics in this section are provided in **Appendix A** of this report.

Calculating the Contribution for a Dependent Student's Parents

Definition of a Parent

If the student's parents are married, the EFC formula considers the income and assets of both parents. Guidance has clarified that if the student's parents are unmarried but living together, the EFC formula will consider the financial resources of both parents.[27]

If the student's parents are divorced or separated and living apart, the EFC formula only directly considers, and the FAFSA only requires, financial information of one parent. The parent whose finances are considered is the parent with whom the student resided with for the greater portion of the 12-month period preceding the date of application. If that criterion does not apply, the EFC formula considers the information of the parent who provided the greater portion of the student's support for the 12-month period preceding the date of application. If neither of the aforementioned criteria apply, the formula considers the financial information of the parent who provided the greater support during the most recent calendar year in which support was provided. If the parent whose financial resources are considered by the EFC formula has remarried, the financial resources of both the parent and stepparent are considered.[28]

There are several components of the EFC formula that may consider support from a parent who is not formally included in the EFC calculation (e.g., a parent the student does not live with). Child support received is considered untaxed income for the recipient parent. Money paid to or on behalf of a child from a noncustodial parent that is not part of a legal child support agreement is considered untaxed income for the student.[29]

[26] This formula is established and described in Section 475 of the HEA (20 U.S.C. 1087oo).

[27] Department of Education, Dear Colleague Letter GEN-13-12, April 29, 2013, http://www.ifap.ed.gov/dpcletters/attachments/GEN1312.pdf.

[28] See Section 475(f)(3) of the HEA (20 U.S.C. 1087oo[f][3]).

[29] See Section 480(b)(1)(F) of the HEA (20 U.S.C. 1087vv[b][1][F]) and question 45(j) of the AY2018-2019 FAFSA.

Parental Available Income

Available income for parents of dependent students is equal to *total income* minus total *allowances against income*. There are five allowances against income:

- *Income protection allowance (IPA)*. The IPA for parents of dependent students is determined by the number of persons in the parents' household and the number of college students in the household. In AY2018-2019, the IPA for a family of four with one student in college is $28,170.
- *Allowance for federal income taxes*. This is equal to actual federal income taxes paid.
- *Allowance for payroll taxes.* This is equal to actual Social Security and Medicare payroll taxes paid.
- *Allowance for state and other taxes*. This is determined by the applicant's total income and state of residence. In AY 2018-2019, the allowance varies from 1% to 8% of total income.[30]
- *Employment expense allowance (EEA)*. The EEA is an additional allowance available to two-parent families in which both parents have earnings from work or in one-parent families in which the parent has earnings from work.

The amount by which total income exceeds total allowances is considered *available income*. Available income is one component of adjusted available income, which is described in a subsequent step.

Parental Available Assets and Asset Conversion

Available assets for parents of dependent students equal *total assets* minus the *asset protection allowance (APA)*. The APA varies by the parent's age (if a single parent) or the age of the older parent (if married).

Parental available assets are then subject to an asset conversion rate of 12%. This means that 12% of parental assets in excess of the APA contribute to adjusted available income, which is described in the next step.

Parental Adjusted Available Income, Assessment, and Calculation of Parental Contribution

Adjusted available income (AAI) for parents is equal to the sum of 100% of parental available income and 12% (the asset conversion rate) of parental available assets. The AAI for parents of dependent students is assessed at progressive rates. AAI levels, assessment rates, and corresponding contributions are presented in **Table 2**. In cases where a family has more than one student in college on at least a half-time basis, the parental contribution is divided by the number of students enrolled in or accepted for enrollment in college. If, for instance, a family has two students in college, the parental contribution is divided in half.

[30] These percentages are for parents with income of $15,000 or more. The allowance for state and other taxes for independent students with dependents and income of less than $15,000 is 1% higher in each state and ranges from 2% to 9%.

Table 2. Assessment Rates and Parental Contribution from Adjusted Available Income

Award Year 2018-2019

If parental AAI is	Parental contribution is
Less than -$3,409	- $750
-$3,409 to $16,400	22% of AAI
$16,401 to $20,500	$3,608 + 25% of AAI over $16,400
$20,501 to $24,700	$4,633 + 29% of AAI over $20,500
$24,701 to $28,900	$5,851 + 34% of AAI over $24,700
$28,901 to $33,100	$7,279 + 40% of AAI over $28,900
$33,101 or more	$8,959 + 47% of AAI over $33,100

Source: 2018-2019 Application and Verification Guide, Table A6, https://ifap.ed.gov/efcformulaguide/attachments/071017EFCFormulaGuide1819.pdf, based on Sections 475 and 478 of the Higher Education Act.

Similar to progressive rates in the income tax system, higher assessment rates only apply to the portion of AAI above the threshold. For example, a parental unit with one student in college and an AAI of $22,000 in AY2018-2019 would have the first $16,400 assessed at 22% (contributing $3,608 to the EFC), the next $4,100 assessed at 25% (adding $1,025 to the EFC), and the remaining $1,500 assessed at 29% (adding $435 to the EFC). The final parental contribution to the EFC in this scenario would be $5,068 ($3,608+$1,025+$435).

The 12% asset conversion rate in the prior step means that assets are assessed in two stages. In practice, this means that additional dollars of income and additional dollars of assets have different effects on the EFC. For example, if a dependent student's parents have one child in college and an AAI above $33,100 (therefore subjecting additional financial resources to the highest 47% assessment rate) and the parents' available income increases by $100, the parents' AAI will increase by $100 and parental contribution to the EFC will increase by $47. Conversely, if the same parents instead report a $100 increase in available assets, the AAI will only increase by $12 due to the 12% asset conversion rate in the prior step and the parental contribution to the EFC will only increase by $5.64 (47% of $12).

Calculating the Contribution for a Dependent Student

In addition to the parents' financial resources, the EFC formula for a dependent student considers the personal financial resources of the student. Financial support from a student's parents whose financial information is reported on the FAFSA is not considered in calculating a dependent student's income or assets.

Dependent Student Available Income, Assessment, and Contribution from Income

Available income for dependent students is *total income* minus total *allowances against income*. Four allowances against income are applied to dependent students' total income:[31]

- *Income protection allowance (IPA)*. The IPA for dependent students in AY2018-2019 is $6,570.

[31] The fifth allowance against income, the Employment Expense Allowance, is not available to dependent students.

- *Allowance for federal income taxes*. This is equal to actual federal income taxes paid.
- *Allowance for payroll taxes*. This is equal to actual Social Security and Medicare payroll taxes paid.
- *Allowance for state and other taxes*. This is determined by the dependent student's total income and state of residence. In AY2018-2019, this allowance ranges from 0% to 6% of total income.

