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ONE PAYMENT, TWO PAYMENTS, RED PAYMENTS, BLUE PAYMENTS:

Compliance with the Truth in Lending Act Obligations in the Drafting of Enrollment Agreements.

By Suzanne Garwood and Heather Broadwater

With families facing increasing financial pressure, many independent schools have worked to offer more flexibility in the payment of tuition and fees. Schools should be aware that the payment plans they offer may be considered loans under the federal Truth in Lending Act, and may trigger obligations to provide parents with consumer disclosures.

When asked to describe their schools, few independent school leaders would say “creditor.” Yet, “creditor” is the definition that the Federal “Truth in Lending Act” (TILA) applies to many independent schools, based on payment plans that allow parents to defer the payment of tuition. When schools meet the definition of “creditor,” they may be required by federal law to provide consumers with standardized disclosures summarizing the cost of credit extended. Therefore, it is critical that independent schools understand how TILA defines “creditor,” the disclosure obligations that attach when tuition payment plans qualify as “credit” under the TILAⁱ, and the penalties for failing to provide the required disclosures.

Is Your School a Creditor?

“Creditors” are persons or entities who regularly extendⁱⁱ “credit” of \$51,800ⁱⁱⁱ or less that is either subject to a “finance charge” or that is payable by written agreement in more than four installments. For purposes of this definition, “credit” means “the right to defer payment of debt or to incur debt and defer its payment.”^{iv} A “finance charge” is the cost of consumer credit as a dollar amount. It includes any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or a condition of the extension of credit. It does not include any charge of a type payable in a comparable cash transaction.^v Below we briefly explore what each of these definitional elements means in the context of tuition payment plans.

STEP #1: DETERMINE IF YOU DEFER TUITION PAYMENTS. The school needs to determine the date on which tuition is due and payable (e.g., the beginning of the school year). If a school permits parents to pay tuition after the date that tuition is due and payable, then the school must continue on to “step #2” to determine whether this deferral qualifies as “credit.” If a school does not permit parents to pay tuition after the due date, then the analysis stops here. The school is not offering credit and it does not qualify as a creditor for TILA purposes.

STEP #2: DETERMINE IF YOU CHARGE A FINANCE CHARGE. Generally speaking, a finance charge includes any amount that parents must pay because the parents have deferred the payment of tuition. Thus, a fee or charge paid by parents who pay tuition on the due date does not qualify as a finance charge. Examples of charges that are not finance charges include charges for books, lunch plans and fees. In contrast, an example of a fee that does meet the definition of a finance charge is a fee charged to those parents to use a third-party service to make the deferred tuition payments. If a school imposes a finance charge then the analysis stops here. The credit is covered by TILA, the school qualifies as a creditor and it must provide required disclosures. This conclusion is true irrespective of the number of payments that the parents make. If the school does not impose a finance charge on the tuition deferral, it must proceed on to “step #3” of the analysis.

STEP #3: DETERMINE THE NUMBER OF PAYMENTS. If the school does not impose a finance charge on the deferred payments, then it must determine the number of payments that the parents will make. Many schools offer two- and ten-payment plans. Because TILA applies only to plans that have more than four payments any two-payment plans (without a finance charge) are not covered by TILA. Ten-payment plans, however, irrespective of whether they are subject to a finance charge will be covered by TILA and the school will need to provide disclosures.

Thus, in sum, a deferral of tuition can become credit in one of two ways. First, the school can impose a finance charge; or, second, the school can permit the parents to repay in more than four installments. If the payment plan meets either of these criteria, then it will constitute credit under TILA and the school must provide the required disclosures.

What Does an Independent School Need to Disclose if it is a “Creditor?”

Assuming that the school qualifies as a creditor and the tuition payment plan it offers its parents qualifies as credit, then the school must provide the parents with clear and conspicuous disclosures of the cost of that credit in a form that the parents may keep (which may be either in paper or electronic) before consummation of the loan. “Consummation” is not defined under TILA; however it is generally understood to mean the time at which the borrower contractually obligates himself to the terms of the loan.^{vi} Generally speaking, this time will not include any rescission periods. The reason for this is because the goal of the law is to act as a shopping tool for the borrower. Accordingly, for certain mortgage loans, TILA makes clear that the rescission period follows both consummation and the providing of loan disclosures; and, while this provision does not expressly apply to tuition loans, the analysis should be the same.^{vii}

The content of the disclosures that schools must provide to students is as follows:

- Creditor – If the school is making the loan in its name, the school must identify itself as the person making the disclosure.
- Amount Financed – The school must disclose the amount of credit provided to the student or on the parent’s behalf along with the following descriptive sentence: “The amount of credit provided to you or on your behalf.” Typically, this amount would equal the amount of tuition due, and may also include any fees that the school is charging, but that are not finance charges.
- Note that if the school is offering financial aid, the amount of the aid may affect the amount financed. Said differently, if the amount of financial aid is known at or prior to the signing of the tuition contract, then the school should reflect the amount of the financial aid as a “credit” to the total of the amount financed. For example, if the school’s tuition is \$10,000 and the parent receives \$1,000 in aid, then the amount financed (or amount of credit provided) is \$9,000.

