STRETCHING YOUR FINANCIAL AID DOLLARS: ANOTHER LOOK AT INCOME VERIFICATION

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SECTION I

BACKGROUND

During the past five years, there has been a growing concern among financial aid administrators regarding the need to verify family financial information to insure that limited student aid dollars are awarded to the neediest students who would otherwise be unable to pursue postsecondary education.

As the newly appointed Director of Financial Aid at California State University, Long Beach in the Fall of 1971, I was one of the College Scholarship Service (CSS) users who shared this concern. Therefore, I recommended and received the approval of the University administration to institute a policy requiring all 1972-73 financial aid applicants who filed a PCS to submit a copy of their parents' 1971 Federal income tax return directly to the Financial Aid Office.

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Although no formal study was made of the impact of this policy on the 1972-73 aid applicant population, there was a decrease in the number of continuing students who reapplied and completed the application procedure by submitting a copy of their parents' Internal Revenue Service (IRS) Form 1040, particularly among those who had previously received aid solely under the College Work-Study Program. Among those new and continuing students who submitted the required IRS 1040 document, the number of reporting discrepancies discovered was sufficient to convince us that the time involved in the comparative review of the IRS and Parents Confidential Statement (PCS) documents was well spent and the policy should be continued during the 1973-74 application period.

The decision to continue the policy for 1974-75 did not fall upon the Long Beach campus. In the Fall of 1973, the Presidents of all nineteen campuses in the California State University and Colleges system were directed by The Trustees to require all dependent financial aid applicants to submit a copy of their parents' U.S. Individual Income Tax Return for the previous tax year in addition to submitting the PCS to the College Scholarship Service for processing. Verification of non-taxable income such as welfare and social security benefits was also required in lieu of the IRS Form 1040. Similar verification procedures were implemented for self-supporting Student Financial Statement (SFS) filers. (This directive resulted from a recommendation of the California State University and Colleges (CSUC) Trustees' Internal Audit Staff who had conducted reviews of several campus financial aid office operations during the Spring of 1973. Their report contained the following statement of concern: "The College Scholarship Service evaluates, without verification of truthfulness, the information furnished. . .")

Since Long Beach had now been involved in the IRS/PCS income verification process for two years, it seemed important to evaluate the results by means of an objective study with a view to forecasting what the implications might be for the CSUC system. Thus, when in the Fall of 1973 I learned of the CSS study underway on the *Accuracy of Parents' Taxable Income Reports for the* 1972-73 *Processing Year,* I decided to ask permission to replicate this study for purposes of comparing the Long Beach results with the CSS national sample. Agreement with CSS and the Educational Testing Services (ETS) was reached in the summer of 1974, and the study was begun with Mr. William D. Van Dusen serving as consultant.

METHODOLOGY

For purposes of this study, the following information obtainable from page one of the U.S. Individual Income Tax Return, IRS Form 1040, was compared with corresponding information provided by the family on the Parents' Confidential Statement:

1. Tax filing status (joint or head-of-household)
2. Number of dependent children
3. Number of other dependents

4. Income from wages, salaries, tips, etc.
5. Dividends and interest
6. Taxable income from all other sources
7. Business expenses
8. Federal income tax paid

Where differences occurred, the PCS information was changed to reflect the data appearing on the IRS form. The PCS was then recomputed to determine the change, if any, in the expected parental contribution.

Information indicating whether the PCS filing date occurred before or after the filing date reflected on the IRS Form 1040 was also recorded to determine whether parental reporting to CSS intended to be more accurate when the IRS Form 1040 had already been completed at the time the PCS data was provided.

SECTION II
Comparability of Parental Reporting of Data

INTRODUCTION

There were a total of 436 families included in this study. In reviewing the data which follow, it should be remembered that in many instances the number of families falling into a particular reporting group may be very small. For example, there were only 49 families who reported total income in excess of $15,000 and only 29 families who reported any income from a farm or business. While data are presented on the differences in reporting for groups such as this, care must be exercised in drawing conclusions about the level of accuracy which might be found if the sample were larger.