The assessment rate for available income for dependent students is 50%. In practice, this means that once a student's income exceeds allowances, an increase in income of $2 will increase the student's contribution by $1.

Dependent Student Assets, Assessment, and Contribution from Assets

There is no *asset protection allowance* for dependent students. Thus, a dependent student's *total assets* are considered *available assets* and are assessed at a 20% rate.

A notable exception to this treatment of assets is the treatment of an education savings account (such as a 529 account) that is owned by a dependent student. In this case, the education savings account is considered an asset of the student's parent. This leads to a more favorable treatment of the asset than if it was assessed as a dependent student's asset.

Dependent Student Contribution

The contribution of a dependent student is the sum of the dependent student's contribution from income and contribution from assets.

Final EFC for a Dependent Student

The final EFC for a dependent student is the sum of the parental contribution and the dependent student's contribution. In cases where the family has more than one student enrolled in or accepted to college for the award year, the parental contribution is divided by the number of students expected to be enrolled in the upcoming year. The contribution of the dependent student is not divided by the number of students in college.

Formula B: Calculation of EFC for Independent Students without Dependents[32]

The calculation of the EFC for an independent student without dependents considers the financial resources of the student and, if applicable, the student's spouse. For the purposes of calculating total income and total assets of a married student, the couple is considered a single unit.

This section describes the full formula for independent students without dependents. Some independent students without dependents may qualify for the simplified needs test and therefore not be subject to the full formula.

Detailed definitions for each term in italics are provided in **Appendix A** of this report.

[32] See Section 476 of the HEA (20 U.S.C. 1087pp).

Available Income, Assessment, and Contribution from Income

Available income is *total income* minus total *allowances against income*. There are five allowances against income:

- *Income protection allowance (IPA)*. The IPA for an independent student without dependents in AY2018-2019 is $10,220 for an unmarried student or a married student whose spouse is enrolled at least half time. The AY2018-2019 IPA for a married student whose spouse is not enrolled in higher education at least half time is $16,380.
- *Allowance for federal income taxes*. This is equal to actual federal income taxes paid.
- *Allowance for payroll taxes*. This is equal to actual Social Security and Medicare payroll taxes paid.
- *Allowance for state and other taxes*. This is determined by the applicant's total income and state of residence. In AY2018-2019, the allowance varies from 0% to 6% of total income.
- *Employment expense allowance (EEA)*. Independent students are eligible for the EEA only if (1) the student is married and (2) both the student and the student's spouse have earnings from work.

The "contribution from income" for independent students without dependents is equal to 50% of available income. In practice, this means that a $2 increase to the available income of an independent student without dependents will increase the student's contribution from income by $1.

Available Assets, Asset Conversion Rate, and Contribution from Assets

For independent students, *available assets* are *total assets* minus the *asset protection allowance* (APA). The asset protection allowance for independent students is based on the marital status and age of the student. APA levels are presented in **Appendix A**. As noted previously, the APA levels for independent students are the same as the APA levels for parents of dependent students, except that the age variable aligns with the age of the student instead of the age of the older parent.

The asset conversion rate for independent students without dependents is 20%. Thus, the "contribution from assets" is 20% of assets in excess of the APA.

Calculation of EFC

The EFC is the sum of the applicant family's contribution from income and contribution from assets. The EFC can also be considered the sum of 50% of the applicant family's available income and 20% of the applicant family's available assets. In cases where both the student and the student's spouse are enrolled in college, each student's EFC is divided by two.

Formula C: Calculation of EFC for Independent Students with Dependents[33]

The calculation of the EFC for an independent student with dependents considers the financial resources of the student and, if applicable, the student's spouse. For the purposes of calculating total income and total assets of a married student, the couple is considered a single unit. Income or assets of an independent student's dependents are not considered by the EFC formula.

This section describes the full formula for independent students with dependents. As noted in the "Determining Eligibility for the Simplified Needs Test" section, an independent student who qualifies for the simplified needs test is only subject to the income components of the EFC formula (not the assets components). An independent student with dependents who qualifies for the simplified needs test and the automatic zero is not subject to the formula and receives a zero EFC.

Detailed definitions for the terms in italics are provided in **Appendix A** of this report.

Available Income

Available income is *total income* minus total *allowances against income*. There are five allowances against income:

- *Income protection allowance (IPA)*. The IPA is determined on the basis of the number of persons in the student's household and the number of college students in the household. In AY2018-2019, the IPA level for a student from a family of four with one person in college is $39,780.
- *Allowance for federal income taxes*. This is equal to actual federal income taxes paid.
- *Allowance for payroll taxes.* This is equal to actual Social Security and Medicare payroll taxes paid.
- *Allowance for state and other taxes*. This is determined by the applicant's total income and state of residence. In AY2018-2019, the allowance varies from 1% to 8% of total income.[34]
- *Employment expense allowance (EEA)*. The EEA is available to two-parent families in which both parents have earnings from work or in one-parent families in which the parent has earnings from work.

The amount by which total income exceeds total allowances is considered available income. Available income is one component of adjusted available income, which is described in a subsequent step.

[33] See Section 477 of the HEA (20 U.S.C. 1087qq).

[34] These percentages are for independent students with dependents with income of $15,000 or more. The allowance for state and other taxes for independent students with dependents and income of less than $15,000 is 1% higher in each state and ranges from 2% to 9%.

Available Assets and Asset Conversion

Available assets equal *total assets* minus the *asset protection allowance* (APA). The APA varies by the student's marital status and the age of the student. The APA levels for independent students with and without dependents are the same.

Available assets are then subject to an asset conversion rate of 7%. This means that 7% of assets in excess of the APA contribute to adjusted available income, which is described in the next step.

Adjusted Available Income, Assessment, and Calculation of EFC

Adjusted available income (AAI) for independent students is the sum of 100% of available income and 7% (the asset conversion rate) of available assets of the student and, if applicable, the student's spouse. The AAI is assessed to calculate EFC. In cases where a family has more than one student enrolled in or accepted for enrollment in college, the EFC is divided by the number of students.

AAI is assessed at a progressive rate. AAI levels, assessment rates, and corresponding contributions are presented in **Table 3**.

Table 3. Assessment Rates and Expected Family Contribution from AAI, Independent Students with Dependents

Award Year 2018-2019

If the applicant's AAI is	EFC is
Less than -$3,409	-$750
$-3,409 to $16,400	22% of AAI
$16,401 to $20,500	$3,608 + 25% of AAI over $16,400
$20,501 to $24,700	$4,633 + 29% of AAI over $20,500
$24,701 to $28,900	$5,851 + 34% of AAI over $24,700
$28,901 to $33,100	$7,279 + 40% of AAI over $28,900
$33,101 or more	$8,959 + 47% of AAI over $33,100

Source: Based on 2018-2019 Application and Verification Guide, Table C6, https://ifap.ed.gov/efcformulaguide/attachments/071017EFCFormulaGuide1819.pdf, based on Sections 477 and 478 of the HEA.

