

UNITED STATES DEPARTMENT OF EDUCATION
WASHINGTON, D.C. 20202

In the Matter of

Docket Nos. 98-72-SA & 98-73-SA

CANNELLA SCHOOLS OF HAIR DESIGN,

Consolidated Student Financial Assistance Proceedings

Respondents.

ACNs: 05-96-74212 & 05-96-74207

Appearances: Stanley A. Freeman, Esq., and Joel M. Rudnick, Esq., Powers, Pyles, Sutter, & Verville, P.C., for Respondents.

Alexandra Gil-Montero, Esq., Office of the General Counsel, U.S. Department of Education, for Student Financial Assistance Programs.

Before: Frank K. Krueger, Jr., Administrative Judge.

DECISION

The Respondents are two cosmetology schools owned by the same individual and separately eligible to participate in the programs authorized under Title IV of the Higher Education Act of 1964, as amended _ the Cannella School of Hair Design, located at 3646 N. Broadway, Chicago, Illinois, and the Cannella School of Hair Design, located at 5912 W. Roosevelt Road, also in Chicago, with a branch at 12840 South Western Avenue, Blue Island, Illinois. This case involves appeals by the Respondents from final audit determinations made by the Student Financial Assistance Programs (SFAP), U.S. Department of Education, concerning the 1995-96 award year and the Pell Grant program. SFAP assessed liability of \$3,775 concerning the Broadway school and \$14,689 concerning the Roosevelt school. Neither school participated in the Federal Family Education Loan program during the award year at issue.

SFAP contends that Respondents improperly excluded the full cost of books, equipment, and other supplies from *pro-rata* refund calculations. For the reasons discussed below, I find in favor of the Respondents.

FACTS:

Students attending the Respondent schools were required to purchase certain books, equipment, and other supplies necessary to participate in the training program. (See Respondents' Exhibit 10-004 for a complete list.) Although the schools made it clear that a student was required to have the necessary supplies at the beginning of the program, and made the supplies available for purchase directly from the school in a supply kit, the students were given the option of purchasing the materials from an outside source. The schools did not include a charge for the supply kit in the student enrollment agreements. Prior to enrollment, the schools presented each student with an "Equipment Acknowledgment" form which notified the student that he or she was not required to purchase the supplies from the school, but could purchase the supplies from an outside source. The form read as follows:

I understand that the fees associated with books, required equipment and chemicals are not being charged to me directly by Cannella School of Hair Design. . . . I further understand that these fees are optional and will be incurred if I elect to purchase such books, equipment and chemicals from Cannella School of Hair Design. . . . I understand that I have the option of purchasing the required books, equipment and chemicals from an outside source, and should I choose to do so, I agree to have a complete set of books, equipment and chemicals prior to the beginning class at Cannella School of Hair Design. . . .

I choose to purchase my books, equipment and chemicals from Cannella School of Hair Design. . . . I understand that the cost of these items is separate from and in addition to my other course costs, and is not refundable except under the circumstances described in the school's refund policy. The cost is: \$600.00

I choose to purchase my books, equipment and chemicals from an outside vendor, such as Sally Beauty Supply or Marianna, etc.

See, e.g., Respondents' Exhibit 6-002. The remainder of the document repeated the same information in Spanish and had a line for the student's signature and date.

Although no student during the year in question elected to purchase the required supplies from an outside vendor, the Respondents' Director of Financial Aid stated that, if a student elected to purchase the supplies elsewhere, the schools would provide the student with a check drawn from the student's Pell Grant or the student would pay for the supplies using his or her own funds. Declaration of David R. Adams, Respondents Exhibit 2-002. There were a number of vendors located within 10 to 20 blocks of each school from which the students could purchase the required supplies. *Id.* at 2-002 - 2-003. There were over one hundred such stores in the Chicago metropolitan area. *Id.* and Declaration of John Kungis, Manager, Cannella School of Hair Design, Respondents' Exhibit 10-001. The cost of the required supplies when purchased from the Respondent schools was competitive with the cost of the supplies when purchased from an outside vendor. *See* Respondents Exhibit 10-002.

If a student dropped out of the Respondent schools, the entire costs of the supply kit was excluded from the *pro-rata* refund calculation. SFAP contends that this practice violates the Title IV regulations.

REGULATORY STANDARDS

The applicable regulation, at 34 C.F.R. § 668.22 (1995), provides as follows:

(c) *Pro Rata refund.* (1) “*Pro rata refund,*” as used in this section, means a refund by an institution to a student attending that institution for the first time of not less than that portion of the tuition, fees, room, board, and other charges assessed the student by the institution equal to the portion of the period of enrollment for which the student has been charged that remains on the withdrawal date

(5)(i) For purposes of this section, “other charges assessed the student by the institution” include, but are not limited to, charges for any equipment (including books and supplies) issued by an institution to the student if the institution specifies in the enrollment agreement a separate charge for equipment that the student actually obtains or if the institution refers the student to a vendor operated by the institution or an

entity affiliated or related to the institution. [Underlining added.]

When this regulation was published in final, the preamble provided as follows:

Comments: One commentator suggested that the definition of “other charges assessed by the institution” not include the documented cost for services provided by the institution as a convenience to the student. For example, a book charge would not be an institutional charge if the institution permitted the purchase of the books as a convenience and the book charge was not included in the enrollment agreement.

