Pomp and Circumstances, Part I: Education Loans

James F. Molleur, Moderator
Molleur Law Office; Biddeford, Maine

Prof. Daniel A. Austin
Northeastern University School of Law; Boston

Hon. Mildred Cabán
U.S. Bankruptcy Court (D. P.R.); San Juan

John Rao
National Consumer Law Center; Boston

Anne J. White
Demeo LLP; Boston

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"UNDUE HARDSHIP": STANDARDS AND CASE LAW UNDER 11 U.S.C. §523(a)(8)

Daniel A. Austin
Northeastern University School of Law
d.austin@neu.edu

Section 523(a)(8) exempts education loan debt from discharge unless the debtor establishes that paying the debt would result in "undue hardship" on the debtor and the debtor's dependants. The term "undue hardship" is not defined in the Code, and bankruptcy courts have devised different tests to determine whether a debtor's circumstances constitute undue hardship.

(i) The *Brunner* Three-Part Test

The majority of courts have adopted the "*Brunner* test" to determine undue hardship. The test is from the Second Circuit case of Brunner v. New York State Higher Educ. Servs. Corp.[1] *Brunner* set forth a three-part test under which the debtor must prove:

> (1) That the debtor cannot maintain, based on current income and expenses, a "minimal" standard of living for herself and her dependents if forced to repay the loans; (2) that additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans; and (3) that the debtor had made good faith efforts to repay the loan.[2]

The *Brunner* prongs are conjunctive, so that judgment must be entered against the debtor if he fails any one of the three requirements, even if any of the others are satisfied.[3] Most jurisdictions have adopted the *Brunner* test, including the Third,[4] Fourth,[5] Fifth,[6] Sixth,[7] Seventh,[8] Ninth,[9] Tenth,[10] and Eleventh Circuits.[11]

Brunner first prong:

The first prong of *Brunner* is that the debtor must prove that with his current income and expenses, he cannot maintain a "minimal standard of living" if forced to repay student loans. One factor in this determination is whether the debtor is maximizing his income and minimizing

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[1] 831 F. 2d 395 (2d Cir. 1987).
[2] *Id*., 831 at 396.
[3] Fabrizio v. U.S. Dept. of Educ. Borrower Services (In re Fabrizio), 369 B.R. 238, 244 (Bankr. W.D. Pa. 2007).
[4] Pa. Higher Educ. Assistance Agency v. Faish (*In re* Faish), 72 F. 3d 298, 306 (3d. Cir. 1995); *cert denied*, 518 U.S. 1009 (1996).
[5] *In re* Frushour, 433 F. 3d 393 (4th Cir. 2005); United Student Educ. Res. Inst. (*In re* Ekenasi), 325 F. 3d 541, 546 (4th Cir. 2003).
[6] U.S. Dept. of Educ. v. Gerhardt (*In re* Gerhardt), 348 F. 3d 89, 51 (5th Cir. 2003).
[7] Oyler v. Educ. Credit Mgmt. Corp. (*In re* Oyler), 397 F. 3d 382, 385 (6th Cir. 2005).
[8] *In re* Roberson, 999 F. 2d 1132 (7th Cir. 1993).
[9] United Student Aid Funds, Inc., v. Pena (*In re* Pena), 155 F. 3d 1108, 1112 (9th Cir. 1998).
[10] Educ. Credit Mgmt. Corp. v. Polleys, 356 F. 3d 1302, 1309 (10th Cir. 2004).
[11] Hemar Ins. Corp. v. Cox (*In re* Cox), 338 F. 3d 1238, 1241 (11th Cir.), *reh'g denied*, 82 F. App.'x 220 (11th Cir. 2003), *cert. denied*, 541 U.S. 991 (2004).

expenses.[12] As part of maximizing income, the debtor must look for a job in any field, not just the one for which the debtor trained or prefers.[13] In considering whether the debtor has minimized expenses, courts look to whether the debtor is in "self imposed hardship" due to unnecessary expenses – *i.e.*, the extent to which the debtor's inability to pay creditors is caused by the debtor's own spending on extraneous expenses.[14] Luxury spending or unreasonable amounts spent on otherwise reasonable expenses (including food) may show that the debtor is able to maintain a minimal standard of living even with loan payments.[15] The relevant date for determining the minimal-standard-of-living element is the date of trial.[16]

The Bankruptcy Code does not define what constitutes a "minimal standard of living." An oft-cited opinion, *In re* Ivory,[17] defines it as follows: (1) shelter (including heating and cooling); (2) basic utilities such as electricity, water, natural gas, and telephones; (3) food and personal hygiene products; (4) vehicles, along with insurance, gas, licenses, and maintenance; (5) health insurance or money to pay for healthcare; (6) some amount of entertainment or diversion, even if only a television or a pet.[18] While the *Ivory* list is often referenced by other courts, it need not be applied mechanically:

> Rather, in appropriate circumstances, the court must be prepared to depart from the list based on its own experiences, common sense, knowledge of the surrounding area and culture, and assessment of the reasonableness of what debtor claims he or she needs. In addition, what is minimal can and probably should change over time, *e.g.*, with new technology driving down the cost of things that might have previously been cost prohibitive.[19]

Although "minimal standard of living" is not supposed to mean that the debtor live in poverty, "it does mean that the debtor is expected to do some financial belt-tightening and forgo amenities to which he may have become accustomed."[20] But standards can change with time. In recent years, courts have found that standard expenses for cell phones, cable and internet are basic and reasonable expenses.[21]

Brunner second prong

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[12] Nixon v. Key Educ. Resources (*In re* Nixon), 453 B.R. 311, 327-328 (S.D. Ohio 2011).
[13] Tirch v. Penn. Higher Educ. Assistance Agency (*In re* Tirch), 409 F. 3d 677, 681 (6th Cir. 2005) ("Tirch should have sought employment in another field when the stress of clinical social work became debilitating"); *In re* Healey, 161 B.R. 389, 395 (E.D. Mich. 1993) (a debtor cannot ignore reasonable options in other fields in order to work in one's "field of dreams").
[14] Educational Management Corp. v. DeGroot, 339 B.R. 201, 208 (D. Ore. 2006). The court also found that as the debtor had a three-bedroom house and no dependents, she should have taken on a roommate to share expenses. *Id.* at 210.
[15] Mandala v. Educ. Credit Mgmt. Corp. (*In re* Mandala), 310 B.R. 213, 221-22 (Bankr. D. Kan. 2004) (holding that debtors could maintain minimal standard of living if they adjusted expenses, including food expenses).
[16] *In re Nixon, supra,* 453 B.R. at 326.
[17] Ivory v. United States (*In re* Ivory), 269 B.R. 890 (Bankr. N.D. Ala. 2001).
[18] *Id*. at 899.
[19] Miller v. Sallie Mae, Inc. (*In re* Miller), 409 B.R. 299, 312 (Bankr. E.D. Pa. 2009).
[20] Campton v. U.S. Dept. of Educ. (*In re* Campton), 405 B.R. 887, 891 (Bankr. N.D. Ohio 2009).
[21] *See e.g., In re* Nixon, *supra,* 354 B.R. at 329 (holding that telecommunications expenses are reasonable to permit debtors to have a source of entertainment, apply for employment online, and to communicate).

To meet the second prong of *Brunner*, the debtor most present "additional circumstances" that show the state of affairs is likely to persist for a significant portion of the repayment period. In essence, the debtor must demonstrate that "circumstances indicate a certainty of hopelessness, not merely a present inability to fulfill financial commitment."[22] This has been described as "the heart of the *Brunner* test… and is difficult to prove because it requires the debtor to show that she will be unable to repay her student loan debt in the future for reasons outside her control."[23]

The debtor may try to show a variety of causes, such as illness, disability, lack of job skills, or a large number of dependants. The most common type of additional circumstance supporting undue hardship discharge appears to be medical-related issues, such as chronic mental or physical ailments that interfere with the debtor's ability to work and generate income. Depression caused by debt, without more, generally does not suffice.[24] Ultimately, however, "the most important factor in satisfying the second prong is that the additional circumstances must be beyond the debtor's control, not borne by free choice."[25] A debtor who left a well-paying nursing career at age 45 to enter chiropractic school could not complain that, at age 54, the profession did not provide enough income for her to repay her student loan debts within her lifetime.[26] In another case, a debtor, an adjunct professor, refused to apply for permanent work at other schools because she deemed them too far from her home, even though the increased income would more than offset extra transportation costs.[27]

But not all choices are necessarily *free* choice. Where a debtor discontinued her studies twenty-five years previous in order to care for her infirm parents, the court characterized her decision as a *moral* choice, not a choice to be poor.[28] In another case, a debtor incurred $200,000 of student loan debt for undergraduate and medical school, but by the time of her bankruptcy petition, had became a full-time stay at home mother with five young children, including two special needs children.[29] The debtor met the second prong of *Brunner*. As the court stated, "[t]his is not a case in which a debtor willfully chose to avoid payments that could have been made or was underemployed or unemployed for no discernible reason. Caring for her five young children has become Walker's full-time occupation."[30]

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[22] Barrett v. Educ. Credit Mgmt. Corp. (*In re* Barrett), 487 F. 3d 353, 359 (6th Cir. 2007).
[23] *In re* Matthews-Hamad, 377 B.R. 415, 422-23 (Bankr. M.D. Fla. 2007).
[24] Katheryn E. Hancock, *A Certainty of Hopelessness: Debt, Depression, and the Discharge of Student Loans Under the Bankruptcy Code*, 33 Law & Psychcol. Rev. 151, 162 (2009) (analyzing mental health as a factor in student loan debt discharge cases).
[25] *In re* Barrett, *supra*, 487 F. 3d at 359.
[26] *In re* DeRose, 316 B.R. 606 (Bankr. W.D.N.Y. 2004)
[27] *In re* Gipson, 2012 Bankr. LEXIS 2745 at *7-*9 (Bankr. D.Md. 2012). The debtor also refused to reactivate her law license to seek work in law, which would provide more income, for the reason that "I'm not interested in being an attorney. I do not consider myself an attorney. I am an educator." *Id.* at *11. *See also, In re* Nixon, *supra* 453 at 331 (Bankr. S.D. Ohio 2011) (holding that debtor could not satisfy the second prong of Brunner without looking for all possible teaching positions).
[28] *In re* Bene, *supra*, 2012 Bankr. LEXIS 2914 at *11-*12.
[29] Sallie Mae v. Walker (*In re* Walker), 650 F. 3d 1227 (8th Cir. 2011).
[30] *Id.* at 1234.