Similar to progressive rates in the income tax system, higher assessment rates only apply to the portion of AAI above the threshold. For example, an applicant with one student in college and an AAI of $22,000 in AY2018-2019 would have the first $16,400 assessed at 22% (contributing $3,608 to the EFC), the next $4,100 assessed at 25% (adding $1,025 to the EFC), and the remaining $1,500 assessed at 29% (adding $435 to the EFC). The final EFC in this scenario would be $5,068 ($3,608+$1,025+$435).

The 7% asset conversion in the prior step means that assets are assessed in two stages. In practice, this means that additional dollars of income have a substantially larger effect on the EFC than an equal number of additional dollars of assets. For example, if an applicant has an AAI above $33,100 (therefore subjecting additional financial resources to the highest 47% assessment rate) and the applicant's available income increases by $100, the applicant's AAI will increase by $100 and the EFC will increase by $47. Conversely, if the same applicant instead sees a $100 increase in available assets, the applicant's AAI will only increase by $7 due to the 7% asset conversion rate in the prior step and the EFC will only increase by $3.29 (47% of $70).

Table 4. Summary of Final Assessment by Dependency Status

Dependency Status	What is Assessed	Assessment Rate	Effect on EFC of Additional $100 of Income or Assets
Dependent student			
Parents of dependent student	Adjusted available income (Sum of 100% of available income and 12% of available assets)	22% to 47%, with higher levels of adjusted available income assessed at higher rates (see **Table 2**)	$100 increase in available income will increase EFC between $22 and $47 $100 increase in available assets will increase EFC between $2.64 and $5.64.
Dependent student	Available income, Available assets	50% of available income, 20% of available assets	$100 increase in available income will increase EFC by $50. $100 increase in available assets will increase EFC by $20.
Independent student without dependents	Available income, Available assets	50% of available income, 20% of available assets	$100 increase in available income will increase EFC by $50. $100 increase in available assets will increase income by $20.
Independent student with dependents	Adjusted available income (Sum of 100% of available income and 7% of available assets)	22% to 47%, with higher levels of adjusted available income assessed at higher rates (see **Table 3**)	$100 increase in available income will increase EFC between $22 and $47. $100 increase in available assets will increase EFC between $1.54 and $3.29.

Source: CRS analysis of Part F of Title IV the Higher Education Act.

Notes: Effect on the EFC assumes one student in college. Effect of additional assets assumes available assets above zero.

Professional Judgment and Students with Unusual Circumstances

In some cases where a family is subject to unusual financial circumstances, the EFC formulas may not accurately reflect a family's current ability to contribute to educational expenses. The HEA gives individual schools' financial aid administrators (FAAs) limited authority "on the basis of adequate documentation, to make adjustments on a case-by-case basis to the cost of attendance or the values of the data items required to calculate the expected student or parent contribution (or both) to allow for treatment of an individual eligible applicant with special circumstances."[35] Such adjustments are commonly known as professional judgment (PJ).

[35] See Section 479A of the HEA (20 U.S.C. 1087tt).

The HEA provides a non-exhaustive list of circumstances that might qualify for PJ. These include unusually high medical, dental, or nursing home expenses as well as unusually high dependent care costs. An applicant may also be eligible for PJ if the data provided on the FAFSA do not accurately reflect the family's current financial circumstances. For example, a student may request PJ if the family recently experienced a job loss of a primary earner or other substantial changes to the family's income or assets.

When exercising PJ, the FAA may not directly change the student's EFC. The administrator may only change suitable input data that may reduce the EFC. For example, if a family experienced the job loss of a primary earner, the FAA may reduce the applicant's income level to more accurately reflect the family's anticipated income in the coming year.

In very limited cases, FAAs may be able to classify a student as independent when the student does not meet any of the statutory criteria for independent students ("dependency override"). Guidance from ED notes that a student may not be classified as independent on the basis of total self-sufficiency or because the student's parents refuse to provide information or contribute financially to the student's education. Circumstances that may trigger a dependency override include abandonment by parents, an abusive family environment that threatens the student's safety or health, or the student being unable to locate his or her parents.[36]

In all cases of PJ, the FAA is required to document evidence of the circumstances. This documentation may be necessary if the school is audited and has to produce evidence for the adjustment of data used to calculate the EFC.

[36] More information on PJ and dependency overrides is in the "Application and Verification Guide" section of the *2018-2019 Federal Student Aid Handbook*, beginning on p. AVG-111. The full handbook is available at https://ifap.ed.gov/ifap/byAwardYear.jsp?type=fsahandbook&awardyear=2018-2019.

Appendix A. Detailed Definitions and AY2018-2019 Levels

A number of terms and formula factors are defined similarly across EFC formulas. This appendix provides detailed definitions of each of these terms and factors. The definitions in this report are a combination of statute and subsequent agency guidance. In cases where a factor is quantitative and revised annually, this report provides the most recent level from AY2018-2019.[37]

Total income

Total income consists of three factors: (1) adjusted gross income (AGI) and (2) untaxed income, both of which contribute to the total income; and (3) excludable income, which reduces it.

Total Income = Adjusted Gross Income + Untaxed Income – Excludable Income

AGI comes from the applicant's prior-year tax return. AGI is the sum of income that is considered for the purposes of federal taxation.[38] If the applicant did not have to file a tax return in the prior year, the applicant declares any earnings from the prior year and these earnings substitute for the AGI.

Untaxed Income

The EFC formulas consider some forms of income that are excluded from federal taxation. Untaxed income that is considered by the EFC formulas includes the following:[39]

- child support received for any of a parent's children, but not including foster care or adoption payments;
- payments to tax-deferred pension and retirement savings plans;
- IRA deductions and payments to self-employed SEP, SIMPLE, Keogh, and other qualified plans;
- tax-exempt interest income;
- untaxed portions of IRA distributions, excluding rollovers;
- untaxed portions of pensions, excluding rollovers;
- housing, food, and other living allowances paid to members of the military, clergy, and others (including cash payments and cash value of benefits), not including the value of on-base military housing or the value of a basic military allowance for housing;
- veterans noneducation benefits, such as Disability, Death Pension, or Dependency and Indemnity Compensation and/or VA Educational Work-Study allowances;

[37] Updated factor levels were published (and in some cases, corrected) throughout the year in the *Federal Register*. Final levels were collected in the 2018-2019 EFC Formula Guide at https://ifap.ed.gov/efcformulaguide/attachments/071017EFCFormulaGuide1819.pdf.