Comparisons will be provided for a similar study conducted during 1973-74 by James L. Bowman, Director of Financial Aids Studies and Programs for ETS, and reported in August 1974 (*The Accuracy of Parents' Taxable Income Reports for the* 1972-73 *Processing Year,* New York: College Entrance Examination Board). Bowman studied a sample of just under 2,000 families who submitted the Parents' Confidential Statement during the 1972-73 operational year and who also provided copies of their fiscal 1972 Internal Revenue Service Form 1040. He reported that his sample was representative of the general PCS filing population from which it was drawn.

NON-INCOME RELATED ITEMS

There were three items included in the data analysis which influence the amount of contribution expected from the parents which are not related to their income or expenses — the tax filing status (joint or head-of-household return), the number of dependent children, and the number of other income tax dependents (grandparents, grandchildren, etc.) Each of these influences the amount of the contribution.

The Long Beach population included a higher percentage of families filing as head-of-household than did the Bowman study. Among Long Beach families 19.5 percent were head-of-household returns and 80.5 percent joint. In Bowman's data 14.7 percent were head-of-household and 85.3 percent joint returns. The comparability of the data reporting, however, was similar in the two studies. Bowman found that 97.5 percent reported the same status to both IRS and CSS, exactly the same percent of comparability found in the Long Beach data. Only 0.7 percent of the Long Beach families reported joint returns to CSS and head-of-household returns to IRS; 1.8 percent reported head-of-household returns to CSS and joint returns to IRS.

A similar level of comparability of reporting was found in the number of dependent children. Bowman found that 91.5 percent reported the same number on the two forms while the Long Beach data showed that 91.4 percent reported the same number.

As the following table shows, 6.2 percent of the families reported more dependent children to CSS than they did to IRS, while 2.4 percent reported fewer to CSS. There is some supposition that the differences may be related to the regulations of IRS concerning claims of dependence for divorced or separated families. In many cases, the parent who has custody has agreed as a part of the divorce or separation that the other parent may claim the children for tax purposes.

Number of Children Reported to CSS	Percent of Sample	Percent Reporting to IRS		
		Fewer	Same	More
1	14.4%	—	96.8%	3.2%
2	24.3	2.8%	94.3	2.8
3	20.5	5.5	93.3	1.1
4	17.2	8.0	90.6	1.4
5	10.3	11.1	84.4	4.4
6 or more	13.2	15.5	81.1	3.4
All Families	100.0	6.2	91.4	2.4

The Long Beach data showed a high level of comparability in reporting the number of other dependents. Very few families reported any other dependents to CSS (only 7.1 percent), and nearly all (98.6 percent) reported precisely the same number to IRS. Bowman found a slightly lower percent of comparable reporting, 97.9 percent.

It would appear that there is little reason to question the accuracy of parental reporting of income tax filing status, number of dependent children, or number of other dependents when the CSS and IRS documents are compared.

COMPARABILITY OF REPORTED INCOME

The parental contribution used by Long Beach in the determination of need for financial assistance is determined by a combination of the income and assets of the family. For most families, however, the prime source for the contribution is the amount of their income. Differences in reporting income amounts and sources could have a significant impact on the amount that would be expected of the parents as a contribution toward the educational expenses of their children.

Under most circumstances, the parents' income from salaries and wages is the most important element of their income for computational purposes. The percent of Long Beach families reporting incomes in the same interval to CSS as to IRS (75.3 percent) is very close to that found by Bowman (76 percent). Among those families who report different amounts from salaries and wages on the two documents, the Long Beach sample differed from that of Bowman. He found that 9 percent of the families reported more to CSS than they did to IRS. Among the Long Beach sample, however, less than 2 percent reported more to CSS. Bowman found that 15 percent reported more to IRS than to CSS, the Long Beach data show nearly 23 percent in this group

Income from Salaries and Wages Reported to CSS	Percent of Sample	Percent Reporting to IRS Less	Same	More
Under $5,000	15.4%	—	73.1%	26.9%
$5,000 - $7,000	17.7	1.3%	68.8	29.9
$7,500 - $10,000	24.8	.9	71.3	27.8
$10,000 - $12,500	18.6	2.5	80.2	17.3
$12,500 - $15,000	18.6	2.5	78.7	18.0
$15,000 and Above	9.5	7.1	85.8	7.1
All Families	100.0	1.8	75.3	22.9

It is interesting to note that there is some tendency toward more comparability of reporting among the higher income families.

