Are Your Enrollment Agreements Creating More Liability Than Revenue?

Insights
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Running a school has become more regulated and difficult. As we look at the creative ways that schools structure enrollment contracts and encourage early payment or accommodate payments over time, many schools may be surprised to learn that their enrollment contracts may violate federal law and possibly create substantial liability.

Although many people have heard of the Truth-in-Lending Act (TILA), most associate it with federal home mortgage programs. But if your enrollment agreement has finance charges, such as tuition discounts, administrative fees, outside tuition management costs, or defers tuition over more than four payments, your contract is subject to the disclosure requirements of Truth-in-Lending. This article will address the specifics of the law, the potential liability for non-compliance, and help schools understand how to opt out or comply.

What Is Truth-In-Lending?

TILA is a federal law that requires certain disclosures to parents (called "consumers") if the school is a "creditor" under the law. A school becomes a "creditor" if: 1) it regularly extends credit (allows parents to defer payment beyond the due date); and 2) the credit is *either* a) subject to a "finance charge" *or* b) payable by written agreement in "more than four installments" (not including a down payment).

The concept of a finance charge is broad under this law. It includes any charge payable directly or indirectly as a condition for the extension of credit. Some examples include administrative/service charges for more than one tuition payment; discounts systems encouraging one tuition payment or early payment; interest; fees charges by tuition management companies; credit report fees, and other fees.

Discount systems are common in enrollment contracts. For example, many schools charge parents less if the parent pays the full cost of tuition up front in one payment. The school then charges slightly more for two payments; and more yet for four, eight, or ten payments. Those differences in the cost of tuition constitute finance charges.

There are certain charges or discounts that are not considered finance charges. For example, enrollment/re-enrollment fees, application fees, fees for unanticipated late payment or delinquency, or discounts to induce payment by a means other than the use of credit (i.e., permitting all payers who elect to pay by cash rather than credit card to take a discount). Also, other forms of discounts that are applicable to all parents regardless of payment plan selected are not finance charges. For example, tuition discounts for more than one child or early enrollment discounts available to all families (regardless of payment plan selected).

When Does TILA Apply?

If the enrollment contract has charges or discounts that fall within the definition of "finance charges," or if the enrollment contract permits payment over more than four payments (not counting the initial enrollment fee or deposit), then the contract falls within the parameters of TILA and the school must give the parent a Truth-in-Lending Disclosure (Regulation Z Form) at the time the transaction is consummated (i.e., when the agreement is signed). This means that the school will need to know at the time of enrollment or re-enrollment whether the transaction will fall within TILA.

This is not an exercise to be taken lightly. There are very specific requirements for what must be included on the disclosure form. In addition, you will have to know how much is being financed and which payment plan is being elected before you can create the form. Unless you "opt out" of TILA (discussed below), compliance will likely require a two-step enrollment process since most schools provide parents with a range of options to choose from. The parent will have to initially opt for the particular payment plan and then the school can create the enrollment agreement and disclosure form.

Moreover, you should use language in the enrollment contract that matches language in the TILA disclosure form. The purpose of TILA is to bring transparency and clarity to the lending process so parents can see exactly how much the "loan" is costing them. Therefore, anything that falls within the definition of "finance charge" should be clearly designated as a "finance charge" so the parent can match the information with the disclosure form.

The FDIC (the agency that enforces the law) has model disclosure forms which can be found on their website. You should check with your tuition management company to see whether they can or will create these forms for you.

Opting Out Of TILA

The school can avoid TILA obligations by structuring its enrollment agreements to eliminate finance charges and to ensure that the number of payments does not exceed four (after the enrollment fee/deposit). This means that all of the creative discounts, charges, fees, and other items will need to be evaluated by your attorney and removed if they fall within the definition of "finance charge."

In addition, the school will need to eliminate the six-, eight-, ten-, and twelve-payment plans. Instead, the school should move to one-, two-, or four-payment plans. The four-payment plan can still be stretched over the course of the year to help reduce parental anxiety and financial strain (i.e. by requiring the enrollment fee/deposit in February; first payment in June; second payment in September, third payment in December; and fourth payment in March), or something similar.

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If you choose to opt out, you should begin planning now to avoid unpleasant surprises for your parent community. Tell them well ahead of time that the school will no longer permit more than four payments of tuition throughout the school year. You don't need to give your parent community all of the reasons, but should give them enough information to plan their payments. You can also explore financial institutions that may partner with your school to offer to finance parent tuition. This removes you from the practice of being a lender to parents (by deferring tuition payments over the full year and then having to manage the collection).

Penalties For Noncompliance

Although there is still little knowledge of these obligations in the independent school world and there may be arguments that your lawyer can make for why your school should not have to comply, if a court finds that the school should have complied, damages can be substantial. TILA provides for actual damages (if any), statutory damages in the amount of two times the amount of any finance charges, with a minimum of $400 and a maximum of $4,000, plus attorneys' fees and costs.

But the real problem is that the law permits class actions, with the amount of damages to be assessed within the discretion of the court, with a cap at $1 million or 1% of the school's net worth. This is what will motivate attorneys to take the case.

TILA is not a hard law to comply with, although it will require some pre-planning and reworking of your enrollment agreement. Now is the time to make decisions regarding what your school should do and get your enrollment contracts revised so that by the time you begin issuing them, you and your parent community will be ready for the change.

For more information or assistance in complying with TILA, contact the author at SBogdan@fisherphillips.com or 954.525.4800.

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