Repayment Options: Income Based Repayment and New Lender/Servicer Programs

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What Qualifies as a Loan under Section 523(a)(8) of the Bankruptcy Code?

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I. BRIEF OVERVIEW OF SECTION 523(A)(8) OF THE BANKRUPTCY CODE

IT IS A CENTRAL TENET OF MODERN U.S. BANKRUPTCY LAW THAT "THE 'HONEST BUT UNFORTUNATE DEBTOR' HAS A RIGHT TO BANKRUPTCY'S 'FRESH START.'" THIS FUNDAMENTAL PRINCIPLE DOES NOT, HOWEVER, APPLY TO THE "HONEST BUT UNFORTUNATE DEBTOR" WHO CANNOT PAY HIS STUDENT LOANS. RATHER, SECTION 523(A)(8) OF THE BANKRUPTCY CODE PROVIDES THAT, "UNLESS EXCEPTING SUCH DEBT FROM DISCHARGE . . . WOULD IMPOSE AN UNDUE BURDEN ON THE DEBTOR AND THE DEBTOR'S DEPENDENTS," A DEBTOR IS NOT ENTITLED TO A DISCHARGE OF HIS OR HER STUDENT-LOAN DEBT.

ALTHOUGH THE ISSUE OF WHETHER REPAYMENT CONSTITUTES AN UNDUE HARDSHIP ARISES WITH GREAT FREQUENCY IN BANKRUPTCY COURTS, A THRESHOLD ISSUE THAT MUST FIRST BE ADDRESSED IS WHETHER THE LOAN QUALIFIES AS AN EDUCATIONAL LOAN IN THE FIRST PLACE. SECTION 523(A)(8) PROTECTS AT LEAST THREE, AND MAYBE FOUR, CATEGORIES OF EDUCATIONAL LOANS FROM DISCHARGE:

- loans made, insured, or guaranteed by a governmental unit;
- loans made under any program partially or fully funded by a government unit or nonprofit institution;
- any "qualified educational loan" as that term is defined in the Internal Revenue Code; and
- loans received as an educational benefit, scholarship, or stipend.[1]

The latter of these categories has caused the most controversy. To understand the issue, a brief examination of the legislative history is required.

II. Expanded Definition of Student Loans Under BAPCPA

Before the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), section 523(a)(8) of the Bankruptcy Code only applied to obligations for funds received from governmental or nonprofit institutions. Specifically, section 523(a)(8) of the Bankruptcy Code read as follows:

1 *See Rumer v. Am. Educ. Servs. (In re Rumer)*, 469 B.R. 553, 561 (Bankr. M.D. Pa. 2012).

> (a) A discharge under section 727, 1141, 1228(a), 1228(b), 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 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.

In 2005, Congress expanded the scope of nondischargeable debts under this section to recognize an important role played by private institutions in providing educational funding for students. Specifically, BAPCPA made the following changes, with emphasis on the changes:

> (a) A discharge under section 727, 1141, 1228(a), 1228(b), 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)*** for an educational benefit overpayment or loan made, insured or guaranteed by a governmental unit, or made under any program funded in whole or part by a governmental unit or nonprofit institution, ***or***
>
> ***(ii)*** for an obligation to repay funds received as an educational benefit, scholarship or stipend; ***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.***

As a result of these amendments, some courts have reached the conclusion that BAPCPA's separation of the phrase "obligation to repay funds received as an educational benefit" from the phrases "loan made, insured or guaranteed by a governmental unit" and "program funded in whole or in part by a nonprofit institution" in section 523(a)(8)(A)(i) of the Bankruptcy Code, must be read as encompassing a broader range of educational benefit obligations. *See In re Daymon*, 2013 Bankr. LEXIS 1387, at **10–11 (Bankr. N.D. Ill. Apr. 2, 2013) (concluding that employer-sponsored tuition reimbursement programs qualify under section 523(a)(8)(A)(ii)); *In re Belforte*, 2012 Bankr. LEXIS 4574, at **16–17 (Bankr. D. Mass. Oct. 1, 2012); *In re Roy*, 2010 Bankr. LEXIS 1218, 2010 WL 1523996 , at * 1 (Bankr. D. N.J. Apr. 15, 2010); *In re Baiocchi*, 389 B.R. 828, 831–32 (Bankr. E.D. Wis. 2008). Based on this conclusion, some courts have held that *any loan* made for the specified purpose of providing an "educational benefit" would be nondischargeable, even if such loan does not qualify under Section 523(a)(8)(A)(i) or 523(a)(8)(B).