[38] Taxable income may be lower than AGI due to exemptions and deductions.

[39] See Section 480(b) of the HEA (20 U.S.C. 1087vv([b]). Definitions in this report also reflect additional clarification and instruction from the AY2018-2019 FAFSA.

- money received, or paid on the student's behalf, not reported elsewhere on the FAFSA, including money received from a parent whose financial information is not reported on the FAFSA and that is not part of a legal child support agreement, but *excluding* money paid on a dependent student's behalf by parents whose information is included on the FAFSA; and
- other untaxed income not otherwise reported, such as workers' compensation, disability, etc., *but not including* extended foster care benefits, student aid, earned income credit, additional child tax credit, welfare payments, untaxed Social Security benefits, Supplemental Security Income, Workforce Innovation and Opportunity Act educational benefits, on-base military housing or a military housing allowance, combat pay, benefits from flexible spending arrangements (e.g., cafeteria plans), foreign income exclusion, or credit for federal tax on special fuels.

Excludable Income

Excludable income is income not considered for the purposes of federal student aid. Excludable income is subtracted from the sum of AGI and untaxed income. Excludable income includes the following:[40]

- education tax credits claimed under Section 25A of the Internal Revenue Code;[41]
- child support paid by the student or parent because of a divorce or separation or as a result of a legal requirement;
- taxable earnings from a need-based employment program, such as federal work study and need-based employment portions of fellowships to assistantships;
- taxable student grant and scholarship aid reported to the IRS in adjusted gross income, including AmeriCorps benefits as well as grant and scholarship portions of fellowships and assistantships;
- taxable combat pay, including special combat pay; and
- earnings from work under a cooperative education program offered by an institution of higher education.

Allowances Against Income

Allowances against income (also known as "protections") offset total income as calculated in the prior step. Allowances have the effect of exempting some (or potentially all) of the applicant's income from contributing to the EFC. The allowances are designed to exempt non-discretionary income (such as taxes and very basic living expenses) from the EFC calculation. The allowances

[40] See Section 480(e) of the HEA. Definitions in the report also reflect additional clarification and instruction from the AY2018-2019 FAFSA. On the FAFSA, information related to excludable income is collected under the heading "Additional Financial Information."

[41] Information on education tax credits is collected alongside excludable income on the FAFSA and is added to other forms of excludable income on the EFC worksheets and formula guides. In statute, however, education tax credits are not listed as a form of excludable income in Section 480(e) and are instead listed as an allowance within the formulas for each dependency status (for example, see Section 476[b][1][A][v] for its application in the formula for independent students without dependents). This report follows the EFC worksheets and formula guides and includes education tax credits as a form of excludable income. Whether education tax credits are considered as part of excludable income or as a separate allowance has no effect on the EFC.

mean that applicants are not expected to contribute to educational expenses from their "first dollar" of income.

There are five allowances against income.[42] The sum of these five allowances is the total allowance against income, which is used to calculate available income (described in the next section). Certain components of the allowances against income vary by dependency status. Some allowances are "fixed" and are the same for all applicants with certain characteristics while other allowances vary by an applicant's financial characteristics and income level.

Allowance Against Income #1: Income Protection Allowance

The Income Protection Allowance (IPA) is designed to exclude income for very basic living expenses from contributing to the applicant's EFC. The IPA is determined by the applicant's dependency status and family size, and the number of students in the family enrolled in college.

IPA levels for applicants of each dependency status are established in statute and updated each year. Typically, a schedule of annual IPA increases is established during a reauthorization and ED is directed to calculate increases in award years beyond those established in statute. The most recent statutorily specified IPA levels were in AY2012-2013. Since then, IPA levels have been subject to annual inflationary increases. ED-calculated increases are based on projected levels of inflation and are published annually in the *Federal Register*.

Table A-1. Income Protection Allowances for Parents of Dependent Students

For AY2018-2019

Family Size (including student)	Number of Family Members in College				
	1	2	3	4	5
2	$18,320	$15,180	—	—	—
3	$22,810	$19,690	$16,560	—	—
4	$28,170	$25,040	$21,920	$18,790	—
5	$33,240	$30,100	$26,990	$23,850	$20,740
6	$38,880	$35,740	$32,630	$29,490	$26,380

Source: EFC Formula Guide for Award Year 2018-2019, Table A3, https://ifap.ed.gov/efcformulaguide/attachments/071017EFCFormulaGuide1819.pdf.

Notes: For family size above six, add $4,390 for each additional family member. For family members in college above five, subtract $3,120 for each additional family member in college.

Table A-2. Income Protection Allowance for Dependent Students

For Award Year 2018-2019

All Dependent Students	$6,570

[42] An additional allowance equal to education tax credits claimed under Section 25A of the Internal Revenue Code is listed in statutory formula for each dependency status alongside the other allowances against income. For example, see the formula for parents of dependent students in Section 477(b)(1)(F) of the HEA (20 U.S.C. 1087qq[b][1][F]). However, as noted in the previous footnote, the FAFSA collects information related to education tax credits along with other forms of excludable income and most student aid worksheets calculate tax credits as part of excludable income. This report follows these documents and lists education tax credits in the excludable income section later in this report. Whether tax credits are claimed as an allowance or added to excludable income does not affect the EFC.

Source: EFC Formula Guide for Award Year 2018-2019, p. 10, line 39, https://ifap.ed.gov/efcformulaguide/attachments/071017EFCFormulaGuide1819.pdf.

Table A-3. Income Protection Allowances for Independent Students without Dependents

AY2018-2019

Status	Income Protection Allowance
Student is single, separated, divorced, or widowed	$10,220
Student is married and spouse is enrolled at least half time	$10,220
Student is married and spouse is not enrolled at least half time	$16,380

Source: EFC Formula Guide for Award Year 2018-2019, p. 21, line 12, https://ifap.ed.gov/efcformulaguide/attachments/071017EFCFormulaGuide1819.pdf.

Table A-4. Income Protection Allowances for Independent Students with Dependents

For AY2018-2019

Family Size (including student)	Number of Family Members in College				
	1	2	3	4	5
2	$25,870	$21,450	—	—	—
3	$32,210	$27,810	$23,390	—	—
4	$39,780	$35,370	$30,960	$26,530	—
5	$46,940	$42,500	$38,100	$33,690	$29,290
6	$54,890	$50,480	$46,080	$41,640	$37,250

Source: EFC Formula Guide for Award Year 2018-2019, Table C3, https://ifap.ed.gov/efcformulaguide/attachments/071017EFCFormulaGuide1819.pdf

Notes: For family size above six, add $6,200 for each additional family member. For family members in college above five, subtract $4,400 for each additional family member in college.