Discussion: The Secretary [of Education] notes that . . . an institution is required to include the full amount of charges for equipment in the calculation of a pro rata refund if a separate charge exists for the equipment by the institution or if the institution requires the student to purchase the equipment from a certain vendor. If an institution does not have a separate charge for equipment and the student has the option of purchasing the equipment from more than one source, the institution would not have to include the equipment charge in the pro rata refund calculation.

59 *Fed. Reg.* 61163 (November 29, 1994) underlining added.

The 1995-96 *Federal Student Aid Handbook*, at 3-85, provides as follows:

Usually, if the student purchases the item from the school, it's an institutional cost. However, ED has determined that if the student has a real and reasonable opportunity of obtaining the items (such as books) elsewhere, and only chooses to get them at the school as a matter of convenience, the cost is a noninstitutional charge.

DISCUSSION

Respondents were in compliance with all applicable regulations and guidelines. Under 34 C.F.R. § 668.22, Respondents were obligated to include in their pro-rata refund calculations “tuition, fees, room, board, and **other charges assessed.**” “Other charges assessed . . . include, but are not limited to, charges for any equipment (including books and supplies) . . . if the institution specifies in the enrollment agreement a separate charge for equipment . . . or if the institution refers the student to a vendor operated by the institution or related to the institution.” Under the clear language of the regulations, “other charges” must be included in the refund calculations if one of two conditions are present _ (1) the enrolment agreement specifies a separate charge or (2) the student is referred to a vendor operated by or related to the institution. This reading of the regulation is consistent with the preamble to the regulation quoted above. In the present case, the enrollment agreements did not contain a separate charge for the supply kit; and the students were not referred to outside vendors operated by or related to the Respondents.

SFAP contends that, since the definition of “other charges” includes the language “but are not limited to,” there may be other unspecified conditions which dictate the inclusion of equipment and supplies in the refund calculation. In other words, even if a school, as Respondents in the present case, does not specify a separate charge for equipment and supplies in the enrollment agreement, and does not refer students to outside vendors operated by or related to the school, the cost of equipment and supplies must still be included in the refund calculation if certain other unspecified conditions are present. SFAP contends that the two conditions specified by the regulation are mere examples and simply provide a framework and are not meant to be exclusive.

Given this framework, in a case such as this where the charges do not fall under either example, we must examine whether the charges represent federal student aid funds paid directly to the institution or whether they were instead paid directly to the students as non-institutional charges.

SFAP misreads the regulation. The “not limited to” language means that “other charges” may include items other than “equipment.” When “other charges” include “equipment” the other charges must only be included in the *pro-rata* refund calculation if one of the two stated conditions are met. The contention that the specified conditions are “examples” and that, if the charges questioned do not fall within either of the examples, we must still examine whether the charges represent Federal funds paid directly to the school is sophistry. Under the clear language of the regulation, if the charges in question do not fall within the “examples,” then the charges need not be included in the refund calculation. The regulation does not state, as SFAP apparently wishes it did, that all Federal payments made directly to a school must be included in refund calculations.

SFAP also contends that Respondents are not in compliance with the *Federal Student Aid Handbook* quoted from above _ namely, that their students did not have a “real and reasonable” opportunity to purchase the required equipment and supplies elsewhere and only chose to purchase them from the school as a matter of convenience. As evidence of this contention, SFAP points out that no students elected to purchase the equipment and supplies from an outside source and that Respondents never made Federal funds available to the students for such purchases. The fact that no students elected to purchase the required equipment and supplies from outside sources is not dispositive. There were a number of retail outlets within ten to fifteen blocks of the schools, and over one hundred such sources in the Chicago metropolitan area, from which the required materials could have been purchased. The schools were not charging prices which were much different from those charged by the retail outlets. Under the circumstances, it is clear that the students purchased the required materials directly from the schools as a matter of convenience, avoiding the hassle of traveling to a retail supplier to purchase the same materials for approximately the same price. As stated by Mr. Adams,

Students purchasing the necessary supplies elsewhere would have to make a separate trip to one or more of the nearby beauty supply stores, locate and acquire the numerous required separate items of equipment, and bring their supplies to the school. Students purchasing equipment directly from Cannella received their supplies at one time, at the school, assembled and packaged largely in one box.

Respondents' Exhibit 2_003. *See also* Respondents' Exhibit 10-003. According to Declaration of Mr. Adams, had a student elected to purchase the equipment and supplies from an outside source, Respondents would have provided the student with a check drawn on the student's Pell account. Respondents' Exhibit 2-002. Although SFAP dismisses this statement as “self- serving,” there is no contrary evidence in the record and I must accept it as true. Given the convenience of purchasing the supplies and equipment directly from the schools, I do not find it unusual that no students elected to purchase the supplies from outside sources.

CONCLUSION

Respondents were in full compliance with all applicable regulations and guidelines when excluding the full costs of their supply kit from *pro-rata* refund calculations for the 1995-96 award year. Accordingly, Respondents have no further liability under the final audit determinations issued in this case.

Frank K. Krueger, Jr.

Administrative Judge

Date: February 22, 1999

SERVICE

A copy of the attached initial decision was sent by registered mail, return receipt requested, to the following:

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