III. Qualified Educational Loans

Government-backed or college-backed loans have long been the subject of section 523(a)(8) of the Bankruptcy Code, however, the new subsection (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 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 noting. For instance, some of the more common ways in which an education loan may fail to satisfy the requirements of a qualified education loan include: (1) use at a college that is not a Title IV institution (i.e., a college that is subject to a program participation agreement under 20 U.S.C. § 108711); (2) use for costs not included within the definition of cost of attendance or in excess of the expected family contribution (or cost of attendance minus aid received); (3) use for study abroad not approved for credit by the home institution; (4) use for rental or purchase of equipment, materials or supplies that are not required by the institution; (5) use for purchase of a computer without obtaining an adjustment to cost of attendance from the college for the cost of the computer; and (6) use for a previous year's school charges.

IV. The Dischargeability of Tuition Receivables

An issue that is not often discussed is whether a debtor may discharge his or her tuition receivable. The few courts that have addressed this issue have generally agreed that such debt may be discharged, unless the creditor establishes the existence of a "loan" between the parties. An examination of the applicable case law is helpful.

In *Cazenovia College v. Renshaw (In re Renshaw)*, 222 F.3d 82 (2d Cir. 2000), the Second Circuit applied the classic definition of a loan: "To constitute a loan there must be (i) a contract, whereby (ii) one party transfers a defined quantity of money, goods, or services to another, and (iii) the other party agrees to pay for the sum or items transferred at a later date. This definition implies that the contract to transfer items in return for payment later must be reached before or contemporaneous with the transfer. When such is the intent of the parties, the transaction will be considered a loan regardless of its form. . . . Absent such an agreement, failure to pay a bill when due does not create a loan." 222 F.3d at 88 (citing *In re Grand Union Co.,* 219 F. 353, 356 (2d Cir. 1914)).

Simply put, nonpayment of tuition qualifies as a loan "'in two classes of cases'": "'where funds have changed hands,' or where 'there is an agreement . . . whereby the college extends credit.'" *Boston University v. Mehta (In re Mehta)*, 310 F.3d 308, 314 (3d Cir. 2002) (quoting *Renshaw*, 222 F.3d at 90). Applying the common law definition of a loan, the Second, Third, and Seventh Circuits have held that an unpaid tuition balance that is not evidenced by a promissory note or any other agreement does not qualify as an educational loan under section 523(a)(8) of the Bankruptcy Code and, therefore, may be discharged in the bankruptcy proceedings. *See In re Chambers*, 348 F.3d 650 (7th Cir. 2003); *In re Mehta*, 310 F.3d 308; *In re Renshaw*, 222 F.3d 82.

If, however, an unpaid tuition balance is evidenced by a promissory note or any other agreement, and such note is executed before or contemporaneous with the transfer, some courts have held that such agreement falls

within the exception set forth in section 523(a)(8) of the Bankruptcy Code.

In *DePasquale v. Boston University School of Dentistry (In re DePasquale)*, 225 B.R. 830 (B.A.P. 1st Cir. 1998), a Boston University student attended classes without paying her tuition. The student later filed a voluntary Chapter 7 petition. Although the facts of that case are somewhat vague, it is clear that the student agreed to pay the school for her tuition, although no payment schedule was set. As a condition to receive her degree, the university insisted that she sign a "Promissory Agreement" in which she promised to pay Boston University the unpaid tuition.

In her bankruptcy proceeding, the student sought a determination that the tuition debt was dischargeable. The bankruptcy court granted summary judgment in favor of the student, and Boston University appealed. The bankruptcy court determined that the deal between the parties was a "credit extension" as opposed to a loan. Because the statute requires the loan to be made under a "funded" program, the court reasoned that money must be paid over to the student. *Id.* at 831–32.

On review, the Bankruptcy Appellate Panel for the First Circuit rejected the student's contention that her promise to pay the tuition at a later date did not constitute a loan. The Panel instead held that the existence of a loan would be determined based upon the "substance of the transaction that created the obligation in question." The Panel further held that "[i]f a qualified institution or agency provides funds, credit, or financial accommodations to a debtor for educational purposes under a contemporaneous, mutual understanding of future repayment, the arrangement may be a loan within the statute's meaning, whether or not funds, as such, were advanced."

In *Johnson v. Missouri Baptist College*, 218 B.R. 449 (B.A.P. 8th Cir. 1998), a college extended credit to a student for tuition, books, and other expenses, for which the student executed a promissory note. The student filed a Chapter 13 bankruptcy petition, and the bankruptcy court determined that the debt to the college was a "loan" under section 523(a)(8) of the Bankruptcy Code and was nondischargeable. On appeal, the parties stipulated that the college was a nonprofit institution and that the credit was extended for educational purposes under a "program."