Allowance Against Income #2: Allowance for Federal Income Taxes

This allowance reflects actual federal income taxes for the reference year. This information is available from tax returns. If the applicant or relevant family member has not yet filed a tax return at the time of filling out the FAFSA, the applicant may estimate income taxes and later correct the FAFSA.

Allowance Against Income #3: Allowance for Federal Payroll Taxes[43]

This allowance is designed to reflect actual federal payroll taxes (Social Security taxes plus Medicare taxes), and is calculated on the basis of earnings from work. The allowance equals

[43] Statute refers to this allowance as offsetting "Allowance for Social Security taxes," though the EFC Formula Guide calculates an allowance that is designed to reflect payroll taxes for both Social Security taxes as well as Medicare taxes.

7.65% of each earner's earnings up to a maximum ($118,500 in the AY2018-2019 formula) and 1.45% of earnings above that maximum. The maximum applies on a per-earner basis, so if multiple earners are considered on an application (for example, two parents and a student), each earner's payroll tax allowance is calculated separately.

Allowance Against Income #4: Allowance for State and Other Taxes

This allowance aims to reflect estimated non-federal taxes, and is calculated on the basis of total income and state of residence. There is variation among states. Allowances for each state are established in statute but are updated each year after ED reviews the Department of the Treasury's Statistics of Income file and the determination of the percentage of income that each state's taxes represent.[44] Updated allowance percentages are published each year in the *Federal Register*.

The allowance percentage for residents of each state varies based on dependency status.

Table A-5. Allowances for State and Other Taxes by Dependency Status

AY2018-2019

State	Parents of a Dependent Student[a]	Dependent Student	Independent Student without Dependents	Independent Student with Dependents[b]
Alabama	2%	2%	2%	2%
Alaska	1%	0%	0%	1%
Arizona	2%	2%	2%	2%
Arkansas	3%	3%	3%	3%
California	7%	6%	6%	7%
Colorado	3%	3%	3%	3%
Connecticut	7%	5%	5%	7%
Delaware	3%	3%	3%	3%
District of Columbia	6%	6%	6%	6%
Florida	1%	1%	1%	2%
Georgia	2%	3%	3%	4%
Hawaii	4%	4%	4%	4%
Idaho	3%	3%	3%	3%
Illinois	5%	3%	3%	5%
Indiana	3%	3%	3%	3%
Iowa	4%	3%	3%	4%
Kansas	3%	2%	2%	3%
Kentucky	4%	3%	3%	4%
Louisiana	2%	2%	2%	2%
Maine	5%	3%	3%	5%
Maryland	7%	5%	5%	7%

[44] See Section 478(g) of the HEA (20 U.S.C. 1087rr[g]).

State	Parents of a Dependent Student[a]	Dependent Student	Independent Student without Dependents	Independent Student with Dependents[b]
Massachusetts	5%	4%	4%	5%
Michigan	3%	2%	2%	3%
Minnesota	5%	4%	4%	5%
Mississippi	2%	2%	2%	2%
Missouri	3%	3%	3%	3%
Montana	3%	3%	3%	3%
Nebraska	4%	3%	3%	4%
Nevada	1%	1%	1%	1%
New Hampshire	3%	1%	1%	3%
New Jersey	8%	4%	4%	8%
New Mexico	2%	2%	2%	2%
New York	8%	6%	6%	8%
North Carolina	4%	3%	3%	4%
North Dakota	1%	1%	1%	1%
Ohio	4%	3%	3%	4%
Oklahoma	2%	2%	2%	2%
Oregon	6%	5%	5%	6%
Pennsylvania	4%	3%	3%	4%
Rhode Island	5%	3%	3%	5%
South Carolina	3%	3%	3%	3%
South Dakota	1%	1%	1%	1%
Tennessee	1%	1%	1%	1%
Texas	2%	1%	1%	2%
Utah	4%	3%	3%	4%
Vermont	5%	3%	3%	5%
Virginia	5%	4%	4%	5%
Washington	2%	1%	1%	2%
West Virginia	2%	2%	2%	2%
Wisconsin	5%	4%	4%	5%
Wyoming	1%	1%	1%	1%

Source: EFC Formula Guide for Award Year 2018-2019, Tables A1, A7, B1, and C1, https://ifap.ed.gov/efcformulaguide/attachments/071017EFCFormulaGuide1819.pdf

a. Percentage in table reflects the allowance for state and other taxes for parents of dependent students with incomes of $15,000 or more. In the case of parents of dependent students with incomes below $15,000, the allowance for state and other taxes is 1% higher than in the table.

b. Percentage in table reflects the allowance for independent students with dependents with incomes of $15,000 or more. In the case of independent students with dependents with incomes below $15,000, the allowance for state and other taxes is 1% higher than in the table.

Allowance Against Income #5: Employment Expense Allowance

The Employment Expense Allowance (EEA) provides an additional allowance to two-adult households in which both adults have earnings from work and to one-adult households with dependents and earnings from work. The EEA is available to parents of dependent students, married independent students without dependents, and independent students with dependents. It is not available to dependent students themselves or unmarried independent students without dependents. The maximum EEA is 35% of the earnings of the lower-earning adult or $4,000, whichever is less.

Available Income

Available income is the difference between total income and the sum of the five allowances against income. In some cases where total allowances against income are greater than total income, available income can be zero or negative.

Total Assets

The consideration of assets aims to reflect financial resources that are not reflected in income. Assets are only considered when applicants do not qualify for the simplified needs test (SNT). Applicants who do qualify for the SNT do not have to provide asset information for federal student aid purposes.[45]

Statute and some federal documents use both "assets" and "net worth" interchangeably for various stages of asset calculations. In the interest of uniformity, this report uses "assets."

The HEA defines assets as

> [C]ash on hand, including the amount in checking and savings accounts, time deposits, money market funds, trusts, stocks, bonds, other securities, mutual funds, tax shelters, qualified education benefits ... and the net value of real estate, income producing property, and business and farm assets.[46]

Exemptions and Special Treatments of Assets

There are substantial exemptions that exclude some assets from being considered in the calculation of total assets. These exemptions include the following:

- *Home equity*. The family's "principal place of residence" or "a family farm on which the family resides" is excluded in the calculation of total assets.
- *Retirement accounts*. These accounts are not mentioned in the definition in law. Agency guidance explicitly excludes them.
- *Family-owned businesses*. Statute excludes from a family's assets "a small business with not more than 100 full-time equivalent employees ... that is owned and controlled by the family."[47]

[45] In some cases, a state will consider an applicant's assets even if the student qualifies for the federal SNT. In these cases, the online FAFSA will still ask the applicant asset questions as they might relate to state student aid.