The distinguishing element in these cases is whether the debtor has options that could increase income or decrease expenses.[31] Changing patterns of income to care for elderly parents or raise children were found to not constitute free choice, whereas personal career changes or preferences were. In addition, the time frame of the choice, *i.e*., a recent choice of the debtor or one in the distant past, can also be a consideration.[32]

Less frequently, the *Brunner* second prong can also be met where a debtor has been unable to find employment despite sustained and diligent efforts. The standard is strict. In one case, a pro se debtor had trained a paralegal, but for ten years had sought unsuccessfully to land any type of a job.[33] The court, having the observed at trial the debtor's demeanor, body language and overall attitude, could not help but be moved: "[s]he has clearly been worn down by the difficulties she has experienced, and it shows."[34] The court then noted the exceptional circumstances in which a debtor's history of failure to secure employment might justify a finding that the second prong of *Brunner* was met:

> Rarely has the Court seen the kind of persistent search efforts in which the debtor has engaged over the past decade. Never had the court seen such utter futility be the result of a debtor's job search efforts. This debtor is truly destitute and has been in these straits for many years without respite. *** If the term "certainty of hopelessness" is to ever have any application, it is in this case.[35]

It is unclear the extent to which a debtor's advanced age may constitute an "additional circumstance" to satisfy the second prong of *Brunner*. In *Brunner*, the court held that no additional circumstances exist where the debtor "is not disabled *nor elderly*."[36] One court cited the debtor's age (early fifties) as limiting her earning capacity and thus her ability to afford loan repayment.[37] However, other courts have held that people who take on education debt at an older age do not suffer undue hardship because they owe debt into their retirement age,[38] even if the debtor asserts he will be unable to pay the loan in their lifetime.[39]

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[31] *See In re* Bene, *supra* 2012 Bankr. LEXIS 2914 at *36-*37 (noting that moral choices made a long time ago are different from lifestyle options that the debtor can feasibly modify after bankruptcy).
[32] *Id. at* *36. In *Bene*, the debtor, who was 64, had worked on an assembly line for 12 years, but with the plant closing and no other skills or degree, the court found that the debtor "had no choice, and has not had a choice for a very long time." *Id.* at *36.
[33] Krieger v. Educ. Credit Mgmt. Corp. (*In re* Krieger), 2012 WL 1155687 *5 (Bankr. C.D. Ill. 2012), *aff'd* 2013 WL 1442305 (C.A. 7 (Ill.) April 10, 2013) ("the [*Brunner* second prong] determination is based on the Court's judgment about whether and where this particular debtor is likely to work in the future and what she is likely to earn in the future").
[34] *Id*. at *6.
[35] *Id.* at *6.
[36] Brunner, 831 F. 2d at 396 (emphasis added).
[37] Hinckle v. Wheaton College (In re Hinckle), 200 B.R. 690, 694 (Bankr. W.D. Wash. 1996).
[38] *See e.g.*, Educational Credit Management Corp. v. Degroot, 339 B.R. 201, 212 (D. Ore. 2006)("where debtors choose to incur educational debt later in life, the fact that they will reach retirement age during the loan repayment period is not enough alone to justify discharge…."); Mandala v. Educ. Credit Mgmt. Corp. (*In re* Mandala), 310 B.R. 213, 222 (Bankr. D. Kan. 2004) (where the debtor chose to return to school late in life on borrowed money, "that student loan payment may progress beyond a borrower's retirement age, standing alone, should not skew the second *Brunner* test against lenders").
[39] Fabrizio v. U.S. Dept. of Educ. Borrower Services (*In re* Fabrizio), 369 B.R. 238, 245-246 (Bankr. W.D. Pa. 2007) ("Debtor's personal belief as to the effect of payment is totally irrelevant on this issue").

Brunner third prong

The third prong of *Brunner* is whether the debtor has made good faith efforts to repay the loan. As a starting point, failure by the debtor to make a payment does not of itself establish a lack of good faith.[40] Rather, a debtor's good faith is measured by his "efforts to obtain employment, maximize income, and minimize expenses."[41] So, where a debtor attempted unsuccessfully find work while living with his mother, and at the same time suffered from debilitating medical conditions, the third prong of *Brunner* was satisfied.[42] On the other hand, a debtor's failure to make *any* payments when earning an income can be evidence of lack of good faith efforts.[43]

Some courts consider whether the debtor has participated in alternative repayment options.[44] Creditors may argue that this means the debtor must have negotiated a repayment plan under the Income Contingent Repayment Program. However, in *In re* Mosley, the Eleventh Circuit rejected a per se test.[45] In that case, although the debtor's payment under an income contingent repayment plan would be zero, interest on the debt would continue to accrue and the amount forgiven at the end of 25 years could be treated as taxable income. As the court pointed out, this is not always a viable option for debtors because it would require them to "'trade one dischargeable debt for another.'"[46]

The Sixth Circuit has also refused to hold that the good faith prong of *Brunner* requires the debtor to participate income contingent repayment, noting that, inter alia, such a rule would in effect eliminate the discharge of student loans for undue hardship from the Bankruptcy Code.[47] The majority of courts agree.[48]

(ii) Totality of the Circumstances Test

The Eighth Circuit uses a "totality of the circumstances test" under which the court considers "(1) the debtor's past, present, and reasonably reliable future financial resources; (2) a

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[40] Educ. Credit Mgnt. Corp. v. Polleys (*In re* Polleys), 356 F. 3d 1302, 1311 (10th Cir. 2004) (holding that the debtor's "failure to make a payment, standing alone, does not establish a lack of good faith").
[41] Educ. Credit. Mgnt. Corp. v. Mosley (*In re* Mosley), 494 F. 3d 1320, 1327 (11th Cir. 2007).
[42] *In re* Mosley, *supra*, 494 F. 3d at 1327.
[43] *In re* Fabrizio, 369 B.R. 238, 245 (W.D. Pa. 2007) (finding lack of good faith where debtor who made $37,000 per year failed to make any payments for two years).
[44] Hertzel v. Educ. Credit Mgmt. Corp. (*In re* Hertzel), 328 B.R. 221, 233-34 (B.A.P. 6th Cir. 2005).
[45] *In re* Mosley, *supra*, 494 F. 3d 1320.
[46] *Id*. at 1327 (quoting *In re* Barrett, *supra*, 487 F. 3d at 364 (6th Cir. 2007). *See also, In re* Brodson, *supra*, 435 B.R. at 802 ("the [income contingent repayment program] might be beneficial for a borrower whose inability to pay is temporary and whose improvement is anticipated, however, such programs may be detrimental to the borrower's long-term financial health").
[47] *In re* Barrett, *supra*, 487 F. 3d 364.
[48] *See, e.g., In re* Brodson, *supra*, 435 B.R. 791; *In re* Crawley, 40 B.R. 421 (Bankr. E.D. Pa. 2011); *In re* Benjumen, 408 B.R. 9 (Bankr. E.D.N.Y. 2009); *In re* Bene, *supra*, 2012 Bankr. LEXIS 2914, *3 (holding that requiring income contingent repayment would effect a repeal of (523(a)(8)); Allen v. Amer. Educ. Services (*In re* Allen), 324 B.R. 278, 281 (Bankr. W.D. Pa. 2005) (whether debtor has participated in deferment or restructuring program "is but one of the factors for the court to consider"); Cagle v. Education Credit Management Corp. (*In re* Cagle), 2011 WL 614087 (Bankr. KS 2011).

calculation of the debtor's and her dependant's reasonable necessary living expenses; and (3) any other relevant facts and circumstances surrounding each particular bankruptcy case."[49] Thus, the court found undue hardship where the debtor cared for five children, including two autistic children, and her spouse's income as a police officer was insufficient to meet their reasonable expenses, much less pay anything towards her $300,000 student loan debt.[50]

The First Circuit has not adopted a specific test, but instead focuses on the debtor's ability to earn an income in the future: "We see no need in this case to pronounce our views of a preferred method of identifying a case of 'undue hardship.' The standards urged on us by the parties both require the debtor to demonstrate that her disability will prevent her from working for the foreseeable future."[51]

In absence of specific instructions from the First Circuit Court of Appeals, the First Circuit BAP and bankruptcy courts in Massachusetts employ a "totality of the circumstances test." Courts adopting this approach find that the second and third prongs *Brunner* go beyond what is required under §523(a)(8). In Bronsdon v. Educ. Credit Mgmt. Corp. (*In re* Bronsdon)[52] the First Circuit BAP rejected the second prong of *Brunner*, which requires a showing that the debtor's state of affairs is likely to persist for a significant portion of the repayment period:

> Many courts interpreting and applying the second *Brunner* prong, however, place dispositive weight on the debtor's ability to demonstrate "additional extraordinary circumstances" that establish a "certainty of hopelessness." The has led some courts to require that the debtor show the existence of "unique" or "extraordinary" circumstances, such as the debtor's advanced age, illness or disability, psychiatric problems lack of usable job skills, large number of dependents or severely limited education…. And, in the absence of such a showing, the court may conclude that the debtor has failed the second *Brunner* prong and the student loans will not be discharged. Requiring the debtor to present additional evidence of a "unique" or "extraordinary" circumstances amounting to a "certainty of hopelessness" is not supported by the text of §523(a)(8). The debtor need only demonstrate "undue hardship."[53]

The BAP also took issue with the third prong of *Brunner*, which requires the debtor to affirmatively prove good faith in attempting to repay the loan:

> Ultimately, the debtor must establish by a preponderance of the evidence that her present and future actual circumstances would impose an undue hardship if her debts are excepted from discharge. * * * The party opposing the discharge of a student loan has the burden of presenting evidence of any disqualifying factor, such as bad faith. The debtor is not required under the statute to establish

[49] Walker v. Sallie Mae Serv. Corp. (*In re* Walker, 650 F. 3d 1227, 1230 (8th Cir. 2011); Long v. Educ. Credit Mgmt. Corp. (*In re* Long), 322 F. 3d 549, 554 (8th Cir. 2003).
[50] *In re* Walker, *supra*, 650 F. 3d at 1234-35.
[51] TI Fed. Credit Union v. DelBonis, 72 F. 3d 921, 937 (1st Cir. 1995).
[52] *In re* Bronsdon, *supra*, 435 B.R. 791.
[53] *In re* Bronsdon, *supra*, 435 B.R. at 801, *citing* Hicks v. Educ. Credit Mgmt. Corp. (*In re* Hicks), 331 B.R. 18, 27-28 (Bank. D. Mass. 2005).

> prepetition good faith in absence of a challenge. The debtor should not be obligated to prove a negative, that is, that he did not act in bad faith, and, consequently, in good faith.[54]

The *Bronsdon* court found that debtor's efforts to repay a loan is just one of the elements in the totality of the circumstances test, and not a dispositive requirement on its own. For example, income contingent or IBR programs allow for suspension or reduction of payments, but can result in the continued accrual of interest. Such "negative amortization" in fact increases the debtor's ultimate debt burden.[55] In addition, federal loan forgiveness effectively trades nondischargeable loan debt for nondischargeable tax debt.[56] Accordingly, many loan repayment programs may not be suitable for debtors, and should not be taken into consideration when determining whether the debtor should be allowed a discharge.[57]

(iii) Partial Discharge of Education Debt

Some courts permit a debtor to discharge part of an education debt using *Brunner* or the "totality of the circumstances" criteria. Whether this is allowed under the Code is unclear. On its face, §523(a)(8) refers to discharge of "an educational benefit overpayment or loan…."[58] This can be construed to mean discharge of a loan in its entirety, and not a discharge of a part of a loan. Other provisions of the Code expressly provide for adjustment of a portion of a debt. For example, §506(a)(1) allows for partial modification (bifurcation) of a secured debt into secured and unsecured components "to the extent of the value of such creditor's interest in [the collateral]."[59] In consumer cases, the debtor may avoid a judgment lien against property of the debtor "to the extent that such lien impairs an exemption to which the debtor would have been entitled…."[60] In these provisions, the words "*to the extent*" show that partial treatment of the claim is allowed. There is no such language with respect to treatment of education debt.