Only 6.9 percent of the Long Beach families reported any income from a farm or business. Among this group, 86.2 percent reported the same amount to CSS as they did to IRS, 6.9 percent reported more to CSS and 6.9 percent reported more to IRS. Because this group is so small, the comparisons of accuracy of reporting by income level could be misleading and are not included in this report.

Slightly more than one quarter of the Long Beach families (26.8 percent) reported income from dividends and interest to CSS. Of those who reported none to CSS, 11 percent did report some to IRS. Among those who reported any to CSS, 88.7 percent reported the same amount to IRS, 1.4 percent reported less to IRS, and 9.9 percent reported more to IRS. The following table shows the distribution of reporting by amount.

Dividends and Interest Reported to CSS	Percent of Sample	Percent Reporting to IRS Less	Same	More
None	73.2%	—	89.0%	11.0%
$1 - $250	17.3	1.3%	92.0	6.7
$250 - $500	3.2	7.1	78.6	14.3
$500 - $750	2.8	16.7	83.3	—
$750 - $1,000	.5	—	50.0	50.0
$1,000 and Above	3.2	14.3	85.7	—
All Families	100.0	1.4	88.7	9.9

The combined income from all taxable sources (salaries, wages, interest, dividends, and profit from farm or business) is the primary source to which Long Beach looks in determining the parental contribution. Among the study sample, 73.9 percent reported income in the same interval to CSS as they did to IRS, 23.3 percent reported more to IRS, and 2.8 percent reported more to CSS. Bowman found that 72 percent reported the same amount, 20 percent more to IRS, and 8 percent more to CSS.

Because these data are compared in intervals, they tend to mask the absolute accuracy of a parental reporting. Income reports which differ by as much as $2,499 *could* fall within the same interval. To eliminate this masking, an absolute difference was calculated by subtracting the IRS reported income from that provided to CSS. The following table shows the results of this calculation:

Total Income Reported to CSS	Percent of Sample	Exactly Equal	± $500	± $1,000
Under $5,000	10.5%	58.7%	63.1%	71.7%
$5,000 - $7,500	18.1	45.6	58.4	66.0
$7,500 - $10,000	25.0	47.7	60.5	72.4
$10,000 - $12,500	20.4	64.0	67.3	77.4
$12,500 - $15,000	14.7	62.5	70.4	75.1
$15,000 and Above	11.2	65.3	73.4	81.6
All Families	100.0	56.0	64.9	73.9

The percent of Long Beach families who reported exactly the same amount to both CSS and IRS is considerably higher than that found by Bowman. In his sample, only 26.9 percent reported exactly the same amount. Within the plus or minus differences of $500 and $1,000, however, the Long Beach data were nearly the same. Bowman found 60.4 percent within $500 and 71.8 percent within $1,000, as compared with 64.9 percent and 73.9 percent in the Long Beach data.

There are two other items which are common to the two forms and are available for comparison. Business expenses, which are a deduction from income in both the IRS taxing system and the CSS calculation system, were reported by 20 percent of the families on the PCS. Comparability of reporting was quite high, with 93.8 percent of families reporting the same amount to both CSS and IRS. This was a considerably higher percentage of accuracy than Bowman found. His data showed that 82 percent of the families gave comparable information to both sources. The other directly comparable item was the amount of federal income tax paid. The comparability of reporting on these data was lower, with only 37.9 percent reporting the same amount and 75.7 percent reporting amounts plus or minus $500. This lower accuracy is not surprising. The PCS asks the family to report the amount paid or "estimated to be paid." For all those who file the PCS before they file their IRS form, the amount of tax of necessity is an estimate. A subsequent section of this report will examine differences in reporting as a function of time of reporting.