[46] See Section 480(f)(1) of the HEA (20 U.S.C. 1087vv[f][1]).

[47] See Section 480(f)(2)(C) of the HEA (20 U.S.C. 1087vv[f][2]).

- *Possessions*. The values of cars, jewelry, and other tangible items are not considered assets by the EFC formulas.

The value of a non-exempt businesses or farm is adjusted so that it is considered an asset at less than 100% of its value. The value is adjusted at a progressive rate. In AY2018-2019, the adjusted value of a non-exempt business or farm worth up to $130,000 is 40% of its value. The percentage increases at higher values and 100% of the value of a business in excess of $655,000 is considered an asset of the family.[48]

Education Savings Accounts

Balances of education savings accounts (such as those commonly known as 529 accounts) are counted as an asset in calculating the EFC. In the case of dependent students, education savings accounts that are owned by the dependent student are considered assets of the student's parents. Because assets of parents are treated more favorably by the EFC formula than assets of dependent students, this results in a lower EFC than if the account were considered as an asset of the student.

Disbursements from education savings accounts that are owned by a student or a parent of a dependent student are not reported on the FAFSA. Disbursements from education savings accounts that are not owned by a student or a parent of a dependent student and therefore not reported on the FAFSA (such as an account owned by a grandparent) are considered untaxed income.

Asset Protection Allowance

As is the case with income, an allowance against assets means that only non-exempt assets in excess of the allowance contribute to the EFC. Unlike the multiple allowances against income, the HEA has a single allowance against assets called the "Education Savings and Asset Protection Allowance." This allowance is also referred to as the "Asset Protection Allowance." This report will follow the terminology used in ED documents and refer to it as the Asset Protection Allowance (APA).

The APA varies by the age and marital status of the student's older parent (in the case of parents of a dependent student) or by the age and marital status of the student (in the case of an independent student). The APA increases with the age of the applicable parent or student. Dependent students are not eligible for an APA. This means that dependent students' assets (except for an education savings account, which is considered an asset of the parent) are assessed from the "first dollar."

APA levels were established in statute (by the 1992 HEA amendments) and are updated by ED each year. Updated levels are published in the *Federal Register* alongside updated income allowances. Updates to the APA are not based on inflation. Instead, the HEA specifies that the APA level for a given year is

> developed by determining the present value cost, rounded to the nearest $100, of an annuity that would provide, for each age cohort of 40 and above, a supplemental income at age 65 (adjusted for inflation) equal to the difference between the moderate family income (as most recently determined by the Bureau of Labor Statistics), and the current average social security retirement benefits. For each age cohort below 40, the allowance shall be

[48] Full information on the adjustments of the value of these assets is in the formulas for each dependency status in Sections 475, 476, and 477 of the HEA (20 U.S.C. 1087oo-1087qq). Levels for AY2018-2019 were published in the EFC Formula Guide for Award Year 2018-2019 at https://ifap.ed.gov/efcformulaguide/attachments/071017EFCFormulaGuide1819.pdf.

> computed by decreasing the allowance for age 40, as updated, by one-fifteenth for each year of age below age 40 and rounding the result to the nearest $100. In making such determinations-
>
> (1) inflation shall be presumed to be 6 percent per year;
> (2) the rate of return of an annuity shall be presumed to be 8 percent; and
> (3) the sales commission on an annuity shall be presumed to be 6 percent.[49]

The single formula for the APA means that the APA is the same for persons of the same age across dependency statuses, though there are slight variations in application. For example, married parents of a dependent student, the older of which is 40 years old, would have the same APA in a given year as a married 40-year-old student.

Unlike the IPA, which increases each year based on estimated inflation, the more sophisticated calculation of the APA means that it can rise or fall from year to year. The APA is calculated based on the difference between "moderate family income" and "current average Social Security benefits," and a change in the difference can increase or decrease the APA. Since the establishment of the APA in statute effective AY1993-1994, average Social Security benefits have increased faster than family incomes, reducing the difference between the two and resulting in a corresponding reduction in the APA.

Table A-6. Asset Protection Allowance, Parents of Dependent Students

AY2018-2019

Age of Older Parent	Allowance for Two Parents	Allowance for One Parent	Age of Older Parent	Allowance for Two Parents	Allowance for One Parent
25 or less	$0	$0	46	$20,300	$12,300
26	1,200	700	47	20,700	12,600
27	2,400	1,400	48	21,300	12,900
28	3,500	2,200	49	21,800	13,200
29	4,700	2,900	50	22,300	13,500
30	5,900	3,600	51	22,900	13,800
31	7,100	4,300	52	23,500	14,100
32	8,300	5,000	53	24,100	14,400
33	9,400	5,800	54	24,800	14,800
34	10,600	6,500	55	25,400	15,200
35	11,800	7,200	56	26,100	15,500
36	13,000	7,900	57	26,800	15,900
37	14,200	8,600	58	27,600	16,300
38	15,300	9,400	59	28,300	16,700
39	16,500	10,100	60	29,100	17,100
40	17,700	10,800	61	30,000	17,600
41	18,100	11,000	62	30,800	18,000
42	18,500	11,300	63	31,700	18,500

[49] See Section 478(d) of the HEA (20 U.S.C. 1087rr[d]).

Age of Older Parent	Allowance for Two Parents	Allowance for One Parent	Age of Older Parent	Allowance for Two Parents	Allowance for One Parent
43	18,900	11,500	64	32,600	19,000
44	19,300	11,800	65 or older	33,600	19,500
45	19,800	12,000			

Source: EFC Formula Guide for Award Year 2018-2019, Table A5, https://ifap.ed.gov/efcformulaguide/attachments/071017EFCFormulaGuide1819.pdf

Note: Allowance applies to independent students with or without dependents.

