Financial aid rules influence household portfolio decisions

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"The findings support the act and the need to simplify the financial aid application process. It is important to find a method that will provide a better picture of household net worth," said Tansel Yilmazer, assistant professor in the MU Department of Personal Financial Planning. "One option would be to combine FAFSA questions with questions on tax forms."

Currently, assets in retirement funds or home equity are not considered in the calculation of need for financial aid. Because of this, families with more money in other types of savings are eligible for less financial aid.

"Ideally, two families with the same income stream should be eligible for the same amount of financial aid," Yilmazer said. "Right now, if one family invests more in retirement or in huge homes with high equity, then that family might be eligible for more financial aid than the family that doesn't make these investments. Thus, the current system might not be achieving horizontal equity."

In the study, Yilmazer examined the impact the marginal financial aid tax rate ¬- a rate calculated using age, income, and number of children in college to determine aid eligibility - has on the assets in retirement funds and home equity. The researchers found that the current system allows for families to intentionally or unintentionally adjust their portfolios to receive more financial aid.

"We hope these findings will influence policy change that will eliminate the current loophole and make the financial aid system more efficient and equal," Yilmazer said.

The study, "The Impact of College Financial Aid Rules on Household Portfolio Choices," included household financial data from the 2001 Survey of Consumer Finances. The study will be published in the December 2009 issue of the *National Tax Journal*.

Source: University of Missouri-Columbia (news : web)