CollegeBoard CSS Profile

PROFESSIONAL JUDGMENT TIP SHEET

TOPIC: Fluctuating Parent Income

What?

While it is common for parental income to change from one year to the next, most families will experience only modest changes. However, some families will have substantial yearly fluctuations in their income. This is often the case with business or farm owners. Annual fluctuations may also affect families who rely on seasonal income, work in sales, earn commissions, or who work in areas where there are frequent layoffs or employment uncertainty.

Why?

Institutional Methodology (IM) and Federal Methodology (FM) use the base year income in determining the family's financial need. The philosophy is that the base year serves as a proxy for determining the family's financial strength. For most families this is appropriate. However, when a family does not have a stable income, it can be difficult to adequately determine the family's ability to contribute to educational expenses.

How do I…..

Determine the approach to take?
Some institutions may decide to treat fluctuating income as a change in income. For these families, it may be reasonable to consider the options below:

- Use either recent year or anticipated year income (refer to "Alternate Year Parent Income" Tip Sheet), or
- Calculate the family's income over a period of years rather than focusing on a single year. It may be more appropriate to take the average of two or three years of income based on the institution's policy.

Collect information?
While there is no single way to document fluctuating income, many aid administrators ask the family to provide income information for the number of years the institution's policy dictates. Examples may include recent tax forms, pay stubs, an estimated income worksheet, etc.

Analyze the information?
If recent or anticipated year income is used, refer to the "Alternate Year Parent Income" Tip Sheet.

In examining the tax documents, determine if the fluctuation is from earned income or from the family's resources or assets. For example, interest or dividends may be the cause of the significant differences more than wages or business income.

Consequently, it may be more reasonable to understand the impact of a family's assets on their income.

If the fluctuation is from earned income and a decision is made to average income over a period of tax years, the key elements necessary for the need analysis calculation would be averaged, such as wages, AGI, taxes paid, etc.

Treatment in IM and FM

If a different income is determined to be more appropriate to use in the methodology, both IM and FM could be approached in a similar fashion.

Additional Considerations

If averaging multiple years, be mindful of the family's income trajectory. Averaging high income years when the family is at a much lower income may result in an unrealistic contribution from the family.

Consider the number of years to factor when using an average, taking into account the burden on the family of documenting multiple years of income and the institution's policy.

PROFESSIONAL JUDGMENT CASE STUDY

TOPIC: Fluctuating Income

The Specter family submitted a financial aid appeal based upon the family's widely fluctuating income over the past few years. The family's father Harvey, a Harvard Law graduate, was a name partner in the law firm Pearson, Specter, Litt. Located in New York City, Pearson, Specter, Litt was one of the city's largest law firms until one of their associate partners was sent to jail for fraud. After the conviction implicated many in the firm, business fled and it was ultimately forced to liquidate after a protracted effort to save the firm. While Harvey was a name partner at Pearson, Specter, Litt, he was highly compensated making $825,000 in 2015.

After the firm closed, Harvey decided to strike out on his own and open his own law office. He states in the appeal that because of the tarnished image remaining from his prior employment, business was slow to embrace the new firm. His wife Donna even returned to work as a legal secretary. Together they will make about $95,000 in 2016. He also states in the appeal that things will improve in 2017 when he expects to close some cases. The family is projected to make about $142,000 in 2017. Furthermore, between lifestyle expenses, starting a new law firm, and contributing a large amount of resources to a dying firm in hopes of saving it, the Specter family has few remaining assets. They show only $30,000 in cash, savings, and investments. They rent an apartment in Manhattan.

Decision

In review of the appeal, the financial aid administrator considered various options for addressing the Specter family's concerns related to their fluctuating income, particularly as it relates to their ability to contribute to current educational expenses. Four options were considered:

- Average income over three years (base, recent, and anticipated)
- Average income over two years (recent and anticipated)
- Use recent year income
- Use anticipated year income

The financial aid administrator decided not to average income over three years, as this would inflate the contribution expectations because of the unusually high income in the base year. In addition, since family income is expected to rise in 2017, the financial aid administrator chose not to average recent and anticipated year income, as this is not reflective of the family's current ability to contribute to educational expenses. For similar reasons, the financial aid administrator elected not to use recent year income.

Based upon the review of the Specter family's circumstances and institutional policy, the aid administrator decided to use the anticipated year income as the basis for the award. The institutional policy requires that when professional judgment for fluctuating income is used, income information in subsequent years is reviewed to determine the appropriate income year(s) to be used to calculate eligibility; as such, the aid administrator flagged this file.

Treatment in Methodologies

IM treatment

Whether the financial aid administrator uses the "Anticipated Year Income" option or overrides the values for adjusted gross income and income allowances, the standard IM treatment would use the base year tax tables to calculate a tax on the revised adjusted gross income (using the anticipated income calculation as defined by the IM rules).

Alternatively, a financial aid administrator could manually recalculate taxes paid using the recent or anticipated year tax tables. There is minimal change to the family contribution should a financial aid administrator choose to use the corresponding year tax tables. An analysis was done comparing tax rates over three consecutive years using the same income and the impact to the family contribution was negligible.

FM treatment

In FM, the financial aid administrator could utilize professional judgment and revise the adjusted gross income, wages, and taxes paid fields according to their institutional policy.