The Bankruptcy Appellate Panel for the Eighth Circuit reviewed the long history and policies behind the section, which was primarily to ensure the continuance of educational loan programs and reflect a congressional policy to limit the dischargeability of educational obligations. The Panel reviewed several dictionary definitions of the term "loan," including "something lent for the borrower's temporary use on condition that it or its equivalent be returned."

The Panel concluded that the term does not require the exchange of funds between lender and borrower. By allowing the student to attend classes, the Panel observed, the college in effect advanced funds or credits to the student's account, which the student drew upon by class attendance. That Panel also emphasized that the student had signed a promissory note to evidence her debt, implying at the very least that the intent of the parties to create an obligation to repay was essential to the definition.

In *Chambers*, the Seventh Circuit noted that educational institutions may avoid having a tuition receivable discharged by taking simple precautions. For instance, when students fail to pay tuition bills on time, institutions can withhold educational services until payment, or they can enter into a separate agreement to accept later payment. A separate agreement to accept later payment would create a loan and would be excepted from discharge under section 523(a)(8) of the Bankruptcy Code. 348 F.3d at 658.

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Administrative Alternatives to Bankruptcy Discharge of Student Loan Debt

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I. GENERAL OVERVIEW OF STUDENT LOANS

A. Higher Education Act of 1965: In 1965, Congress, in response to a perceived need for financial assistance to students in higher education, passed the Higher Education Act of 1965 (HEA). The purpose of the HEA is to "keep the college door open to all students of ability," regardless of socioeconomic background.

B. (There Were) Two Federal Student Loan Programs: The HEA governs two federally-backed student loan programs: the Federal Family Education Loan Program (FFEL Program) and the William D. Direct Loan Program (Direct Loan Program). Under the Health Care and Education Reconciliation Act of 2010, Congress eliminated the FFEL Program, effective July 1, 2010. Currently, the total debt at stake in the two federal student loan programs is an estimated 1.2 trillion dollars.

1. FFEL Program: Under the FFEL Program, eligible lenders make guaranteed loans on favorable terms to students or parents to help finance student education. The loans are guaranteed by guaranty agencies (state agencies or private non-profit corporations), which are ultimately reinsured by the United States Department of Education (ED).

2. The Direct Loan Program: Under the Direct Loan Program, ED makes loans directly from the federal treasury to student and parent borrowers.

C. Types of Federal Loans:

1. HEA: Loans under the HEA include Perkins Loans, Stafford (subsidized and unsubsidized) Loans, PLUS Loans and Consolidation Loans. Grants include Pell Grants and Supplemental Education Opportunity Grants. The terms of Stafford, PLUS and Consolidation loans in both the FFEL Program and the Direct Loan Program are similar except that the Direct Loan Program offers a Public Service Loan Forgiveness program and two income-related payment options (income based and income contingent). *See infra* at II.G., III.B.

2. Health and Human Services Loans: The United States Department of Health and Human Services (DHHS) also administered a student loan program, Health Education Access Loan program, (HEAL), for borrowers engaged in health related studies. This program is no longer active. Like FFEL Program loans, HEAL loans are also presumptively nondischargeable. Courts have construed the dischargeability standard of "unconscionability" for HEAL loans as being a "higher standard" than that of FFEL Program/Direct Loan loans, which require a showing of "undue hardship." Even though HEAL loans are administered by DHHS, HEAL loans are eligible for consolidation along with FFEL Program loans in the Direct Loan program.

D. Non-HEA Loans: Private Loans: Private loan programs have also emerged on the scene to provide educational funds to students who have exhausted their federal loan limits or are otherwise ineligible to borrow under the federal loan programs. Private loans are not eligible for administrative relief discussed below and may not be consolidated under federally-backed

consolidation programs. The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, however, expressly included private loans in the presumption of nondischargeability under 11 U.S.C. § 523(a)(8).

II. NONBANKRUPTCY RELIEF

There are numerous administrative remedies for student loan borrowers to consider in lieu of seeking discharge under § 523(a)(8). Unlike relief under 11 U.S.C § 523(a)(8), borrowers may be entitled to administrative relief irrespective of whether they've filed bankruptcy. But these administrative options require administrative determinations and, thus, should not be the basis for claim objections or adversary proceedings in a bankruptcy context.[1]

A. Total and Permanent Disability Discharge (TPD):

1. Eligibility Criteria: Borrowers may be eligible to have their federal student loan debt discharged because of a total and permanent disability.

a. TPD application: A medical doctor or doctor of osteopathy must certify that the borrower (1) is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment that (i) can be expected to result in death;(ii) has lasted for a continuous period of not less than 60 months; o r(iii) can be expected to last for a continuous period of not less than 60 months; or (2) has been determined by the Secretary of Veterans Affairs to be unemployable due to a service-connected disability.

b. Social security award letter: As of July 1, 2013, borrowers who receive Social Security Disability Insurance (SSDI) or Supplemental Security Income (SSI) benefits may use their SSA award letter in lieu of obtaining a separate certification from a physician on the TPD discharge application. The letter must state that the borrower's next scheduled disability review will be within 5 to 7 years from the date of the most recent SSA disability determination. Borrowers may also submit a Benefits Planning Query (BPQY) that can be obtained by calling 800.772.1213.