In absence of express language allowing for partial discharge of education debt, some courts grant partial discharge pursuant to §105(a), which allows the court to "[i]ssue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title."[61] Thus, courts have granted partial discharge of student loan debt by discharging part of the principal, accrued interest or attorney's fees, instituting a repayment schedule, deferring repayment, or even by allowing a debtor to reopen bankruptcy proceedings to revisit the question of undue hardship.

The Sixth Circuit has held that partial discharge is permitted under §105(a)[62] using the three-part *Brunner* criteria.[63] To receive the discharge, the debtor must satisfy each prong of the

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[54] *Id.* at 800-801.
[55] *Id.* at 802.
[56] *Id.* at 802-803.
[57] *Id.*
[58] 11 U.S.C. §523(a)(8).
[59] *Id.* §506(a)(1).
[60] *Id.* §522(f)(1)(A).
[61] *Id.* §105(a).
[62] Tenn. Student Assistance v. Hornsby (*In re* Hornsby), 144 F. 3d 433, 440 (6th Cir. 1998). *See also*, Miller v. Pa. Higher Assistance Agency (*In re* Miller), 377 F. 3d 616, 620 (6th Cir. 2004)("when a debtor does not make a

Brunner test with respect to the portion of the debt to be discharged, and the discharge is allocated pro rata among the debtor's loans.[64] In one case, a bankruptcy court applied the three-part *Brunner* test in discharging all but $8,045.02 of the debtor's total student loan debt of $36,284.81.[65] "The debtor's inability to repay the student loans must result from factors beyond the debtor's reasonable control…."[66] The court found that the most important element causing the debtor's financial problem was her cancer, and that because of this, "it is highly likely that [debtor's] financial predicament will persist for many years, and possibly the rest of her life."[67]

Courts in the Tenth Circuit,[68] Eleventh Circuit,[69] and lower courts in the Ninth Circuit[70] also grant partial discharge of student loans using the *Brunner* criteria. Other courts have ordered partial discharge under the "totality of the circumstances" test. For example, a Massachusetts bankruptcy court held that although the debtor had not proven undue hardship at trial, her long-term income prospects were dubious given her advanced age and history of poor health. Therefore, the court held that if the debtor participated in the Ford Program and abided by the income-based option, the court would discharge whatever portion of the debt remained at the expiration of the repayment program.[71]

A hybrid approach was taken by the court in *In re* Hinkle.[72] In that case, the court ruled that there was no authority under the Code to a grant partial discharge of any education debt, but that where a debtor had multiple debts, the court could grant a full discharge to some of the debts while leaving the others nondischargeable, based upon the *Brunner* criteria.[73] Thus, of the debtor's six student loans, the court found that the three loans that had been in repayment the longest time, totaling $18,143, were dischargeable, but that the debtor would be able to pay the three remaining loans totaling $10,014.[74] Other courts use a similar loan-by-loan approach.[75]

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showing of undue hardship with respect to the entirety of her student loans, a bankruptcy court may – pursuant to its §105(a) powers—contemplate granting … a partial discharge of the debtor's student loans.").

[63] *In re* Oyler, 397 F. 3d 382 (6th Cir. 2005); *In re* Nixon, *supra*, 435 B.R. 311, 336 (Bankr. S.D. Ohio 2011)(court may grant partial discharge of student loan debt).

[64] *In re* Nixon, *supra*, 435 B.R. at 336 (debtor with education debt of more than $270,000 may discharge any amounts in excess of $214,200, based upon *Brunner* criteria).

[65] Jorgensen v. Educational Credit Mngmt. Corp. (*In re* Jorgensen), 2012 Bankr. LEXIS 254 (Bankr. HI, Jan. 19, 2012).

[66] Id. at *14.

[67] Id. at *13.

[68] Alderete v. Educational Credit Management Corp. (*In re* Alderete), 412 F. 3d 1200 (10th cir. 2005).

[69] Hemar Ins. Corp. v. Cox (*In re* Cox), 338 F. 3d 1238 (11th Cir. 2003), cert. denied, 541 U.S. 991 (2004)("Because the specific language of §523(a)(8) does not allow for relief to a debtor who has failed to show 'undue hardship,' the statute cannot be overruled by the general principals of equity contained in §105(a).").

[70] Saxman v. Educ. Mgmt. Corp. (*In re* Saxman), 325 F. 3d 1168, 1173 (9th Cir. 2003) ("bankruptcy courts may exercise their equitable authority under 11 U.S.C. §105(a) to partially discharge student loans."); Educational Credit Mgmt. Corp. v. Jorgensen (*In re* Jorgensen), 2012 Bankr. LEXIS 4303 (B.A.P. 9th Cir., Sept. 11, 2012) (partial undue hardship discharge of student loan debt affirmed as challenged expenses were justified by debtor's medical condition).

[71] Stevenson v. Educ. Credit Mgmt. Program (*In re* Stevenson), 2011 WL 3420428 (Bkrtcy D. Mass. 2011).

[72] In re Hinkle, *supra*, 200 B.R. 690.

[73] *Id.* at 693.

[74] *Id.* at 694. *See also, In re* Gharavi, 335 B.R. 492, 501 (Bankr. D. Ma. 2006) (debtor who suffered from fatigue due to MS established undue hardship in showing that she only had enough income to afford payments on the oldest of four loans).

One problem with the loan-by-loan approach is that it requires a court to decide which loan(s) which will be paid and which ones discharged. There is nothing in the Bankruptcy Code that addresses this type of prioritization, and several courts have held that loan-by-loan discharge is inappropriate for this reason.[76]

A number of courts have held that the Bankruptcy Code does not allow for partial discharge. These include the Third Circuit[77] and many bankruptcy courts.[78]

[75] Ledbetter v. United States Dep't of Educ. (*In re* Ledbetter), 254 B.R. 714 (Bankr. S.D. Ohio 2000); Hollister v. Univ. of N.D. (*In re* Hollister) 247 B.R. 485 (Bankr. W.D. Okla. 2000); *In re* Gharavi, 335 B.R. 492 (Bankr. D. Mass. 2006) (court discharged three out of four student loans, but debtor remained liable on one of them).
[76] Pincus v. Graduate Loan Center (*In re* Pincus) 280 B.R. 303, 313 (Bankr. S.D.N.Y. 2002); Young v. PHEAA (*In re* Young), 225 B.R. 312 (Bankr. E.D. Pa. 1998).
[77] *In re* Faish, *supra*, 72 F. 3d at 307.
[78] *See, e.g., In re* Pincus, supra 280 B.R. at 311 ("The Bankruptcy Code does not permit a court to discharge in part a single student loan obligation").

Legislative History of Bankruptcy Code Provisions Regarding Student Loans and the Current Definition of Student Loans Under the Bankruptcy Code

Anne J. White, Esquire
DEMEO LLP
One Lewis Wharf
Boston, MA 02110
awhite@demeollp.com

I. The Student Loan Problem

As the cost of education has mushroomed far in excess of the cost of living, aggregate student loan debt has increased exponentially. For example, in 1990 students borrowed approximately $11.7 billion in loans to fund their education. [1] During the period from 2010-2011, students borrowed $103.9 billion.[2] As the beginning of 2012, federal student loan debt totaled approximately $904 billion with private loans adding another $150 billion, surpassing both consumer credit card debt ($679 billion) and auto loan debt ($737 billion).[3]

Considering all student borrowers, approximately 14% of all students default on their loans within three (3) years of graduation.[4] At for-profit schools, 22% of the students default within 3 years of leaving school.[5] When viewed over a longer period of time, the default rate is even higher. According to an analysis conducted by the Federal Reserve Bank as of late 2011, 47% of student loan borrowers were in deferral or forbearance, 27% had a past due balance, and 21% were delinquent or in default.[6]

Section 523(a)(8) of the Bankruptcy Code (i.e. 11 U.S.C. Section 101, et seq.) exempts educational loans from discharge unless the debtor establishes that paying the debt would result in "undue hardship" on the debtor and the debtor's dependants. Such hardship discharges are rare. As Daniel A. Austin, Associate Professor at Northeastern University School of Law explains in his comprehensive article entitled, "The Indentured Generation: Bankruptcy And Student Loan Debt,"

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[1] United States General Accounting Office, *Report to the Secretary of Education, Federal Student Aid: Timely Performance Plans and Reports Would Help Guide and Assess Achievement of Default Management Goals* (GAO-03-348, February 2003).
[2] The College Board *Trends in Student Aid* 2011, p. 10, *available at* http://trends.collegeboard.org/student_aid/
[3] Trends in Student Aid 1011, supra note 2 at 10.
[4] Len Boselovic, *Newly Minted Grads Face Loan Loads*, Pittsburgh Post-Gazette, Marcy 30, 2012, available at http://www.post-gazette.com/stories/business/heard-off-the-street/newly-minted-grads-face-loan-loads-294820/
[5] United States Senate, *For Profit Education: The Failure to Safeguard the Federal Investment and Ensure Student Success*, http://www.help.senate.gov/imo/media/for_profit_report/PartI.pdf
[6] Meta Brown, et al, "Grading Student Loans," http://libertystreeteconomics.newyorkfed.org/2012/03/grading-student-loans.html/ (July 9, 2012). A chart showing the increase in households with education loan debt is in Federal Reserve Bank 2010 Survey of Consumer Finances (SCF) Chartbook, p. 1082, *available at* http://www.federalreserve.gov/econresdata/scf/files/2010_SCF_Chartbook.pdf.

> Some 37 million Americans owe a total of approximately $1 trillion dollars in student loans. They constitute an Indentured Generation as many of them will be burdened with student loan debt for much of their lives… Members of the Indentured Generation who are in particularly dire circumstances will turn to bankruptcy for a "fresh start." But, with few exceptions, student loan debtors will not get relief through bankruptcy…Because of this, education debt servitude will last a lifetime for tens of thousands of Indentured Generation.

The Indentured Generation: Bankruptcy And Student Loan Debt, 53 Santa Clara Law Review (May 2013)[7]

II. Legislative History of Bankruptcy Code Provisions Regarding Student Loans SECTION 523(a)(8)

A. The Initially Enacted Statutory Language (Effective October 1, 1979)

Pursuant to the Bankruptcy Code as enacted on November 6, 1978 (which became effective on October 1, 1979), Section 523(a)(8) [8]

> **(a) A discharge under section 727, 1141, or 1328(b) of this title does not discharge an individual debtor from any debt—**
> **…**
>
> **(8) to a governmental unit, or a nonprofit institution of higher education, for an educational loan, unless—,**
> **(A) such loan first became due before five years before the date of the filing of the petition; or**
> **(B) excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor's dependents**

According to a Senate Report at the time, these provisions in the Bankruptcy Code as enacted in 1978 were intended to generally follow current law and except from discharge student loans until such loans have been due and owing for five years. Such loans include direct student loans as well as insured and guaranteed loans. The provision included educational loans owing to a governmental unit and nonprofit institution of higher education. S Rep No. 989, 95th Cong, 2d Sess 79 (1978)

B. The Corrective Statutory Language (Effective October 1, 1979)

[7] Electronic copy available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2157461
[8] REFORM ACT OF 1978, Public Law 95–598, 1978 HR 8200

However, it was immediately recognized that the language needed corrections and that a gap had inadvertently been created between the effective date of the Bankruptcy Code and Section 523(a)(8) and the repeal of the sections of the applicable Higher Education Act. As Senator DeConcini explained in July 1979, "When the Bankruptcy Reform Act was enacted upon the President's signature on November 6, 1978, that section of the Higher Education Act dealing with the dischargeability of student loans was repealed and replaced by a provision in the new law which makes such obligations nondischargeable. However, because the new law does not take effect until this forthcoming October 1, between these two times there was created a gap. During this period, without a specific provision limiting dischargeability of such obligations, the matter will be dealt with under existing bankruptcy law which does not provide for the nondischargeability of such debts. This was not the intent of the law under the Higher Education Act, is not the intent of the new bankruptcy law, and is an oversight which we now must cure. (125 Cong Rec S 9160 (daily ed. July 11, 1979); remarks of Sen. DeConcini)

The initial statutory language also ignored the standard practice of granting suspension periods for student loans following graduation. In addition there was an oversight with respect to direct student loans issued by the Department of Health, Education and Welfare.