SECTION III
Impact of Differences in Reporting On Calculations of Estimated Parental Contribution

While the absolute accuracy of reporting by parents on the College Scholarship Service Parents' Confidential Statement and the Internal Revenue Service Form 1040 is of some interest, for the purposes of awarding financial aid it is academic. The important question for the student aid officer is the impact that any differences in data submitted to the two sources would have on the amount that the aid officer would estimate that the parents could contribute toward the costs of postsecondary education. This involves calculation of the parental contribution with the different sets of data under common procedures and according to common formulae.

For the purposes of this study, the amount of parental contribution which would have been predicted by the College Scholarship Service on the basis of the data submitted on the Parents' Confidential Statement was compared with the amount which would have been calculated under the same procedures using the information provided on the IRS Form 1040. Information from the Form 1040 was transferred to the Parents' Confidential Statement and the estimated parental contribution re-calculated according to the same rules and procedures. This re-calculation included not only the information comparable between the two forms, but information submitted only on the Parents' Confidential Statement, such as residence equity, business and farm equity, value of investments, savings, etc.

The table on the following page shows the results of this re-calculation, and replicates Table 13 of the Bowman study with the exception that the parental income intervals have been truncated to reflect the differences in distribution of income in the Long Beach data (where there were considerably fewer families with incomes above $15,000 per year).

The Bowman study found that 18.9 percent of the cases would have resulted in exactly the same parental contribution if IRS data had been used. The Long Beach data shows a higher percentage of cases in which exactly the same contribution would have been calculated. Exactly one-third (33.3 percent) of the cases would have had the same calculation computed if

Calculated Amount of Parental Contribution Using IRS Data	Amount of Parental Income						
	Under $5,000	$5,000- $7,500	$7,500- $10,000	$10,000- $12,500	$12,500 $15,000	$15,000 or Above	All Families
Greater by							
Over $500	0.7%	2.5%	3.7%	2.8%	3.0%	0.6%	13.3%
$250 - $500	0.7	1.4	3.0	2.5	1.1	1.2	9.9
$100 - $250	0.2	1.8	4.8	3.4	1.8	2.2	14.2
$1 - $100	0.9	2.8	3.0	4.1	1.8	1.8	14.4
Equal	8.8	8.8	6.4	4.4	3.9	2.6	33.3
Less by							
$1 - $100	—	0.5	1.6	0.9	0.5	0.9	4.4
$100 - $250	—	0.9	0.9	0.5	1.1	0.5	3.9
$250 - $500	—	0.2	1.4	0.9	0.9	0.7	4.1
Over $500	—	—	0.2	0.9	0.5	0.9	2.5

IRS data were used. This is consistent with the Bowman data, however, Bowman found that greater comparability of contribution was found at the lower income levels. And the generally lower distribution of parental income in the Long Beach data would make this the expected result.

When cases where different levels of differences were found are compared, the Long Beach and Bowman data are quite comparable. For those with differences of plus or minus $100, the Long Beach data showed 52.1 percent within the interval and the Bowman data 50.1 percent. Differences of plus or minus $250 were shown in 70.2 percent of the Long Beach cases and 68.1 percent of the Bowman cases; differences plus or minus $500 in 84.2 percent and 82.1 percent respectively.

The following table shows the differences in expected parental contribution by income level. For all families, use of data from the IRS form would have resulted in awards lower by $250 or more in 23.2 percent of the cases. Awards greater by $250 or more would have been justified to 6.6 percent of the families. In about seven out of ten cases (70.2 percent) the awards would have been within $250 of that justified by use of the Parents' Confidential Statement data.