ED has designated Nelnet as its disability servicer for all TPD applications submitted after July 1, 2013. Under the new TPD process, borrowers must submit a single TPD discharge application directly to ED/Nelnet rather than to their individual loan holders. Borrowers may initiate the TPD process by going to www.disabilitydischarge.com.

[1] The discharge provisions described here are illustrative only of the administrative relief available under the HEA. For full detail of requirements necessary for relief, see 34 C.F.R. §§ 682.100 *et seq.*, 685.100 *et seq.* These administrative options are available for both FFEL Program and Direct Loan Program loans unless otherwise noted.

If the TPD request is approved, the account is immediately discharged by ED.[2] The three-year post-discharge monitoring period remains in effect. During this three-year period, borrowers cannot earn more than 100% of the federal poverty guidelines for a family of two (in 2013 = $15,510) and cannot have obtained any new federal student loans. Typically, Nelnet will contact the borrower when the three-year mark is approaching to update the disability status and financial status to ensure that the borrower's discharge criteria have not changed.

2. Veterans with service-connected disabilities: Veterans who have a 100% service-connected disability are immediately eligible for discharge of their federal student loan debt without further certification under the TPD regulation. They need only provide their Veteran's Administration disability rating paperwork to the loan holder who will process the discharge.

B. Loan Rehabilitation: Federal regulations allow borrowers who default on repayment of their loan a one-time opportunity to bring their loans out of a default status and repair the negative credit information reported to credit bureaus. Payment amounts are set at a reasonable rate and borrowers must make nine consecutive on-time payments over a 10-month period. Completing rehabilitation restores a borrower's loans to good standing and helps to repair credit. Entering a loan rehabilitation agreement has immediate effect on a borrower's defaulted loans: it stops all collections activity and legal proceedings, prevents wage garnishment, and it may protect a borrower's state and federal tax refunds from IRS offsets.

Successfully completing a loan rehabilitation program restores loans to their pre-default status, it reestablishes eligibility for deferment, forbearance, alternative repayment options, title IV financial aid, resets loans to their original terms, interest rate, and repayment period, minus the 9-month rehabilitation period, and shows positive payment progress on a borrower's credit report, which may repair some of the damage done by default.

C. Closed School Discharge: Borrowers whose school closed before they could complete the program of study may be eligible for discharge. The borrower must show they were enrolled at the time of closure or that they withdrew from the school not more than 90 days prior to the date the school closed and that they were unable to complete the program of study through a teach-out at another school or by transferring academic credits or hours earned at the closed school to another school.

D. False Certification Discharge: A borrower's student loans can be discharged if a school falsely certified the student's eligibility for a federal student loan on the basis of ability to benefit from the education, signed the borrower's name without authorization by the borrower on

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[2] Under the Internal Revenue Code, student loan debt forgiven or discharged by TPD may constitute a taxable event. This is a nonissue in most cases because any forgiven debt is taxable only to the extent the borrower is solvent. Thus, it is unlikely that borrowers with large student loan debts will have assets that exceed the debt discharged by TPD.

the loan application or promissory note, or someone else obtained a federal student loan because of identity theft.

E. Death Discharge: If an individual borrower dies, or the student for whom a parent received a PLUS loan dies, the obligation of the borrower and any endorser to make any further payments on the loan is discharged."

F. Teacher Loan Forgiveness Program: Teachers who meet the requirements in 34 C.F.R. § 685.217 are eligible for forgiveness of up to $17,500. Typically, this provision is for teachers in low-income areas and those who teach math or science at schools designated eligible by the U.S. Department of Education. (Direct Loan Program loans only).

G. Public Service Loan Forgiveness: Borrowers who make 120 qualifying payments under the IBR, ICR, or 10-year fixed payment schedule while employed in the public sector are eligible to have any balance remaining on their student loan debt forgiven. Public service includes employment with most local, state, federal, tribunal nation, or § 501(c)(3) corporations. (Direct Loan Program loans only).