Table A-7. Asset Protection Allowance, Independent Students

Award Year 2018-2019

Age of the Student	Student is Married	Student is Single	Age of the Student	Student is Married	Student is Single
25 or less	$0	$0	46	$20,300	$12,300
26	1,200	700	47	20,700	12,600
27	2,400	1,400	48	21,300	12,900
28	3,500	2,200	49	21,800	13,200
29	4,700	2,900	50	22,300	13,500
30	5,900	3,600	51	22,900	13,800
31	7,100	4,300	52	23,500	14,100
32	8,300	5,000	53	24,100	14,400
33	9,400	5,800	54	24,800	14,800
34	10,600	6,500	55	25,400	15,200
35	11,800	7,200	56	26,100	15,500
36	13,000	7,900	57	26,800	15,900
37	14,200	8,600	58	27,600	16,300
38	15,300	9,400	59	28,300	16,700
39	16,500	10,100	60	29,100	17,100
40	17,700	10,800	61	30,000	17,600
41	18,100	11,000	62	30,800	18,000
42	18,500	11,300	63	31,700	18,500
43	18,900	11,500	64	32,600	19,000
44	19,300	11,800	65 or older	33,600	19,500
45	19,800	12,000			

Source: EFC Formula Guide for Award Year 2018-2019, Table B4 and C5, https://ifap.ed.gov/efcformulaguide/attachments/071017EFCFormulaGuide1819.pdf

Note: Allowance applies to independent students with or without dependents.

Available Assets

Available assets are the difference between an applicant's total assets and the asset protection allowance. In cases where the allowance is greater than the applicant's total assets, the applicant's available assets and contribution from assets are zero.

Asset Conversion Rate

The asset conversion rate is the portion of available assets that either

- contribute to the final EFC, or
- contribute to the calculation of adjusted available income that is subsequently assessed to calculate the EFC.

Statute refers to the resulting product of multiplying available assets by the asset conversion rate as "contribution from assets." The asset conversion rate varies by dependency status. Asset conversion is discussed in greater detail in the description of each formula.

Adjusted Available Income (AAI)

AAI is an intermediate calculation prior to final assessment that is only performed for parents of dependent students and independent students with dependents. AAI is the sum of available income and the product of available assets and the asset conversion rate. The application of the AAI is discussed in the description of the formulas for parents of dependent students and independent students with dependents.

Assessment Rate and Calculation of the EFC

The assessment rate is the portion of available income, available assets, or AAI that is determined to be available for educational expenses and contributes to the EFC. Depending on dependency status, the assessment rate can be a flat percentage (such as the 50% assessment of a dependent student's available income) or a progressive percentage (such as the increasing assessment rates for independent students with dependents in **Table 3**).

In practice, the assessment rate is the portion of an "additional dollar" that contributes to the EFC. For example, the assessment rate for available income for independent students without dependents is 50%. This means that a $10 increase in available income will increase the EFC of such a student by $5.

Appendix B. Legislative History

Financial need has been a key component of federal student aid since the enactment of the original Higher Education Act (HEA) in 1965, though the specific processes for determining need have evolved. Generally, reauthorizations of the HEA and other legislative action have gradually increased statutory direction in determining the ability of students and their families to contribute to educational costs while reducing the discretion of the administering agency (originally the Office of Education, now the Department of Education [ED]).

Enactment of the HEA and Action through 1986

Need-based aid programs and corresponding provisions related to the determination of need were established in Title IV of the HEA of 1965 (P.L. 89-329). Modified versions of these programs remain in Title IV of the HEA, as amended. As such, student aid programs are often collectively referred to as "Title IV programs."

Title IV of the original HEA authorized, among other programs, Educational Opportunity Grants to institutions of higher education to support students with "exceptional financial need." Establishing student need and disbursing awards was the responsibility of the grantee institution, though the law directed the Commissioner of Education[50] to prescribe "basic criteria or schedules (or both) for the determination of the amount of any such educational opportunity grant, taking into account the objective of limiting grant aid under this part to students of exceptional financial need[.]"[51]

The 1972 amendments to the HEA (P.L. 92-318) established the term "expected family contribution" and used the EFC in the determination of need-based grants. The 1972 amendments did not establish an EFC formula, but instead offered a general framework and instructed the Commissioner of Education to publish an annual family contribution schedule (FCS) in the *Federal Register*. The statutory framework for the EFC and corresponding FCS in the 1972 amendments specified factors that the agency should consider when determining the EFC (such as effective income, amount of assets, and the number of dependents in the family), but it did not specify treatments of these factors (such as assessment rates).[52]

The 1972 amendments required the Office of Education to publish the proposed FCS by February 1 of each year. Subsequent to this publication, "interested parties" may "present their views and make recommendations with respect to such schedule." The law also gave both the House and the Senate the authority to adopt a resolution of disapproval related to the schedule. The commissioner was required to take any feedback into consideration prior to publishing a final FCS by July 1.[53]

The Education Amendments of 1980 (P.L. 96-374) established a revised need analysis system in Section 482 of the HEA, as amended. This system applied across most Title IV programs, including the newly renamed Pell Grants. The system established in the 1980 amendments

[50] Prior to the establishment of the Department of Education, federal education activities were administered by the Office of Education under the Department of Health, Education, and Welfare.

[51] See Section 402 of P.L. 89-329.

[52] See Section 411(a)(3)(B)(ii) as amended by P.L. 92-318 for the full list of factors considered.

[53] See Section 411 of the HEA as amended by P.L. 92-318.

offered more congressional direction than prior legislation, but still left substantial decisionmaking authority to the Department of Education.[54]

A relatively short time after the enactment of the 1980 amendments, various legislation modified the need analysis provisions of the HEA, establishing separate systems for Pell Grants and other campus-based programs with ED publishing contribution schedules in the *Federal Register*. Several other laws made short-term modifications to eligibility for Pell Grants and other forms of need-based aid between 1981 and the enactment of the Higher Education Amendments of 1986.[55]

Higher Education Amendments of 1986

The Higher Education Amendments of 1986 (P.L. 99-498) made substantial statutory changes to the need analysis system.[56] This law established one need analysis formula for Pell Grants ("Pell Formula") and a different formula for most other Title IV programs ("Part F Formula").[57] The 1986 amendments marked a change from Congress providing guidelines to ED and the agency determining factor definitions and levels to Congress specifying in statute what factors would be considered and what the treatment of those factors would be (e.g., prescribing allowance levels and assessment rates in statute).

Both the Pell Formula and the Part F Formula established three dependency statuses with corresponding treatments of income and assets for each status: dependent student, independent student with dependents, and independent student without dependents. The law established that a student would be considered independent if he or she met criteria related to age (24 or older on December 31 of the award year) or other criteria. Under the 1986 amendments, a student could be classified as independent if the student was not claimed as a dependent for tax purposes by his or her parents in the prior year (in the case of a married student or graduate student) or the prior two years (in the case of a single undergraduate student).[58]

While terminology and definitions varied between the formulas, both the Pell Formula and the Part F Formula followed the same general process of determining the financial resources of the student (and if applicable, the student's parents and/or spouse) by calculating the applicant's total income (and assets), subtracting specified allowances, and then assessing financial resources in excess of those allowances. Both formulas considered family size and the number of family members in college.