Because new 11 U.S.C. 523(a)(8) applies only to debts for educational loans owing to a governmental unit or to a nonprofit institution of higher education, it has a very uneven effect upon the student loan programs administered by the Department of Health, Education, and Welfare. For example, National Direct Student Loan (NDSL) funds are administered by both nonprofit and profit-making institutions of higher education.

The statutory language as effective October 1, 1979[9] became:

> **(a) A discharge under section 727, 1141, or 1328(b) of this title does not discharge an individual debtor from any debt—**
> **…**
>
> **(8) for an educational loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or a nonprofit institution of higher education, unless—,**
> **(A) such loan first became due (exclusive of any applicable suspension of the repayment period) before five years before the date of the filing of the petition; or**
> **(B) excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor's dependents**

[9] PL 96–56, 1979 HR 2807 Approved August 14, 1979 (Effective October 1, 1979)

C. The Statutory Language (Effective May 29, 1991)

In the 1990, Congress revised the student loan issue and modified the statutory language. Section 201 of the act extends the Bankruptcy Code's nondischargeability of student loans to debts which are similar in nature to student loans. It also extends the time limitation on the discharge of these debts from 5 to 7 years. The new provisions in Section 523(a)(8) became effective 180 days after the enactment of the law on November 29, 1990.

> **(a) A discharge under section 727, 1141, or 1328(b) of this title does not discharge an individual debtor from any debt—**
> **…**
>
> **(8) for an educational benefit overpayment or loan made, insured or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution, or for an obligation to repay funds received as an educational benefit, scholarship or stipend, unless—,**
> **(A) such loan, benefit, scholarship, or stipend overpayment first became due more than 7 years (exclusive of any applicable suspension of the repayment period) before the date of the filing of the petition; or**
> **(B) excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor's dependents**

D. The Significant Statutory Language Revision (Effective October 7, 1998)

In 1998 as significant change was enacted in the treatment of student loans. In its conference report, Congress indicated: "The conferees, in the effort to ensure the budget neutrality of this bill, adopted a provision eliminating the current bankruptcy discharge for student borrowers after they have been in repayment for seven years. The conferees note that this change does not affect the current provisions allowing any student borrower to discharge a student loan during bankruptcy if they can prove undue economic hardship. The conferees also note the availability of various options to increase the affordability of student loan debt, including deferment, forbearance, cancellation and extended, graduated, income-contingent and income-sensitive repayment options." (H.R. Conf. Rep. No. 750, 105th Cong. 2nd Sess. 1998 (September 25, 1998) to accompany H.R. 6)

The amendment to Section 523(a)(8) applied to all cased commenced after October 7, 1998[10]

[10] PL 105–244 (HR 6) October 7, 1998

> **(a) A discharge under section 727, 1141, or 1328(b) of this title does not discharge an individual debtor from any debt—**
> **…**
>
> **(8) for an educational benefit overpayment or loan made, insured or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution, or for an obligation to repay funds received as an educational benefit, scholarship or stipend, unless excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor's dependents**

E. The Statutory Language Under BAPCPA (Effective October 17, 2005)

The provisions of the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) expanded the definition of the kinds of student loans including in Section 523(a)(8)

> **(a) A discharge under section 727, 1141, or 1328(b) of this title does not discharge an individual debtor from any debt—**
> **…**
>
> **(8) unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor's dependents, for—**
> **(A) (i) an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution~~,~~; or**
> **(ii) an obligation to repay funds received as an educational benefit, scholarship; or**
> **(B) any other educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who is an individual;**

Section 220 of the Act [BAPCPA] amends section 523(a)(8) of the Bankruptcy Code to provide that a debt for a qualified education loan (as defined in section 221(e)(1) of the Internal Revenue Code) is nondischargeable, unless excepting such debt from discharge would impose an undue hardship on the debtor and the debtor's dependents. (HR Rep. No. 31, 109th Cong., 1st Sess 220 (2005)).

III. Expanded Definition of Student Loans under BAPCPA

Under the 2005 amendments of BAPCPA, Section 523(a)(8) now includes a new Section B for those student loans which the taxpayer may claim a deduction for interest paid on the student loan on their tax returns. Government-backed or college-backed loans have long been

the subject of Section 523(a)(8), however the new Section B includes "any other educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who is an individual."

Section 221(d)(1) of the Internal Revenue Code of 1986, provides, in part:

> **The term "qualified education loan" means any indebtedness incurred by the taxpayer solely to pay for qualified higher education expenses –**
> **(A) which are incurred on behalf of the taxpayer, the taxpayer's spouse, or any dependent of the taxpayer as of the time the indebtedness was incurred,**
> **(B) which are paid or incurred within a reasonable period of time before or after the indebtedness is incurred, and**
> **(C) which are attributable to education furnished during a period during which the recipient was an eligible student.**

While this definition is broad and makes many private student loans no longer dischargeable, there are certain exceptions worth note. For example, since these qualified education loans must be solely to pay qualified higher education expenses, mixed use loans do not qualify as education loans. Thus, if the private loan is in part for residential improvements and in part for education expenses, the loan does not qualify as an education loan.[11] Similarly, cash advances, revolving lines of credit and credit card debt is generally not qualified education loans unless the borrower used the line of credit solely to pay qualified higher education expenses.[12] Secondly, the loan needs to be furnished during a period in which the recipient is an eligible student. As explained in more detail in the Student Loan Law, NCLC Consumer Credit and Legal Practice Series (4th Ed. 2010 and Supp.)[13] at page 179, "aggressive proprietary schools in some cases enroll non-high-school graduates …[who] are eligible to administratively cancel their loans and should also be categorized as "ineligible" students." Also, some purported educational institutions are scams or become unaccredited. Under these circumstances the loan amounts would not satisfy the requirement of being a "qualified higher educational expense."[14]

Certain private loans will not be included in the broad sweep of 523(a)(8)(B), if it can be established that the purposes of the loan were not educational. In In re Segal, 57 Fe.3d 342 (3rd Cir. 1995), for example, a nonprofit hospital paid off their employee's student loans and replaced them with new loans owed to the hospital. The Circuit Court found that the hospital paid the loans as a business expense and as a hiring incentive. The loans were not primarily educational loans and were dischargeable.

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[11] 26 C.F.R.§ 1.221-1(e)(4) ex. 6
[12] 26 C.F.R.§ 1.221-1(e)(4); 64 Fed. Reg. 3257, 3258 (Jan. 21 1999)
[13] Student Loan Law, NCLC Consumer Credit and Legal Practice Series (4th Ed. 2010 and Supp.) available http://shop.consumerlaw.org/
[14] See, Student Loan Law, NCLC Consumer Credit and Legal Practice Series (4th Ed. 2010 and Supp.) at page 179

Finally, it is well established that bankruptcy debtors may discharge tuition debts when the creditor fails to establish the existence of a 'loan' involving a transfer of funds and a formal agreement with specific repayment terms. For example, in In re Chambers, 348 F.3d 650 (7th Cir. 2003) the tuition debt was held dischargeable where there was no evidence that the parties entered into any loan arrangements prior to services being provided.[15]

[15] See, Student Loan Law, NCLC Consumer Credit and Legal Practice Series (4th Ed. 2010 and Supp.) at page 180 for a collection of recent cases on point.

PAYING STUDENT LOANS

James F. Molleur, Esq.
Molleur Law Office
419 Alfred Street
Biddeford, Maine 04005
jim@molleurlaw.com

Pre-Default Payment Programs

1. Standard, Graduated, and Extended Repayment Programs

Standard repayment programs are the most common repayment arrangements, with the highest monthly payments, with the same amount for each installment, over a 5 – 10 year payment plan. Graduated repayment plan usually start out low and increase over time and work best for individuals who expect their income to increase quickly. These plans also must be repaid over 10 years. Extended repayment plans are available for individuals borrowing over $30,000 and can be paid in a standard plan or graduated plan over 25-30 years.

2. Repayment Plans Tied to Borrower's Income: Income-Based Repayment (IBR), Income-Contingent Repayment (ICR), and Income-Sensitive Repayment

The Income Based Repayment Plan (IBR) is available to borrowers with FFEL (Federal Family Education Loan) or Direct Loans, but not Perkins or Parent Plus loans. The payments are tied to a borrower's income and can result in negative amortization. However, there will be loan balance forgiveness after 25 years, although the forgiven loan amount can be taxable to the borrower. The IBR is only available to borrowers not in default. The repayment formula is 15% of the adjusted gross income above 150% of the DHHS poverty guideline.

The Income Contingent Repayment Plan (ICR) is also available to Direct Loan borrowers not in default. The payments are 20% of any earnings above poverty level. If

borrowers make these payments for 25 years, any remaining debt is forgiven. The IBR applies to more loans than ICR and has been used more frequently.

There is also an Income Sensitive Repayment Plan (ISR) which requires borrowers to submit annual income information to the lender and needs to be paid over a shorter time period and are less affordable that the IBR or ICR.

3. Loan Servicing

AES/PHEAA, Great Lakes Education Loan Services, Nelnet, and Sallie Mae each have 5 year contracts to service student loans with revenues to the companies determined in part by the borrowers not in default. In other words, if fewer borrowers default, there is more revenue to the company.

Postponing Repayment on Federal Student Loans

1. Grace Periods

Generally, on Direct Stafford loans, six months after a student leaves school, the borrower must begin repayment of the loan. PLUS loan borrowers must begin paying 60 days after the final loan disbursement.

2. Deferments

Borrowers can request a deferment if they are not in default. Deferments can last about 3 years. Deferments are permitted for economic hardship, unemployment, military service, or post active duty time periods. PLUS loans, Perkins loans, and FFEL loans have additional deferment opportunities.

3. Forbearances

The forbearance programs generally allow borrowers to prevent a default on their loans, or to resume payments to eliminate defaults. They can include temporary stoppage of payments, extending payments or making smaller payments.

Student Loan Defaults

Federal loans are in default if a borrower is unable to make current monthly payments over a 9 month time period. Collection activities by the lender may follow. Private student loan defaults have been hidden by forbearances. Defaults can include any typical defaults under any private bank loan. Private student lenders do not have all the collection remedies available to federal student lenders.

Getting Out of Default

1. Consolidation

Borrowers can consolidate their student loan to eliminate their default. The principal consolidation loan is a Direct loan. There must be at least one FFEL or Direct Loan to qualify for consolidation. Borrowers can make 3 loan payments under the original loan schedule or enter into an IBR or ICR to obtain a consolidated loan.