H. September 11 Survivors Discharge: Survivors of or eligible victims of the September 11 attacks may request discharge of their student loan debt. (Direct Loan Program loans only).

I. Administrative Discharges Specific to Perkins Loans: In addition to the above-mentioned non-bankruptcy discharge options, borrowers may also request discharge or forgiveness of their Perkins Loans for the following reasons:

- full-time teacher in elementary school serving students from low-income families (up to 100%);
- full-time special education teacher (up to 100%);
- full-time qualified professional provider of early intervention services for the disabled (up to 100%);
- full-time teacher of math, science, foreign language, bilingual education, etc. in designated teacher shortage area (up to 100%);
- full-time employee of public or nonprofit child or family-services agency for high-risk children and families from low-income areas (up to 100%);
- full-time nurse or medical technician (up to 100%);
- full-time law enforcement or corrections officer (up to 100%);
- full-time staff member in education component of Head Start Program (up to 100%);
- VISTA or Peace Corps volunteer (up to 70%);

- Service in the U.S. Armed Forces (up to 50% in areas of hostilities or imminent danger);
- full-time teacher in designated educational service agency serving students from low-income families (up to 100%);
- full-time staff in prekindergarten or child care program licensed or regulated by State (up to 100%);
- full-time firefighter (up to 100%);
- full-time faculty member at TribalCollege or University (up to 100%);
- full-time speech pathologist with master's degree working in Title I-eligibility elementary or secondary school (up to 100%);
- librarian (master's degree) working in Title I-eligibile elementary or secondary school or public library serving title-eligible schools (up to 100%);
- full-time attorney working in public or community defender organization (up to 100%).

III. FLEXIBLE, AFFORDABLE PAYMENT OPTIONS: INSIDE OR OUTSIDE OF BANKRUPTCY

Both the FFEL Program and the Direct Loan Program have flexible, affordable payment options for borrowers who have financial hardship. These payment options are available whether or not the borrower has filed bankruptcy. ECMC will always rely on the most affordable payment amount available to the borrower when defending undue hardship discharge cases.

A. Consolidation: Consolidation benefits a borrower by spreading the payments over a term of up to 30 years, depending on the total loan balance. Since July 1, 2010, consolidations are available only in the Direct Loan Program. Borrowers who have previously consolidated their loans in the FFEL Program may reconsolidate their loans (even if defaulted) into the Direct Loan Program but not vice-versa.

B. Income-Driven Payments: In addition to fixed, amortized extended payment terms, there are two payments options that are based on a borrower's income and family size: the Income Based Repayment plan (IBR) (available in both the FFEL and Direct Loan Program) and the Income Contingent Repayment plan (ICR) (available only in the Direct Loan Program).

1. Income Based Repayment:

a. Eligibility for IBR: Defaulted student loans, PLUS loans, or federal consolidation loans that contain underlying PLUS loans or a mix of Stafford loans and PLUS loans are not eligible for the IBR in either the FFEL Program or the Direct Loan Program.

Stand-alone Perkins loans are also not eligible for the IBR. But a borrower may include a Perkins loan in a consolidation loan that will be IBR-eligible.

Borrowers who have defaulted FFEL Program loans may re-consolidate their defaulted loans into the Direct Loan Program and elect the IBR in the Direct Loan Program. (Re-consolidating removes the default because the borrower has a new loan). Borrowers also have a one-time opportunity to rehabilitate their loan to remove the default status and be eligible for the IBR in either federal student loan program. *See supra* II.B.

b. Borrowers who have IBR-eligible loans must first demonstrate partial financial hardship (PFH). Borrowers can demonstrate PFH if the annual amount due on all eligible student loans under a 10-year repayment schedule is more than 15% of their adjusted gross income (AGI). Most borrowers whose total loan balance exceeds their annual earnings will satisfy the PFH requirement.

The IBR payment is calculated using the borrower's AGI and family size. If the borrower earns less than 150% of the poverty level for their family size, the IBR payment will be $0. The required annual loan payment under the IBR is capped at 15% of earnings above 150% of the applicable poverty level. Because the monthly IBR payment is calculated as a percentage of the borrower's income, if the borrower's income drops, the monthly payment is reduced accordingly.

The IBR payment is recalculated annually based on household income. Married borrowers who file separate tax returns have their IBR payments based on their own respective incomes but may still count each other and any dependents in the family size. Borrowers may contact their lender/servicer at any time if they experience a change in financial circumstances that could impact their required IBR payment. The IBR repayment period is 25 years. At the conclusion of the 25-year repayment period, any remaining balance is forgiven.[3] *But see infra* III.B.3 (discussing 10-year repayment term for the Public Service Loan Forgiveness Program).