	Contribution Calculated With IRS Data		
Parental Income	Less by $250 or More	± $250	Greater by $250 or More
Under $5,000	—	86.9%	13.1%
$5,000 - $7,500	1.3%	77.2	21.5
$7,500 - $10,000	6.4	67.0	26.6
$10,000 - $12,500	9.0	65.2	25.8
$12,500 - $15,000	9.4	62.5	28.1
$15,000 and Above	14.3	69.4	16.3
All Families	6.6	70.2	23.2

SECTION IV

Differences in Reporting as a Function of Time

There are many reasons why information collected on the Parents' Confidential Statement and the Internal Revenue Service Form 1040 would differ. The IRS form is considerably more specific in its instructions as to what information is to be included, excluded, or reported in a particular way. The PCS instructions are not as extensive or specific. Parents may report the same information in different ways on the two forms, giving the appearance of reporting different information. For example, a divorced parent with custody of a child might be precluded from claiming the child as a tax dependent on the IRS form because of an agreement made as a part of the divorce but would consider that child as dependent according to the instructions on the PCS. Another reason might be "rounding," where a parent who earned exactly $9,783 as shown on the W-2 form might report $9,500 or $10,000 on the PCS. Yet another, and perhaps more logical, reason is timing.

The Parents' Confidential Statement is available and can be submitted early in the Fall. Although the Long Beach filing date was not until February 15, the required filing date of the California State Scholarship Program encourages early filing by candidates interested in state awards. For all those who file the PCS before they have completed their IRS form (or at least have the data available to complete their IRS form) the PCS data must of necessity be estimated. It might be expected that their estimates would vary from the data submitted on their Form 1040.

To invesigate the impact of time of filing on the comparability of data, the cases in the study group were identified as to whether the PCS had been filed before or after the date on the IRS form. The income and contribution of these two groups were analyzed separately.

As the following table shows, the accuracy of reporting total income is greatly enhanced if the PCS is filed after the IRS Form 1040. When the PCS was filed first, 41.5 percent of the families reported the same information. When the IRS form was filed first, that percentage was increased to 72.0 percent. The percent of families who under-report income on the PCS decreases from 53.8 percent when the PCS is filed first to 21.1 percent when the PCS is filed after the IRS form.

	When PCS is Submitted	
Income Reported to IRS	Before IRS	After IRS
Greater by		
More than $2,500	16.6%	7.7%
$2,000 - $2,500	3.1	.5
$1,500 - $2,000	3.9	1.9
$1,000 - $1,500	10.1	1.4
$500 - $1,000	10.5	4.8
$1 - $500	9.6	4.8
Equal	41.5	72.0
Less by		
$1 - $500	1.3	1.9
$500 - $1,000	.4	2.0
$1,000 - $1,500	.8	1.0
$1,500 - $2,000	.4	—
$2,000 - $2,500	.8	.5
$2,500 or Above	.9	1.4

These data are quite similar to those found in the Bowman study. His data indicated that 62.7 percent of reported income was plus or minus $1,000 when the PCS was filed before the IRS form, while the Long Beach data show that 63.3 percent fall in this group. Bowman found that 84.8 percent reported plus or minus $1,000 on the two forms when the PCS was filed after the IRS form, while the Long Beach families included 85.5 percent reporting plus or minus $1,000 under the same circumstances.

A corresponding increase in the comparability of calculated parental contribution occurs when the PCS is filed after the IRS form. Among the families filing the PCS first, 26.6 percent would have been calculated to make the same contribution had the subsequently submitted IRS data been used. When the PCS was filed after the IRS form, the same calculated contribution would have been produced in 40.6 percent of the cases. The following table show the differences in contribution which would have resulted:

Contribution Calculated Using IRS Data	When PCS is Submitted Before IRS	After IRS
Greater by		
More than $500	17.0%	9.2%
$250 - $500	14.0	5.3
$100 - $250	16.2	12.1
$1 - $100	14.0	15.0
Equal	26.6	40.6
Less by		
$1 - $100	4.4	4.3
$100 - $250	3.5	4.3
$250 - $500	3.1	5.3
$500 or Above	1.3	3.9

The fact that 41.6 percent of the cases would have resulted in a larger parental contribution if the IRS data had been used than was calculated on the basis of the PCS data even when the PCS was submitted after the IRS form indicates that time is not the only variable which influences the comparability of the two reports.

SECTION V

CONCLUSIONS

In summary, the California State University, Long Beach study of 436 families revealed that the accuracy with which parents report the same data to both the Internal Revenue Service and the College Scholarship Service is not very different from the national sample of 2,000 PCS filers included in the Bowman study for CSS. (An update of the Bowman study including 5,700 families — *Accuracy of Parents' Taxable Income Reports for the* 1973-74 *Processing Year* — also reflects results comparable to those reported here and in the previously cited Bowman study.)