2. Loan Rehabilitation

To rehabilitate a loan, a borrower must make 9 timely monthly payments within a 10 month time period. For FFEL borrowers, HEA (Higher Education Act) regulations permit more liberal rehabilitation standards, without minimum loan payments, although collectors often seek higher payments than may be affordable for borrowers. HEA regulations only allow 1 rehabilitation per loan.

3. Compromise and Write-Off Authority

There is authority to compromise or write-off FFEL or Perkins loans where a borrower is unable to pay the full amount in a reasonable time, the cost of collection doesn't justify collection of the full amount, or there is a significant doubt regarding the government's ability to prove its case in court. Collection costs and 30% of the principal and interest can be waived in the compromise. There are additional write-off procedures, but they bind the guaranty authority, not the United States.

Federal Student Loan Collection

1. Pre-Default Collection

When a loan is delinquent, the lender must send a written collection letter, followed by at least 4 attempts to contact the borrower by telephone, with at least one attempt by telephone to occur before the 90th day of delinquency and one attempt after the 90th day. At least 2 collection letters sent to the borrower during that time period must advise the borrower of the consequences of default. A final demand letter is sent after the 241st day and before the 270th day to encourage the borrower to bring the loan out of default.

2. Post-Default Collection

There are collection activities taken at least every 180 days, with enforcement letters to borrowers that advise of future actions the lender may take. These letters need to comply with the FDCPA for any collection agency.

3. Credit Bureau Reporting

The Department of Education, guaranty agencies, and lenders have agreements with each credit reporting agency to report the status of the student loan, on a monthly basis. Any defaults will be negative notations on the credit report, which can be cleaned up only by payment of the loan, loan rehabilitation, or a bankruptcy or non-bankruptcy discharge of the loan (closed school, false certification, or unpaid refund discharges).

4. Collection Fee and Penalties

Collection fees must be reasonable, and if the loan is sent to a collection agency, a percentage contingency fee arrangement is permissible. If loans are rehabilitated or consolidated, there can be a 18.5% collection fee added to the loan.

5. Deceptive and Abusive Debt Collection Tactics

There is little governmental oversight of collection agencies, and the agencies do not always look at a borrower's ability to pay in determining an amount the collection agency seeks to collect monthly from a borrower. There are occasional threats of wage garnishment without any hearing, although the statutes require notice and an opportunity for an administrative hearing before garnishment can occur. SSD benefits can be offset to pay defaulted loans, but SSI

benefits cannot be offset. The usual litany of FDCPA prohibited collection techniques are also reported by student loan borrowers (criminal threats, harassment, calling neighbors, etc.). The FDCPA is effective against collection agencies for student loans.

6. Defenses to Federal Student Loan Collection Actions

While a status of limitations defense is generally not available to borrowers, defenses of lack of standing, forgery, mistake, infancy, fraud are available.

7. Tax Refund Offsets

Tax refunds can be offset where the loan is a Federal student loan and the money is owed to the Department or a guaranty agency. If the borrower enters into a repayment plan and makes initial payments under that plan, an offset can be avoided.

8. Administrative Wage Garnishments

Administrative wage garnishments can occur between 15% - 25% of disposable income. Notice needs to be provided to the borrower. A borrower can seek to prevent the garnishment if he or she can demonstrate financial hardship.

9. Seizure of Federal Benefits

Most Federal benefits can be offset against a borrower on a defaulted student loan except for SSI benefits.

10. Federal Salary Offsets

Up to 15% of disposable income can be offset from a federal government borrower, after notice and an opportunity for a hearing.

11. Professional License Suspensions and Revocations

Some state laws permit revocation, suspension, or refusal to renew profession or vocational licenses for failure to pay student loans. If the loans are rehabilitated or a payment plan is entered into, the borrower can usually regain his or her license.

Statutory Discharges of Federal Student Loans

1. Closed School Discharges

HEA requires a discharge of a student loan if the school's closure prevents completion of the borrower's program. The Secretary of Education keeps a list of the official school closure dates, which can be found on the Department of Education website.

2. False Certification Discharge

A borrower can obtain this discharge if a school falsely certified to the student lender that the borrower was eligible for the loan, that the borrower would benefit from the program, or that the borrower would be able to meet minimum state employment requirements for the job for which the borrower is being trained.

3. Unpaid Refund Discharges

This discharge usually applies to borrowers who attended trade schools, where they never attended or withdrew from the school in time to be entitled to a refund, but where they never received the refund from the school.

4. Disability Discharges

Partial or full loan discharges are available to borrowers who are permanently and completely disabled, when the loans are FFEL, Direct loans, and Perkins loans. The standard for disability is the same as Social Security Disability.

5. Profession-Related Loan Cancellations

Certain public service jobs can entitle a borrower for a Direct loan cancellation, such as military service, law enforcement, early childhood education, public education, etc.

Treatment Of Student Loans In Chapter 13; Addressing Student Loans in the Future

John Rao
National Consumer Law Center, Inc.

A. Dealing with Student Loan Debt in Chapter 13

Separate Classification

If the debtor does not seek a hardship discharge in a chapter 13 case, the debtor is obligated to pay the remainder of the debt that has not been paid during the plan after the case has terminated, including any interest on the debt that has accrued during the plan.[1] When that is the case, it is in the debtor's interest to pay off as much of the student loan in the chapter 13 plan as possible.

One way to pay more on the student loan than on other unsecured debts is to separately classify the student loan for payments at a higher percentage than other unsecured debts pursuant to 11 U.S.C. § 1322(b)(1). Recent cases have been divided, both in the means of analysis and the result, as to whether students can separately classify student loans, some allowing separate classification[2] and some not.[3] Some courts have even issued opinions providing guidance as to

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[1] If the student loan debt is nondischargeable, postpetition interest will not be discharged. *See In re* Kielisch, 258 F.3d 315 (4th Cir. 2001); *In re* Pardee, 218 B.R. 916 (B.A.P. 9th Cir. 1998), *aff'd*, 187 F.3d 648 (9th Cir. 1999); *In re* Jordan, 146 B.R. 31 (D. Colo. 1992).

One court has held that, while unmatured, postpetition interest may not be included in the student loan creditor's claim, section 502(b) does not prevent the creditor from applying chapter 13 plan payments to accrued interest, including postpetition interest, on the nondischargeable debt. *In re* Kielisch, 258 F.3d 315 (4th Cir. 2001). *See also* U. S. Dep't of Educ. v. Harris, 339 B.R. 673 (W.D. Tenn. 2006) (in a second chapter 13 case, DOE can apply trustee payments first to interest and charges that accrued postpetition during earlier chapter 13 case, then to principal).

[2] *In re* Pracht, 464 B.R. 486 (Bankr. M.D. Ga. 2012) (discriminatory classification in favor of student loan debt; decreasing general unsecured creditors recovery from 20% to 15%, allowed when this preserves debtor's participation in Public Service Loan Forgiveness program); *In re* Kalfayan, 415 B.R. 907 (Bankr. S.D. Fla. 2009) (separate classification allowing maintenance of current payments on student loan not unfairly discriminatory because debtor must be current on student loans to keep optometrist license and thereby fund plan for all creditors); *In re* Webb, 370 B.R. 418 (Bankr. N.D. Ga. 2007); *In re* Cox, 186 B.R. 744 (Bankr. N.D. Fla. 1995); *In re* Tucker, 159 B.R. 325 (Bankr. D. Mont. 1993); *In re* Foreman, 136 B.R. 532 (Bankr. S.D. Iowa 1992); *In re* Boggan, 125 B.R. 533 (Bankr. N.D. Ill. 1991); *In re* Freshley, 69 B.R. 96 (Bankr. N.D. Ga. 1987). *See also In re* Potgieter, 436 B.R. 739 (Bankr. M.D. Fla. 2010) (classification of student loan to make ongoing payments outside of plan while the plan provides for 100% payment of all other general unsecured claims not unfairly discriminatory); *In re* Sullivan, 195 B.R. 649 (Bankr. W.D. Tex. 1996); *In re* Dodds, 140 B.R. 542 (Bankr. D. Mont. 1992).

the amount of discrimination that will be allowed.[4] Debtors are permitted to discriminate among similar classes of creditors in a plan. The issue is whether a separate classification for one

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On the analogous question of whether nondischargeable child support debts may be separately classified, many courts have concluded in the affirmative. *E.g.*, *In re* Leser, 939 F.2d 669 (8th Cir. 1991); *In re* Husted, 142 B.R. 72 (Bankr. W.D.N.Y. 1992); *In re* Whittaker, 113 B.R. 531 (Bankr. D. Minn. 1990) (allowing a fresh start is sufficient to justify discriminatory classification in favor of nondischargeable support debt).

[3] *In re* Groves, 39 F.3d 212 (8th Cir. 1994) (plan could not discriminate in favor of student loans solely due to their nondischargeability); *In re* Bentley, 266 B.R. 229 (B.A.P. 1st Cir. 2001) (chapter 13 plan that favored student loan creditor failed unfair discrimination test by altering "allocation of benefits and burdens" to detriment of other unsecured creditors); *In re* Sperna, 173 B.R. 654 (B.A.P. 9th Cir. 1994) (plan could not discriminate in favor of student loans solely due to their nondischargeability); *In re* Birts, 2012 WL 3150384 (E.D. Va. Aug. 1, 2012) (non-dischargeable nature of student loan debt and federal policy favoring payment of student loans do not justify discriminatory treatment; unsecured creditors recovery would increase from 7% to 16% if student loan paid under plan); *In re* Kubeczko, 2012 WL 2685115 (Bankr. D. Colo. July 6, 2012) (unfair discrimination when student loan creditors receive 46.86% dividend, but all other unsecured creditors a 0.27% dividend); *In re* Renteria, 2012 WL 1439104 (Bankr. D. Colo. Apr. 26, 2012) (if student loan debt paid separately outside plan, all other unsecured creditors would receive 1% payment, as opposed to 12% if student loan debt paid uniformly with all unsecured claims through plan; unfair discrimination to make $550 monthly student loan payment outside plan); *In re* Sutton, 2012 WL 433480 (Bankr. E.D.N.C. Feb. 9, 2012) (rejecting separate classification for student loan in Chapter 11 case because, *inter alia*, debtor failed to present evidence of reasonable basis for disparity of 100% payment to student loan creditor and 3.8% distribution to other unsecured creditors); McCullough v. Brown, 162 B.R. 506 (N.D. Ill. 1993); *In re* Knecht, 410 B.R. 650 (Bankr. D. Mont. 2009) (denying confirmation of plan with separate classification for student loan and paying zero dollars to all other unsecured creditors); *In re* Thibodeau, 248 B.R. 699 (Bankr. D. Mass. 2000) (plan was not proposed in nondiscriminatory manner based on debtor's sizeable income and lack of good faith); *In re* Burns, 216 B.R. 945 (Bankr. S.D. Cal. 1998); *In re* Gonzalez, 206 B.R. 239 (Bankr. S.D. Fla. 1997); *In re* Coonce, 213 B.R. 344 (Bankr. S.D. Ill. 1997); *In re* Willis, 189 B.R. 203 (Bankr. N.D. Okla. 1995), *rev'd and remanded*, 197 B.R. 912 (N.D. Okla. 1996); *In re* Colfer, 159 B.R. 602 (Bankr. D. Me. 1993) (refusing to allow separate classification); *In re* Smalberger, 157 B.R. 472 (Bankr. D. Or. 1993), *aff'd*, 170 B.R. 707 (D. Or. 1994); *In re* Chapman, 146 B.R. 411 (Bankr. N.D. Ill. 1992); *In re* Scheiber, 129 B.R. 604 (Bankr. D. Minn. 1991); *In re* Furlow, 70 B.R. 973 (Bankr. E.D. Pa. 1987) (separate classification of student loan debt not allowed without further explanation of reasons). *See also In re* Pora, 353 B.R. 247 (Bankr. N.D. Cal. 2006) ("majority approach" requires debtor to show that proposed separate classification for student loan does not unfairly discriminate).