2. Income Contingent Repayment: Like the IBR, the ICR is recalculated annually and the payment amount is based on 20% of the difference between a borrower's AGI and 100% of the federal poverty level for the family size. If the AGI is below 100% of the poverty level for the borrower's family size, then the ICR payment is $0. The ICR is the only income-driven payment option available to PLUS loan borrowers or to borrowers who have defaulted loans in the Direct Loan Program. The ICR is always based on household income regardless of tax filing status. After 25 years, any balance that is remaining is forgiven by the Secretary of Education. *See* Note 3.

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[3] Under the Internal Revenue Code, student loan debt forgiven at the end of the IBR (and ICR, discussed *infra*) term may constitute a taxable event. This is a nonissue in most cases because any forgiven debt is taxable only to the extent the borrower is solvent. Thus, it is unlikely that borrowers with large student loan debts will have assets that exceed the debt forgiven 25 years into the future.

3. Public Service Loan Forgiveness: Borrowers who make 120 qualifying payments under the IBR, ICR, or 10-year fixed payment schedule while employed in the public sector are eligible to have any balance remaining on their student loan debt forgiven. Public service includes employment with most local, state, federal, tribunal nation, or § 501(c)(3) corporations. There is specific language in this regulation that exempts any forgiven debt from constituting a taxable event. (Direct Loan Program loans only).

C. Alternative Payment Arrangements: Borrowers who believe that none of the payment options are suitable may request an alternative repayment plan from the Secretary of Education. *See* 34 C.F.R. § 685.208(g).

D. Suspension of Payments: In addition to the different types of repayment plans, borrowers may seek deferment or forbearance. Deferment or forbearance may be granted for specific bases stated in federal regulations, which include, but are not limited to, poor health, economic hardship, federal student loan payments that are equal to or greater than 20% of monthly gross income, or other reasons acceptable to ED.

During a deferment period, no interest accrues on subsidized loans, but interest continues to accrue on unsubsidized loans. The borrower may pay the accruing interest on any unsubsidized loans or have it added to the principal when the deferment expires. Forbearance postpones or reduces the monthly repayment for a limited, specific period, during which interest on subsidized and unsubsidized loans continues to accrue. If the interest is not paid during the forbearance, it is added to the principal balance when the forbearance period ends.

IV. ADMINISTRATIVE REMEDIES v. § 523(a)(8): IS THERE COMMON GROUND?

A. Exhaustion of Administrative Remedies: In general, individuals must exhaust all administrative remedies available under a statute before resorting to judicial review. *See, e.g.*, *Myers v. Bethlehem Shipbuilding Corp.,* 303 U.S.41, 50-51 (1938). This rule both protects administrative authority and promotes judicial efficiency. *McCarthy v. Madigan,* 503 U.S. 140, 145 (1992) ("Agencies, not the courts, ought to have primary responsibility for the programs that Congress has charged them to administer.").

B. Interplay of Administrative Remedies and the Bankruptcy Code: There is growing tension about the significance administrative remedies should play in a bankruptcy court's judicial determination of student loan dischargeability matters. Fundamental principles of statutory construction require courts to construe statutes harmoniously to avoid absurd results:

> If a literal construction of the words of a statute be absurd, the act must be so construed as to avoid the absurdity. The court must restrain the words. The object designed to be reached by the act must limit and control the literal import of the terms and phrases employed.

Rector, etc. of Holy Trinity Church v. United States, 143 U.S. 457, 460 (1892). It is unlikely that Congress intended administrative remedies to supplant legal remedies in 11 U.S.C. § 523(a)(8) or vice versa. The majority view is that administrative programs, especially the IBR and ICR, while not dispositive on the "good faith" prong of *Brunner*, must be considered an important component of the undue hardship analysis.*See infra* V.C.

1. Failure to consider or pursue IBR/ICR favors nondischargeability:[4]

a. First Circuit:

***Ayele v. Educ. Credit Mgmt. Corp.*, 468 B.R. 24 (Bankr. D. Mass. 2012), *aff'd* 2013 WL 1200326 (D. Mass. Mar. 2013).** Availability of IBR supported determination that student loan was non-dischargeable; however, court ruled under § 105(a) that if debtor enrolled in and abided by the terms of the IBR, any remaining debt at the expiration of the plan was discharged (same IBR holding as *Stevenson*; both opinions were authored by Judge Feeney).