- **Itemization of Amount Financed** – The school may either provide a detailed description of the items that constitute the amount financed or ask that the parent request a copy. If the school opts to provide this disclosure, it must be separate from the other required disclosures.
- **Finance Charge** – The school must disclose the cost of credit as a numerical value using the term “finance charge” and a brief description, such as “the dollar amount the credit will cost you.” This disclosure must be “more conspicuous” than the others. To make the disclosure more conspicuous, the school can highlight this disclosure in bold.
- It is not required to use a larger font size.
- **Annual Percentage Rate** – The school must disclose the cost of credit as a percentage using the term “annual percentage rate” and a brief description, such as “the cost of your credit as a yearly rate.” Essentially, this disclosure is the disclosure of the finance charge as an annualized rate. And, similar to the finance charge disclosure, this disclosure must be “more conspicuous” than the others.
- **Payment Schedule** – The school must disclose the number, amount and timing of payments scheduled to repay the obligation. For example, the school may disclose a payment schedule of nine payments of \$1,000, each payment due on the first of the month.
- **Total of Payments** – The school must disclose the total of payments using that term and a descriptive explanation such as “the amount you will have paid when you (parents) have made all scheduled payments.” The total of payments equals the total of the amount financed plus the finance charge as disclosed according to the requirements set forth above.
- **Demand Feature** – The school must disclose if the loan has a demand feature (meaning that the school can require repayment prior to the term of the loan).
- **Prepayment Fees** – The school must disclose: (i) whether the loan contains a fee for prepayment of the loan prior to maturity; and (ii) a statement indicating whether the borrower is entitled to a rebate of any unearned finance charge if the borrower prepays the loan prior to maturity. A prepayment fee requirement would be rare in a school loan, and a school should consult state laws to ensure it has the authority to impose such a fee.
- **Late Payment** – The school must disclose if the loan imposes a fee upon a borrower’s late repayment of the loan. Again, the school should consult state laws to ensure that any late payment fees it imposes are consistent with state law.
- **Total Sale Price**. The school must disclose the total cost of the tuition including any downpayment. Thus, if a student is required to give a downpayment, the amount of that downpayment should be subtracted from the total “sale price” or amount of tuition due.

Although the disclosure obligations may appear complex, Regulation Z, the implementing regulation to TILA, provides model forms for providing these disclosures. Use of these model forms constitutes a safe harbor in litigation. However, schools must ensure that the numerical values that constitute the actual prices contained in the disclosures are accurate. Software packages are available to assist schools with calculating these values.

What Are the Penalties for Failing to Provide Disclosure?

TILA provides for a private right of action (enabling parents to bring a suit against the school), as well as criminal penalties. Aggrieved borrowers (parents) can sue schools that fail to provide disclosures, or who provide disclosures that are inaccurate, for statutory and actual

damages in an individual or class action. Successful plaintiffs are entitled to attorney's fees and costs.

The amount of statutory damages available in an individual action is capped at \$2,000. Class-action damages are capped at \$1 million. Parents must bring action within a one-year statute of limitations.^{viii}

Given the potential penalties for failing to provide the disclosure required by TILA, independent schools should review their tuition payment plans to determine whether they may meet the definition of "creditor" under TILA, and whether they are meeting TILA's disclosure requirements. Schools with questions about TILA coverage and obligations, or schools wishing to explore how they might revise their tuition payment plans to avoid falling under the definition of "creditor" should contact their Venable independent school attorney for further discussion.

ⁱ 15 U.S.C. §§ 1601 et seq.

ⁱⁱ A person "regularly extends credit" if he extended credit more than 25 times in the preceding (or current) calendar year. 12 C.F.R. § 1026.2(a)(17) n. 3.

ⁱⁱⁱ This dollar value is adjusted on an annual basis.

^{iv} 12 C.F.R. § 1026.2(a)(14).

^v 12 C.F.R. § 1026.4(a).

^{vi} "Consummation" means the time that a consumer becomes contractually obligated on a credit transaction. 12 C.F.R. § 1026.2(a)(13). The Commentary explains "[w]hen a contractual obligation on the consumer's part is created is a matter to be determined under applicable law; Regulation Z does not make that determination." 12 C.F.R. Off. Staff Comm. § 1026.2(a)(13) – 2.

^{vii} 12 C.F.R. § 1026.23. "The consumer may exercise the right to rescind until midnight of the third business day following consummation, delivery of the notice . . . or delivery of all material disclosures."

^{viii} 15 U.S.C. § 1640.

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