Although it can be stated with considerable assurance that the majority of parents provide accurate information on the PCS, such assurance does not negate the importance of verifying data provided by *all* PCS or (American College Testing Program or Basic Educational Opportunity Grant BEOG) filers against either their State or Federal income tax reports. In their final analysis, the degree of accuracy in reporting data is only meaningful to the degree that the estimated parental contribution is affected. The fact that in 37.4 percent of the Long Beach cases the estimated parental contribution was increased by more than $100, yielded a saving of approximately $90,000 in Federal and State student aid dollars. Conversely, in 10.5 percent of the cases, the estimated parental contribution was decreased by more than $100 causing awards to be increased by approximately $30,000. Thus, the estimated overall savings in student aid dollars approximated $60,000. Since the maximum eligibility was only $1500 for a commuter student and $2000 for a resident student, the savings would have been even more substantial at a higher cost institution. Only by verifying the financial data provided by all financial aid applicants can we insure that limited student aid dollars will be equitably distributed and that the neediest students from low-income family backgrounds will be given the opportunity for both access and choice in postsecondary education.

It is encouraging to note that in recent months the need for verifying family financial data has been recognized at both the national and the state level.

The National Task Force on Student Aid Problems recommends that:

1. ". . .awarding agencies and institutions be strongly urged to verify appropriate financial data for the current year by use of state or federal tax statements.
2. ". . .need analysis services and state agencies which serve as processors provide extensive edit checks and diagnostic statements to financial aid officers to help them identify those applications which may need careful attention and follow-up for verification of data.
3. ". . .all agencies and institutions support the verification process by exchanging information appropriate to the administration of student aid. Legislatures should be urged to oppose laws that will limit this exchange. Laws should be passed to permit public agencies not directly involved with financial aid administration (e.g., state and local tax bureaus) to provide agencies and institutions with verification information.
4. ". . . applications for financial assistance beyond a student's initial year of postsecondary education should be based on and filed *after* the base year tax forms are completed.
5. ". . .the current efforts of the services to develop procedures and systems of verification and validation be continued and expanded as appropriate means of addressing these issues."

The *Master Plan for the Administration and Coordination of Publicly Funded Student Aid in California* (prepared by the California State Scholarship and Loan Commission for the State Legislature - June, 1975) contains the following recommendation:

> "The Scholarship and Loan Commission, in cooperation with representatives of the segments, students, and parents, should work with the Franchise Tax Board to develop procedures for verification of information submitted for the determination of financial need from California income tax returns with authorization from the taxpayer(s). The procedure for such verification should be developed to operate during the 1976-77 processing year for awards to be made for the 1977-78 academic year."

The "Dear Colleague" letter concerning the BEOG program dated August 25, 1975, contains the following announcement:

> "In order to obtain a better estimate of the degree of potential program abuse, as well as to test preliminarily some methods for detecting and correcting discrepancies, we have engaged a contractor to undertake these three activities:

1. Follow-up of applicants based on institutional referrals;
2. Follow-up of applicants selected from the Basic Grant applicants data base in accordance with pre-established criteria; and
3. A statistical study to determine the extent of misreporting under the Basic Grant Program."

Just as the need to complete separate application forms for different financial aid programs with different application filing periods has posed a barrier for some, the requirement to submit Federal or State income tax forms to different institutions and agencies at different points in time will only add to the confusion and may discourage some needy families from applying at all. Therefore, now that there seem to be a consensus that verification of reported income should be undertaken, it is of critical importance to develop a centralized verification procedure, coordinated with the processing of the common form for determining financial aid eligibility (for all student aid programs, *including BEOG*) according to the calender recommended by the National Task Force.

When this goal has been achieved, the financial aid application process will have been significantly improved. Such action will also assure all concerned parties that student aid awarded under the various Federal, State, and institutional programs will be based upon the same data, submitted at the same point in time, and verified against the same yardstick.