***Stevenson v. Educ. Credit Mgmt. Corp.*, 463 B.R. 586 (Bankr. D. Mass 2011), *aff'd* 475 B.R. 286 (D. Mass.2012).** Availability of IBR supported determination that student loan was non-dischargeable; however, court ruled under § 105(a) that if debtor enrolled in and abided by the terms of the IBR, any remaining debt at the expiration of the plan was discharged.

b. Second Circuit:

***In re Hixson*, 450 B.R. 9 (Bankr. S.D.N.Y. 2011).** Chapter 7 debtor who had at least $1,272 of disposable income per month and a required ICR

[4] The following circuit-level cases have held that the IBR and ICR are an important consideration in the undue hardship analysis: *Educ. Credit Mgmt. Corp. v. Jesperson (In re Jesperson)*, 571 F.3d 775, 783 (8th Cir. 2009) ("When a debtor is eligible for the ICR, the court in determining undue hardship should be less concerned that future income may decline. The ICR formula adjusts for such declines, without regard to the unpaid student loan balance, which in most cases will avoid undue hardship"); *Educ. Credit Mgmt. Corp. v. Mason (In re Mason)*, 464 F.3d 878, 885 (9th Cir. 2006) (debtor failed good faith prong in part because of failing to pursue the alternative payment arrangements with any diligence); *Educ. Credit Mgmt Corp. v. Frushour (In re Frushour)*, 433 F.3d 393, 396-397 (4th Cir. 2005) (failure to seek out loan consolidation options to make the debt less onerous is an important inquiry in good faith); *Tirch v. Pa. Higher Educ. Assistance Agency (In re Tirch)*, 409 F.3d 677, 682 (6th Cir. 2005) (although not necessarily a per se indication of bad faith, failure to take advantage of the ICR is certainly probative of his intent to repay and is a "difficult, although not necessarily insurmountable burden" to overcome); *Alderete v. Educ. Credit Mgmt Corp. (In re Alderete)*, 412 F.3d 1200, 1206 (10th Cir. 2005) (failing to consider alternative repayment options indicative of bad faith).

payment of $808 did not satisfy the "minimal standard of living," prong of *Brunner* test.

c. Third Circuit:

***In re Lepre*, 466 B.R. 727 (Bankr. W.D. Pa. 2012), *aff'd* No. 12-545 (W.D. Pa. Mar. 25, 2013).**Chapter 7 debtor seeking to discharge his student loan debt failed to make requisite showing of "good faith" effort to repay loans, given lack of evidence of any payments on loans or of any effort on his part to seek adjustment, deferment or forbearance, or to seek to consolidate his student loans.

***Goforth v. U.S. Dept. of Educ.*, 466 B.R. 328 (Bankr. W.D. Pa. 2012).**Chapter 7 debtors' failure to participate in voluntary repayment program that would have reduced their monthly student loan payments to more manageable level, along with the short interval between initial due date for consolidated student loan debt and debtors' Chapter 7 filing and the fact that student loan debt constituted about 72% of debtors' unsecured debt and appeared to be significant factor in their bankruptcy filing, supported finding that debtors had not made good faith effort to repay their student loans and prevented discharge of this debt on "undue hardship" theory.

***In re Armstrong*, 394 B.R. 43 (Bankr. M.D. Pa. 2008).** The court granted summary judgment for the creditors, largely because of debtor's failure to demonstrate good faith. It held that the court must consider two factors when examining debtor's good faith efforts: (1) whether the debtor incurred substantial expenses beyond those required to pay for basic necessities; and (2) whether the debtor made efforts to restructure her loan before filing her petition in bankruptcy. Here, the court held that the debtor had made many discretionary purchases while refusing to make even a single payment on her student loans, including money to dine out, video games, fireworks, movies, music, and sporting goods. "Debtor made a conscious decision to ignore her student loan debts in favor of making consumer purchases for the benefit of herself and her children." Moreover, the debtor had not made any efforts to repay her student loans—as testified in her deposition, failed to seek out alternative repayment options, and filed her bankruptcy case within seven months of filling out her last student loan application.

d. Fourth Circuit:

***Velarde v. Educ. Credit Mgmt. Corp. (In re Velarde)*, 2009 WL 2614688 (Bankr. E.D. Va. Aug. 23, 2009)**. Debtor's annual income was marginally above the Federal poverty level. The debtor put in very little evidence concerning her expenses, so the court utilized the expenses listed

in her schedules despite the fact that court believed her listed expenses were likely understated. Nevertheless, the debtor's schedules indicated a net surplus of $213. With a surplus of $213, the debtor could afford each of the four repayment option under the Ford Program and thus was not entitled to a discharge.