[4] *In re* Mason, 456 B.R. 245 (Bankr. N.D. W. Va. 2011) (separate classification of student loan debt to receive higher percentage payment than other unsecured creditors may be approved if debtor can articulate a non-arbitrary reason for treatment, such as preventing unwarranted accrual of interest and penalties during term of plan); *In re* Boscaccy, 442 B.R. 501 (Bankr. N.D. Miss. 2010) (separate classification of student loan to allow for cure allowed unless the classification creates a substantial disparity in percentage paid to other general unsecured

creditor discriminates *unfairly* against other creditors. Classifying student loan debts so that they receive a higher percentage distribution from the debtor's plan payments than other non-priority unsecured debts can be appropriate upon consideration of several factors. These factors include the need to protect the goal of the fresh start so that a debtor's debt burden is not worse for having sought bankruptcy relief. Another factor favoring separate classification is the clear federal policy to encourage payment of student loan debts.[5]

A useful alternative to separate classification, in those jurisdictions where separate classification has not been approved, is to cure a default and maintain ongoing payments on the student loan pursuant to 11 U.S.C. § 1322(b)(5).[6] This allows the debtor to cure an arrearage on the student loan over time while maintaining the postpetition payments during the life of the plan. Some courts have permitted debtors to make ongoing student loan payments from income on this basis.[7] An added benefit of this approach is that the ongoing payments will include postpetition interest that would not otherwise be paid as part of a claim under the plan,[8] though some courts have held that the BAPCPA amendment adding section 1322(b)(10) prohibits interest being paid unless it is a 100% plan. By failing to give effect to section 1322(b)(5) as a

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creditors); *In re* Simmons, 288 B.R. 737 (Bankr. N.D. Tex. 2003) (plan providing for 100% repayment of student loan and zero percent to general unsecured creditors may be confirmed when all of debtor's disposable income paid into plan for first thirty-six months and student loan creditor paid in months forty-one through forty-eight of plan); *In re* Williams, 253 B.R. 220 (Bankr. W.D. Tenn. 2000) (plan that provides for 100% repayment of student loan will be confirmed only if other unsecured creditors are paid at least 70%; debtors may show "unique circumstances" to justify confirmation of plans with more than 30% difference in repayment percentage).

[5] *In re* Mason, 456 B.R. 245 (Bankr. N.D. W. Va. 2011).

[6] Section 1322(b)(5) permits the curing of defaults under the plan and maintenance of ongoing payments, typically made outside the plan, on any secured or unsecured claims when the last payment on the debt is due after the final payment under the plan.

[7] *In re* Johnson, 446 B.R. 921 (Bankr. E.D. Wis. 2011); *In re* Webb, 370 B.R. 418 (Bankr. N.D. Ga. 2007) (debtor may pay general unsecured creditors a 1% dividend through plan payments while making regularly scheduled student loan payments directly to student loan creditor pursuant to 11 U.S.C. § 1322(b)(5); new section 1322(b)(10), added by BAPCPA, does not preclude this plan structure). *See In re* Knight, 370 B.R. 429 (Bankr. N.D. Ga. 2007) (payment of student loan under section 1322(b)(5) permitted despite BAPCPA changes to disposable income test under section 1325(b)(1)(B)); *In re* Williams, 253 B.R. 220 (Bankr. W.D. Tenn. 2000); *In re* Chandler, 210 B.R. 898 (Bankr. D.N.H. 1997); *In re* Sullivan, 195 B.R. 649 (Bankr. W.D. Tex. 1996); *In re* Cox, 186 B.R. 744 (Bankr. N.D. Fla. 1995); *In re* Christophe, 151 B.R. 475 (Bankr. N.D. Ill. 1993) (plan can propose cure of student loan default pursuant to section 1322(b)(5)); *In re* Benner, 156 B.R. 631 (Bankr. D. Minn. 1993); *In re* Saulter, 133 B.R. 148 (Bankr. W.D. Mo. 1991). *See also In re* Machado, 378 B.R. 14, 17 (Bankr. D. Mass. 2007) (in providing for cure and maintenance of payments, chapter 13 plan can allow for current payments to be paid by debtor directly to creditor, while only payments to cure prebankruptcy arrearage need be paid through trustee and subject to trustee's commission).

[8] *In re* Williams, 253 B.R. 220 (Bankr. W.D. Tenn. 2000) (maintenance of ongoing payments on student loans under section 1322(b)(5) includes payment of postpetition interest).

distinct plan provision, however, many courts have required debtors proposing to pay student loans outside the plan to satisfy the unfair discrimination test under section 1322(b)(1).[9]

A final approach for below-median debtors might be to establish a five-year plan, not separately classify the student loan for the first three years of the plan, and then classify it for greater payment during the plan's final two years.[10] The basis for this approach is the Bankruptcy Code provision that requires disposable income only to be paid out over three years for below-median debtors.[11] Any amount that creditors receive in the final two years would be a bonus in any event. Courts have split on whether they will allow this separate classification of student loans in years four and five of a chapter 13 plan.[12]

Co-Debtor Stay

Another advantage of chapter 13 is that there is an additional type of "automatic stay" that goes into effect when the case is filed. This stay prohibits any act or legal action to collect a debtor's consumer debt from a co-debtor or co-obligor.[13] Students who file under chapter 13 can thus protect from collection parents or other family members who may have co-signed a student loan as long as the student's plan provides for payment of the student loan.[14] In addition, the

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[9] *In re* Labib-Kiyarash, 271 B.R. 189 (B.A.P. 9th Cir. 2001) (use of section 1322(b)(5) is subject to debtor showing that classification is fair under section 1322(b)(1)); *In re* Kubeczko, 2012 WL 2685115 (Bankr. D. Colo. July 6, 2012) (classification for cure of long-term student loan debt under section 1322(b)(5) must comply with prohibition on unfair discrimination under section 1322(b)(1)); *In re* Zeigafuse, 2012 WL 1155680 (Bankr. D. Wyo. Apr. 5, 2012) (debtor's payment of $320 monthly on student loan outside plan subject to section 1322(b)(1) prohibition on unfair discrimination; unfair because unsecured creditors receive 19% dividend if student loan paid uniformly with other unsecured debts under plan, but only 1.2% if student loan payments made separately outside plan); *In re* Harding, 423 B.R. 568 (Bankr. S.D. Fla. 2010) (plan's cure provision with payment of student loan outside plan violated prohibition on unfair discrimination against remaining unsecured creditors); *In re* Kruse, 406 B.R. 833 (Bankr. N.D. Iowa 2009) (plan's "cure and maintain" treatment of student loan debt unfairly discriminatory); *In re* Parrott, 2009 B.R. 5216043 (Bankr. E.D. Tenn. Dec. 29, 2009); *In re* Simmons, 288 B.R. 737 (Bankr. N.D. Tex. 2003); *In re* Edwards, 263 B.R. 690 (Bankr. R.I. 2001); *In re* Thibodeau, 248 B.R. 699 (Bankr. D. Mass. 2000).

[10] *In re* Strickland, 181 B.R. 598 (Bankr. N.D. Ala. 1995) (holding that nondischargeable student loan debt could not be treated more favorably than other unsecured claims for first thirty-six months of chapter 13 plan, but remaining twenty-four months could be devoted solely to payment of student loan).

[11] 11 U.S.C. § 1325(b)(1)(B).

[12] *Compare In re* Stickland, 181 B.R. 598 (Bankr. N.D. Ala. 1995) (allowing separate treatment in years four and five), *and In re* Rudy, 1993 WL 365370 (Bankr. S.D. Ohio 1993) (same), *with In re* Sullivan, 195 B.R. 649 (Bankr. W.D. Tex. 1996) (not allowing separate classification).

[13] *See* 11 U.S.C. § 1301.

[14] The Department of Education regulations acknowledge the chapter 13 co-debtor stay by noting that guaranty agencies must suspend all collection efforts against a "co-maker or endorser" if the student borrower has filed under chapter 13. *See* 34 C.F.R. § 682.402(f)(2).

need to retain the co-debtor stay may provide an additional justification for the separate classification of a student loan in a chapter 13 plan.[15]

Student Loan Payments as "Special Circumstances" Under the Means Test

In order to reduce current monthly income, an above-median-income debtor will often want to show the maximum allowable expenditures and expenses. Student loan payments would appear to be an obvious choice to apply toward this reduction. Unfortunately, student loan debt payments, like most general unsecured debts, are not allowable deductions from current monthly income for the means test calculation.[16] Yet, there is still a way in which the debtor may use student loan payments to reduce current monthly income and avoid the presumption of abuse. After deductions for allowed expenditures, the Code permits the debtor to rebut the presumption of abuse by demonstrating "special circumstances" that may bring the debtor's disposable income under the presumed abuse tolerance level set by the means test formula.[17] The Code defines these "special circumstances" only generally. The circumstances must "justify additional expenses or adjustments of current monthly income for which there is no reasonable alternative."[18] As examples of acceptable "special circumstances," the Code mentions "a serious medical condition or a call or order to active duty in the Armed Forces."[19]

May an obligation to pay a nondischargeable student loan be a "special circumstance" similar to a serious medical condition or a call to military service? Several courts have said yes.[20] For example, in *In re Delbecq*, the means test left the debtor with $304 in disposable monthly income, and she faced a trustee's motion to dismiss asserting the presumption of abuse.

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[15] 11 U.S.C. 1322(b)(1). *See In re* Linton, 2011 WL 3207366 (Bankr. E.D. Va. July 27, 2011) (full payment of $76,000 student loan through separate classification under plan not unfairly discriminatory when payment protects debtor's non-filing spouse who was jointly liable with debtor on student loans); § 10.9.1, *supra*.

[16] 11 U.S.C. § 707(b)(2)(A)(ii)(I) ("other necessary expenses" "shall not include any payments for debts"). *See also In re* Thompson, 457 B.R. 872 (Bankr. M.D. Fla. 2011) (student loan debt not an allowed priority expense under section 707(b)(2)(A)(ii), (iv), for Official Form 22A).

[17] 11 U.S.C. § 707(b)(2)(B)(i).

[18] 11 U.S.C. § 707(b)(2)(B)(i).

[19] *Id*.

[20] *In re* Edwards, 2012 WL 3042233 (Bankr. D. Ala. July 25, 2012) (agreeing that in some cases student loan payments may constitute special circumstances, but not in this case because debtors incurred other high unnecessary expenses); *In re* Sanders, 454 B.R. 855 (Bankr. M.D. Ala. 2011) (debtors who "either directly or on guarantor basis" were responsible for their son's student loan could claim the expense as a "special circumstance" under section 707(b)(2)(B)); *In re* Martin, 371 B.R. 347 (Bankr. C.D. Ill. 2007); *In re* Delbecq, 368 B.R. 754 (Bankr. S.D. Ind. 2007); *In re* Haman, 366 B.R. 307 (Bankr. D. Del. 2007) (debtor's obligation to pay as co-signor on son's student loan is "special circumstance"); *In re* Templeton, 365 B.R. 213 (Bankr. W.D. Okla. 2007). *See* Anthony P. Cali, *The "Special Circumstance" of Student Loan Debt Under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, 52 Ariz. L. Rev. 473 (Summer 2010) (reviewing decisions and policies related to issue and generally supporting treatment of student loans payments as "special circumstance").