The formulas differed in some of their treatments of certain financial resources and the construction of some of their allowances. For example, when calculating assets the Pell Formula

[54] For example, the law established a maximum assessment rate for families with incomes below $25,000 and prescribed an asset protection allowance of $10,000. See Section 482(b) of the HEA, as amended by P.L. 96-374.

[55] For example, P.L. 97-301, the Student Financial Assistance Technical Amendments of 1982, separated the Pell Grant family contribution schedule from the need analysis system for campus-based programs and established direction for the Pell Grant FCS for award years 1983-1984 and 1984-1985. P.L. 98-79, the Student Loan Consolidation and Technical Amendments of 1983, subsequently modified some of the need analysis provisions of P.L. 97-301 and established new direction related to award years 1984-1985 and 1985-1986.

[56] Many of the statutory changes in P.L. 99-498 were based on policies that were already in place in regulations. When this section refers to changes, it is referring to their codification in statute.

[57] The formula for Pell Grants was in Sections 411A-411F of the HEA as amended by P.L. 99-498. The formula for most other programs was in Sections 471-480 of the HEA as amended by P.L. 99-498. The formula in Sections 471-480 applied to all Title IV aid except Pell Grants and Grants to States for State Student Incentives authorized by Subpart 3 of Part A of Title IV.

[58] For full criteria for independent students, see Sections 411F(12) and 480(d) of the HEA as amended by P.L. 99-498.

only considered home equity in excess of $30,000 while the Part F Formula considered home equity in its entirety.[59] The two formulas also have different final assessment rates of each applicant's income and/or assets.

The 1986 amendments established a simplified needs test (SNT) for qualified applicants. Applicants who were eligible for the SNT were required to provide less financial information in the application process and no information related to assets. To qualify for the SNT under the 1986 amendments, the applicant's family must have an adjusted gross income of $15,000 or less and file tax form 1040A. The SNT criteria were applicable to all Title IV programs.[60]

1992 Amendments to the Higher Education Act

The 1992 amendments to the Higher Education Act (P.L. 102-325) established the foundation for the current EFC system. They merged the need analysis systems, creating a single system that calculated a single EFC that applied across need-based HEA Title IV programs.[61] Prior to the 1992 amendments, separate formulas existed for Pell Grants and other types of aid and could yield different family contributions for their respective programs. In merging the two formulas, the 1992 amendments also made changes to the factors that the formula considered.

Creation of the FAFSA and the Combining of EFC Formulas

The 1992 amendments created the Free Application for Federal Student Aid (FAFSA).[62] The FAFSA was intended to be a standardized data collection tool for all students. Prior to the FAFSA, several entities were under contract with the federal government to collect and process data related to federal student aid. These contracted entities, known as Multiple Data Entry processors or MDEs, each developed different forms. The MDEs shared information with states and institutions, but could charge a fee to the applying student or to the state or institution that received the data.

The 1992 amendments specified that ED would create a common application for federal student aid that would be distributed and processed at no charge to the student. The law also specified that the MDEs must provide student data to states and institutions at no cost. To incentivize states and institutions to only use FAFSA-collected data in their student aid decisions, the law allows the inclusion of questions on the FAFSA that do not affect federal aid but may affect nonfederal aid.[63] Provisions pertaining to FAFSA distribution, processing, and the inclusion of additional

[59] The Part F formula had an exemption where home equity was not considered if the student (or, in the case of a dependent student, the student's parent) was a dislocated worker or dislocated homemaker. For example, see Section 475(d) of the HEA as amended by P.L. 99-498 for this provision as it applies to parents of dependent students.

[60] See Section 479 of the HEA as amended by P.L. 99-498.

[61] P.L. 102-325 amended the HEA so that eligibility for Pell Grants and all other aid was determined on the basis of the EFC calculated in Part F of Title IV of the HEA, as amended.

[62] The FAFSA was established in Section 483 of P.L. 102-325. It currently remains codified in Section 483 of the HEA (20 U.S.C. 1090).

[63] For example, the FAFSA asks for the highest level of education completed by the student's parents. The answer to this question does not impact federal aid but may establish eligibility for state or institutional programs that target aid for first-generation college students. This allowance for state-driven items was established by Section 483(a)(1) of P.L. 102-325, which stated that ED "may include on the form developed pursuant to this paragraph not more than eight nonfinancial data items selected in consultation with the States to assist the States in awarding State student financial assistance." In current law, Section 483(a)(5) permits the inclusion of "specific data items as the Secretary determines are necessary to meet State requirements for need-based State aid."

questions on the FAFSA were established by Section 483 of P.L. 102-325 and remain in Section 483 of the HEA.

Formula Changes in the 1992 Amendments

In combining formulas from prior legislation, it was necessary to make a number of changes to each formula. For example, the Pell Formula and Part F Formula from the 1986 amendments had different assessment rates, so changes were necessary to develop a standardized formula. In addition to these "compromises" necessary to combine the formulas, the 1992 amendments also made some changes to the EFC formula that did not have precedent in either prior formula. For example:

- The 1992 amendments completely eliminated home equity from consideration when determining a family's assets.
- The 1992 amendments eliminated the provision by which a student could establish independence on the basis of "total self-sufficiency" for two years.

Reauthorizations and Amendments Since 1992

Since the 1992 amendments, the HEA was reauthorized by the Higher Education Amendments of 1998 (P.L. 105-244) and the Higher Education Opportunity Act of 2008 (P.L. 110-315), and each law made changes to the EFC formula. The EFC formula was also amended by the College Costs Reduction Act of 2008 (P.L. 110-84) as well as by other appropriations and reconciliation laws. These changes were largely incremental and did not have systemic effects on the scale of some of the prior reauthorizations.

The most far-reaching provisions of the post-1992 changes to the need analysis formulas have primarily been numeric adjustments to the income protection allowances (i.e., the amount of income that is exempt from assessment in calculating the EFC) and/or changes to qualifications for alternative formula such as the "automatic zero" EFC. These changes usually (but not always) have resulted in lower EFCs for at least some students.[64]

Non-numeric changes since 1992 have included establishing protocol for enrollment periods of less than nine months and expanding the range of circumstances in which financial aid administrators could use professional judgment to adjust formula factors to reflect students with special circumstances.[65]

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[64] For example, P.L. 109-171 (the Deficit Reduction Act of 2005) and P.L. 110-84 (the College Cost Reduction and Access Act of 2007) each increased income protection allowances for some student populations. A notable exception to the trend of amendments expanding aid was the Consolidated Appropriations Act of 2012 (P.L. 112-74), which reduced the income threshold for an "automatic zero" EFC from $32,000 to $23,000.

[65] See Sections 473, 474, 475, and 479A of the HEA, as amended by P.L. 105-244.

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