In response, the debtor argued that her monthly student loan payment of $350 was a "special circumstance" that rebutted the presumption.[21] If her disposable income was reduced by the amount of her student loan payments, she would have no disposable income under the means test formula. The court agreed with the debtor and denied the trustee's motion to dismiss.[22]

A similar issue involving student loans and the debtor's projected disposable income has arisen in chapter 13 cases. Under BAPCPA, above-median-income debtors must pay their projected disposable income to creditors under a chapter 13 plan. The calculation of disposable income for this purpose uses the same standards under section 707(b)(2)(A) and (B) that apply in determining the presumption of abuse under the chapter 7 means test. If the student loan payments can be excluded from projected disposable income as a "special circumstance," the payment of the regular monthly installments on the long-term debt directly to the creditor would be appropriate. The same "special circumstances" standard of section 707(b)(2)(B)(i) that reduces current monthly income under the means test for chapter 7 applies to adjustments to disposable income in chapter 13.

At least one court has agreed with this analysis in the context of chapter 13.[23] Finding that monthly payments of $450 toward a nondischargeable student loan were "special circumstances," the court in *In re Knight* held that a downward adjustment of the debtor's projected disposable income in the full amount of his scheduled student loan payments was appropriate. The court found that the debtor had no reasonable alternative to payment of his student loans. There would be a demonstrable economic unfairness to the debtor if completion of a chapter 13 plan left him in default on his student loans and subject to garnishment or tax offsets.[24] This would be inconsistent with the intent of BAPCPA to encourage debtors to complete chapter 13 repayment plans.

Some courts have rejected the view that the obligation to pay a nondischargeable student loan debt is, per se, a "special circumstance" that justifies additional deductions from monthly income under the means test.[25] A per se rule that any specific debt within a general category of

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[21] *In re* Delbecq, 368 B.R. 754 (Bankr. S.D. Ind. 2007).
[22] *Id*.
[23] *In re* Knight, 370 B.R. 429 (Bankr. N.D. Ga. 2007).
[24] *Id.* at 437.
[25] *In re* Campbell, 2012 WL 162287 (Bankr. E.D. Ky. Jan. 18, 2012) (rejecting special circumstances treatment when debtor presented no evidence beyond nondischargeable nature of student loan debt); *In re* Thompson, 457 B.R. 872 (Bankr. M.D. Fla. 2011) (debtors did not establish student loan expense was necessary and could not be deferred under long-term payment options); *In re* Johnson, 446 B.R. 921 (Bankr. E.D. Wis. 2011) (student loan taken out voluntarily for career enhancement can never support "special circumstances" treatment, but debtor may classify student loan payments separately under section 1322(b)(5) to maintain payments); *In re* Harmon, 446 B.R. 721 (Bankr. E.D. Pa. 2011) (proceeding under chapter 13 would not impose unduly severe consequences upon debtor); *In re* Conlee, 435 B.R. 490 (Bankr. N.D. Ohio 2010); *In re* Siler, 426 B.R. 167 (Bankr. W.D.N.C. 2010); *In re* Carillo, 421 B.R. 540 (Bankr. D. Ariz. 2009); *In re* Pageau, 383 B.R. 221 (Bankr. D.N.H. 2008); *In re* Lightsey, 374 B.R. 377, 382 n.3 (Bankr. S.D. Ga. 2007).

expenditures will always qualify for the "special circumstances" deduction is not a tenable position, and it is not one that any courts have endorsed. Under a fair reading of the statute, the debtor must make some particularized showing that, in his or her case, there is no alternative to payment of the student loan debt.[26] However, in rejecting debtors' arguments that student loan payments were "special circumstances," some recent decisions endorsed a line of reasoning that deviates from the statutory language as widely as does the view that student loans should always be treated as a "special circumstances." These courts adopted the position that "special circumstances" must be the result of some involuntary hardship that befell the debtor.[27] According to these courts, student loans are a routine obligation that individuals take on voluntarily. Under this view, payments toward a nondischargeable student loan would almost never be a special circumstance reducing disposable income under section 707(b)(2)(B).

B. Addressing Student Loans in the Future

1. Private Student Loan Rulemaking

   On July 12, 2102, the Consumer Protection Financial Bureau and Department of Education issued a report on private student loans, as required by the Dodd-Frank Act.[28] On February 27, 2013, the CFPB initiated a Request for Information Regarding an Initiative To Promote Student Loan Affordability, requesting information from the public to determine options that would increase the availability of affordable payment plans for borrowers with existing private student loans.[29]

2. Proposed Student Loan Legislation

   S. 114 - "Fairness for Struggling Students Act of 2013
   H.R. 532 - "Private Student Loan Bankruptcy Fairness Act of 2013"
   H.R. 646 - "Bankruptcy Non-discrimination Enhancement Act"

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[26] *See In re* Champagne, 389 B.R. 191 (Bankr. D. Kan. 2008) (emphasizing fact-intensive nature of special circumstances determination; rejecting view that nondischargeable student loan obligation is per se a special circumstance but also rejecting view that student loan debt burden can never satisfy this requirement).

[27] *In re* Zahringer (Bankr. E.D. Wis. May 30, 2008); *In re* Pageau, 383 B.R. 221 (Bankr. D.N.H. 2008) (there must be "special circumstances" in the reasons that led debtor to incur education loan).

[28] The Report can be downloaded at: http://www.consumerfinance.gov/reports/private-student-loans-report/.

[29] The Notice is available at: http://www.consumerfinance.gov/notice-and-comment/.

Treatment Of Student Loans In Chapter 13

John Rao
National Consumer Law Center, Inc.

Case Summaries on Separate Classification

Cases in which separate classification and payment of student loan debt allowed:

Funds used are in excess of projected disposable income.

> *In re* Stull, 2013 WL 1279069 (Bankr. D. Kan. Mar. 27, 2013) (distinguishing this case from *In re Kubezcko*, which involved a below median debtor, court holds that an above-median debtor's chapter 13 plan to separately classify and pay a non-dischargeable obligation from income earned in excess of the projected disposable income committed to pay unsecured debt does not unfairly discriminate; plan in this case ultimately rejected because it proposed to pay interest on the student loan, which is prohibited by § 1322(b)(10) absent provision to pay all allowed claims in full).

Discrimination advances the goal of fresh start and the public policy objective of paying off student loan debts.

> *In re* Pracht, 464 B.R. 486 (Bankr. M.D. Ga. 2012) (separate classification and higher payment rate for student loan debt not unfairly discriminate because it allowed debtor to participate in the Public Loan Forgiveness program and gave her the chance to write off approximately $50,000 of student loan debt. Such discrimination advanced the goal of a fresh start for the debtor and the public policy objective of payment of student loan debts. The cost of this discrimination to unsecured creditors was 5%, or a total of only $5,000).

Discrimination not unfair when there is no harm to the unsecured creditors.

> *In re* Potgieter, 436 B.R. 739 (Bankr. M.D. Fla. 2010) (chapter 13 plan that separately classified student loan obligation and proposed to pay it at the contract rate outside of the plan did not unfairly discriminate because the plan provided for full repayment of all general unsecured claims; the student loan obligation was non-dischargeable such that the debt would be fully repaid at some point; and the debtor had the right, under § 1322(b)(4), "to provide for payments on any unsecured claim to be made concurrently with payments on any secured claim").

There is a reasonable basis and/or a less discriminatory approach would leave the debtor or creditors worse off.

> *In re* Mason, 456 B.R. 245 (Bankr. N.D. W. Va. 2011) (separate classification to allow student loan creditor to receive a higher percentage payment than other unsecured creditors may be allowed if the debtor can articulate a non-arbitrary reason why the

discrimination is necessary and demonstrate that a less discriminatory approach is not advisable).

In re Boscaccy, 442 B.R. 501 (Bankr. N.D. Miss. 2010) (in consolidated bankruptcy cases, debtors' separate classification for long-term student loan debt to allow for cure and maintenance not unfairly discriminatory when such classification reduced payments to other unsecured creditors by 21% and 26% because failure to maintain payments on student loan debts would leave debtors in a much worse position than they were in prior to filing; separate classification was unfair discrimination where equal treatment of all unsecured creditors would reduce the student loan payment by 20% while increasing the distribution to other creditors by 80%).

In re Kalfayan, 415 B.R. 907 (Bankr. S.D. Fla. 2009) (separate classification of student loans to allow for maintenance of payments not unfairly discriminatory because it benefited the very creditors who were being discriminated against; debtor risked losing her optometry license, under state law, if she fell behind on her student loan payments which would jeopardize her ability to pay other unsecured creditors).

In re Webb, 370 B.R. 418 (Bankr. N.D. Ga. 2007) (direct payments to student loan creditors in accordance with contract terms is not unfair discrimination because general unsecured creditors would realize only an additional .2% dividend in the absence of such discrimination while debtors would otherwise suffer needless accrual of interest and penalties and may face the consequences of default upon completion of the chapter 13 plan).

In re Freshly, 69 B.R. 96 (Bankr. N.D. Ga. 1987) (discrimination not unfair where separate classification of student loan from other unsecured debt was necessary for the debtor's rehabilitation under chapter 13, i.e. it would allow him to return to university and earn a degree and in light of the public policy goal of insuring repayment of student loans; plan proposed to full pay student loan debt of $2,258.00 while paying 1% of $5,314.53 of remaining unsecured debt).

Discrimination not unfair when classification is for long-term debt under § 1322(b)(5)

In re Cox, 186 B.R. 744 (Bankr. N.D. Fla. 1995) (proposal to pay student loans outside chapter 13 plan, according to the terms of each individual loan, did not unfairly discriminate even though it reduced the dividend to other unsecured creditors by 42% because such treatment is specifically sanctioned by § 1322(b)(5) when the terms of repayment on the student loans extend beyond the life of the plan).

In re Dodds, 140 B.R. 542 (Bankr. D. Mont. 1992) (separate classification of student loan debt to allow for payment according to the terms of the loan over 54 months not unfair discrimination; unsecured creditors were to receive payment of 79% over 36 months of the plan as opposed to 75% if the discrimination was disallowed. Court held that plan's treatment of student loan debt as long-term debt satisfied § 1322(b)(1) and (5)).

Payment of student loans, ahead of other unsecured debt, not unfair discrimination

In re Foreman, 136 B.R. 532 (Bankr. S.D. Iowa 1992) (debtor's plan, which proposed concurrent payment of student loans and a secured claim, to be followed by full payment of the remaining unsecured claims did not unfairly discriminate under the test set forth in *Matter of Tucker* because the plan provided for full repayment of all unsecured claims; the student loan obligations were non-dischargeable; and the debtor had a right to under § 1322(b)(4) to propose this repayment structure).

Discrimination not unfair so long as unsecured creditors receive at least as much as they would in chapter 7 proceeding

In re Tucker, 159 B.R. 325 (Bankr. D. Mont. 1993) (plan that proposed to pay nondischargeable student loan debt in full while only paying 29% dividend to other unsecured creditors did not unfairly discriminate because creditors would otherwise receive little or no payment under a Chapter 7 filing; the discrimination had a reasonable basis, i.e. allows full repayment of student loans; allows for a fresh start; the discrimination was not proposed in bad faith; and the degree of discrimination was directly related to the rationale for the discrimination).

In re Boggan, 125 B.R. 533 (Bankr. N.D. Ill. 1991) ("chapter 13 plan may provide for a greater percentage payment to an educational lender than to other unsecured creditors, but not by reducing the payments to those other creditors to a level below what they would get in a Chapter 7 liquidation of the debtor's assets"; plan that proposed to pay student loan debts in full but only 15% of other unsecured debts approved).

Cases in which separate classification and payment of student loan debt not allowed:

Nondischargeability, by itself, does not justify discrimination

In re Groves, 39 F.3d 212 (8th Cir. 1994) (nondischargeability of student loans does not, by itself, justify "substantial" discrimination against general unsecured debt; additionally, a debtor's interest in a fresh start does not justify separately classifying student loans for the sole purpose of paying those debts in a manner that prejudices other unsecured claims).

In re Sperna, 173 B.R. 654 (B.A.P. 9th Cir. 1994) (nondischargeability, on its own, is not a reasonable basis for preferential treatment of student loans and does not demonstrate that such discrimination is necessary; record in these cases did not provide a sufficient evidence to determine if discrimination in favor of student loans was unfair; at issue were two chapter 13 plans that proposed to pay student loans in full while paying other unsecured debt lesser amounts, i.e. 1.4% and 12.21%)

McCullough v. Brown, 162 B.R. 506 (N.D. Ill. 1993)(chapter 13 plans that proposed to pay nondischargeable student loans in full and other unsecured claims between 10% and 20% could not be confirmed on the basis of nondischargeability; court holds that for a plan to pass the unfair discrimination test "debtor must place something material onto the scales to show a correlative benefit to the other unsecured creditors").

In re Willis, 189 B.R. 203 (Bankr. N.D. Okla. 1995), *rev'd and remanded*, 197 B.R. 912 (N.D. Okla. 1996) (nondischargeability of student loans does not justify discriminatory treatment).

In re Colfer, 159 B.R. 602 (Bankr. D. Me. 1993) (nondischargeability does not, on its own, demonstrate that plan to separately classify and pay student loan debt in full is fair).

Student loans co-signed by parents for children do not fall into the consumer debt exception and thus must meet the unfair discrimination requirement

In re Santana, 480 B.R. 222 (Bankr. D.P.R. 2012) (limiting the application of the § 1322(b)(1) consumer debt exception to co-signed debt acquired for the benefit of the debtor rather than a co-signer, court holds that a student loan co-signed by debtor father for his son did not fall within the exception because students loans generally benefit the co-signer and not the debtor).

Fresh start and/or public policy in favor payment of student loans is not reasonable justification for discrimination

In re Birts, 2012 WL 3150384 at 4 (E.D. Va. Aug. 1, 2012) (reversing bankruptcy court approval of chapter 13 plan that proposed to pay student loans outside of the plan thereby allowing the student loan lender to be paid more than three times as much as other unsecured creditors even though the student loan debt comprised a third of total unsecured debt. Debtor's status as a single mother with three children, her generic interest in a "fresh start" and a strong public policy in favor of the federal student loan program were insufficient to justify discrimination in favor of the non-dischargeable student loan debt; no case law supported this first reason while the other reasons were not unique and exist in every bankruptcy case involving student loans).

In re Sullivan, 195 B.R. 649 (Bankr. W.D. Tex. 1996) (separate classification of student loan debt could not be justified solely on the basis that failure to pay this debt separately from other unsecured debt would interfere with debtors' fresh start; however, to the extent that the student loan debt qualified as a long-term debt under the bankruptcy code, debtors would not be prevented by "unfair discrimination" limitation from curing and maintaining student loan debt based on the terms of each individual loan).

In re Bentley, 266 B.R. 229 (B.A.P. 1st Cir. 2001) (chapter 13 plan to pay debtors' student loan debt in full but a 3.6% dividend to other unsecured creditors was unfair discrimination; debtors' interest in a fresh start did not justify discrimination in a plan that proposed to pay only the minimum required into the plan, i.e. projected disposable income over three years. Court holds that where a plan redistributes benefits and burdens to benefit the debtor but burden the credit, it can only be found fair if there is some other correlative benefit to the unsecured creditors).

In re Coonce, 213 B.R. 344 (Bankr. S.D. Ill. 1997) (court rejects debtors' assertion that discrimination is fair because if creditors were afforded equal treatment under the plan, interest accruing on the student loan debt could increase the amount due on those loans at

the conclusion of the plan thereby undermining the debtor's fresh start; debtor's fresh start must be balanced against creditors' right to fair treatment).

In re Smalberger, 157 B.R. 472 (Bankr. D. Or. 1993), aff'd, 170 B.R. 707 (D. Or. 1994) (debtor's interest in fresh start does not pass muster under unfair discrimination test for a plan that proposes to separately classify and pay student loans in full while paying nothing to unsecured creditors; court indicates that it would be open to allowing separate classification under a viability-of-the-plan theory, if the debtor can show that the discrimination is necessary for the plan to succeed).

In re Chapman, 146 B.R. 411 (Bankr. N.D. Ill. 1992) (plan that proposed, *inter alia*, to separately classify and pay student loan debt in full while paying 10% to unsecured creditors was unfair because it benefitted only the debtor at the expense of the general unsecured creditors; chapter 13 bankruptcy requires the balancing of the debtor's need for a fresh start against creditors' right to fair treatment and there was no such balancing in the debtor's plan).

In re Scheiber, 129 B.R. 604 (Bankr. D. Minn. 1991) (debtors' interest in a fresh start is not sufficient to deprive general unsecured creditors of the additional 46.5% they would receive in the absence of discrimination; plan proposed to pay student loan debt in full and 3.5% to general unsecured creditors when, in the absence of discrimination, 50% of the student loan debt prior to the completion of the plan, leaving $3,750.00 to be paid).

In re Pora, 353 B.R. 247 (Bankr. N.D. Cal. 2006) (debtor did not meet her burden, under the *Wolff* test, to show that plan to separately classify and pay 40% of student loan debt and 6% of other unsecured creditors was not unfairly discriminatory when absent separate classification, unsecured creditors would receive a dividend of 23%; debtor's interest in fresh start as well as public policy in favor of education did not justify discrimination).

In re Williams, 253 B.R. 220 (Bankr. W.D. Tenn. 2000) (court finds fresh start, nondischargeability of student loans, and fact that general unsecured creditors stood to get more in chapter 13 plan than they would in chapter 7 proceeding insufficient to justify discrimination; in ruling on the content of several plans, court holds that "it will not confirm Chapter 13 plans that provide for the payment of interest to student loan creditors but not to other unsecured creditors; that accelerate the repayment of student loans at the expense of general unsecured creditors; that provide for repayment of 100% of student loan claims when other unsecured claims are not paid at least 70%; or that provide for the repayment of student loans before other unsecured claims are paid." The court does hold, however, that it "will permit arrearages on student loans to be paid in full, even though unsecured claims will not be paid in full, if the student loan is treated as a long term debt pursuant to § 1325(b)(5)).

Avoiding harm to the debtor is not a reasonable basis for discrimination

In re Kubeczko, 2012 WL 2685115 (Bankr. D. Colo. July 6, 2012) (unfair discrimination in a chapter 13 plan that separately classified student loan debt and proposed to pay a 48.86% dividend on that claim while remaining unsecured creditors would be paid a

dividend of 0.27%. Absent the separate classification, all unsecured creditors would receive a dividend of approximately 8.06%. The fact that separate classification and payment of the student loan would have prevented debtor's default on student loans and the accrual of substantial interest was not enough to justify the discrimination).

In re Knecht, 410 B.R. 650 (Bankr. D. Mont. 2009) (debtor failed to demonstrate, under the four-factor *Wolff* test, chapter 13 plan that proposed to pay more than $36,000 to student loan debt and nothing to general unsecured creditors did not unfairly discriminate; debtor's sole basis for the discrimination was not knowing if he would live or work long enough to repay his student loan debt because of health issues but he failed to link his health issues to his life span or his ability to earn a respectable wage after completion of the plan; debtor admitted that he could carry out the plan without the discrimination; there was no evidence that the plan was proposed in good faith; and no evidence that the proposed discrimination was related to the basis or rationale for the discrimination).

Discrimination unfair in the absence of proof that it is necessary or reasonable

In re Thibodeau, 248 B.R. 699 (Bankr. D. Mass. 2000) (debtor failed, under *Leser* test, to demonstrate that plan to separately classify and fully pay student loan arrearages, maintain student loan payments outside of plan and pay a 27% dividend on other general unsecured claims, while devoting less than the full amount of debtor's net disposable income to payments under the plan, did not unfairly discriminate).

In re Gonzalez, 206 B.R. 239 (Bankr. S.D. Fla. 1997) (chapter 13 plan that proposed to pay student loan debt in full and a 6% dividend to unsecured creditors could not be confirmed because debtor's offered no proof of the discrimination being "fair" or "necessary").

In re Renteria, 2012 WL 1439104 (Bankr. D. Colo. Apr. 26, 2012) (below median income debtors' chapter 13 plan to separately classify student loans to allow for 64% repayment of those claims over 60 month period versus a 1% repayment of all other unsecured claims constituted unfair discrimination under the *King/Simmons* test and *Machado* framework. The Plan failed under *King/Simmons* because the general unsecured creditors would receive less than they would absent the separate classification, i.e. 1% versus 12%. It also failed under *Machado* because the debtors did not propose to cure student loan arrearages and there was no evidence that the discriminatory treatment was necessary to ensure the debtors would not be worse off at the end of the Plan).

In re Sutton, 2012 WL 433480 (Bankr. E.D. N.C. Feb. 9, 2012) (unfair discrimination in chapter 11 plan that proposed to separately classify student loan debt and pay in full while only paying 3.8% of debt owed to all other unsecured creditors; debtor failed to provide evidence as to a reasonable basis for discrimination as analyzed through the four factor test in *Ownby*.)

In re Furlow, 70 B.R. 973 (Bankr. E.D. Pa. 1987) (court holds that different treatment of unsecured debt is permissible and, thus not unfairly discriminatory, if the debtor provides a reasonable basis for the degree of discrimination in the plan; here, debtor failed to provide a reasonable basis for a plan that proposed to separately classify and pay 40% of student loan debt and only 10% of other unsecured claims but was given further opportunity by the court to justify her plan).

In re Simmons, 288 B.R. 737 (Bankr. N.D. Tex. 2003) (in consolidated action, court notes that determination of whether a chapter 13 plan unfairly discriminates is based on a comparison between what unsecured creditors would receive under a proposed plan with the amount they would receive from the Debtor's disposable income over the first 36 months of the plan if there was no separate classification; court finds that plan that proposed to pay unsecured creditors nothing was unfairly discriminatory and holds that for another plan, student loan debt could not be classified as a personal expense for the purposes of allowing it to receive a 65% dividend while unsecured creditors received 6.35% and would otherwise be paid 11.1%).