***Sperrazza v. Univ. of Md.*, Civ. No. 07-792, 2008 WL 818616 (E.D. Pa. Mar. 24, 2008).** The District Court affirmed the bankruptcy court's determination that a debtor who had made no voluntary payments on his debt, had not sought to restructure his loans, had made several payments to his parents (and so "demonstrate[d] that he has some concept of what it is to repay a debt") but not on his student loan debts, and had contributed over $2,000 to a retirement savings plan – all suggested that he had no interest in repaying his student loans. Further, because the Court "faced a debtor who has testified under oath that he is actively choosing not to work so that he can avoid payment of his educational debts," it held that "[i]f the *Faish* test is to retain any integrity whatsoever, it has to be that [debtor] has not demonstrated a good faith effort to repay his debts."

e. Fifth Circuit:

***Educ. Credit Mgmt. Corp. v. Young*, 376 B.R. 795 (E.D. Tex. 2007)**. Debtor, an attorney, who owed nearly $235,000 was unable to establish good faith efforts because he failed to minimize his expenses—namely his monthly $220 contribution to his 401(k), because "[w]hile saving money for one's retirement is certainly wise, Congress, through its demanding standard, has chosen to give priority to the repayment of student loan debts" and his food expenditures (approximately $650/month for him and his 12-year old son). The court also found it germane that Debtor had failed to maximize his income in that he had not yet obtained his law license in Texas, failed to investigate the Ford consolidation plan, but instead researched bankruptcy discharge, and never increased his $50 monthly payments to his student loans even when his salary increased by $16,000 annually.

***Jones v. Bank One Tex.*, 376 B.R. 130 (W.D. Tex. 2007)**. Although debtor has no legal obligation to apply to the ICR, the debtor's effort to pursue options to make her debt less onerous is an important indicator of good faith. "Debtor's reason that she does not have disposable income to make payments under the ICR lacks merit because at this time she would owe zero dollars ($0)." Debtor did not have ample justifications for "refusing to take a simple step that would have allowed her to fulfill her commitments in a manageable way."

f. Sixth Circuit:

***In re Malone*, 469 B.R. 768 (Bankr. N.D. Ohio 2012).** The debtor did not establish that he made requisite good-faith effort to repay debt; debtor made only one payment on his student loan obligation and filed for bankruptcy relief less than one year after graduating, majority of debtor's unsecured debt consisted of his student loan obligations, and debtor did not offer sufficient explanation for his quick resort to bankruptcy, particularly since debtor, although not using his degree, had salary consistent with his expectations in obtaining degree, such that his financial situation did not arise as a result of events beyond his control.

***In re Goodman*, 449 B.R. 287, 297 (Bankr. N.D. Ohio 2011).** The DOE offered to agree to discharge any portion of the student loan debt outstanding following completion of the ICR or IBR. The court found a lack of a good faith effort to repay the loans because the debtors refused to take part in either program and because no payments had been made in nearly fifteen years.

***In re Roberts*, 442 B.R. 116 (Bankr. N.D. Ohio 2010).** While debtor did not have present ability to repay her nearly $200,000 in student loan debt, debtor's lack of good faith effort to repay debt, as demonstrated by fact that she had made only two minor payments eight years earlier and that she was currently enrolled in IRCP under which her monthly payment was $0.00, prevented debtor from obtaining an undue hardship discharge. Another factor that weighed against a finding of good faith was that the debtor and her husband had continued to receive student loans (in combined amount of more than $400,000) even while the circumstances that allegedly prevented them from repaying the debt were in existence (the birth of five children, three of whom had special needs).

***Sanborn v. Educ. Credit Mgmt. Corp. (In re Sanborn)*, 431 B.R. 5 (Bankr. D. Mass. 2010)**. Despite having medical testimony evidencing a chronic, but fluctuating disease (chronic fatigue/myalgic encephalomyelitis), the court found that the availability of the ICR program, "it appears that nondischarge [sic] of the loan likely would not impose on the Debtor a payment obligation that is greater than her ability pay during periods of continuing disability, and the Court therefore concludes that the continuance of her medical disability for the indefinite future has not been shown to constitute an undue hardship."

***In re Gibson*, 428 B.R. 385 (Bankr. W.D. Mich. 2010).** Debtor failed the third prong because she refused the consolidation options, particularly the ICR "explaining that she regarded the repayment trigger levels as 'arbitrary'" The court found that "In other words, she believes that her obligation to begin repaying the loans would commence, under the

programs, before her income would support a middle class lifestyle *and* repayment." The court held that these repayment plans are a product of regulation, not negotiation. The debtor also found a 25-year repayment period contrary to a "fresh start." The court rejected this stating, this "ignores the fact that student loans are excepted from the Chapter 13 discharge." Finally, the court rejected the debtor's concerns regarding the possible tax implications of the ICR's forgiveness of debt.

g. Seventh Circuit:

***Educ. Credit Mgmt. Corp. v. Vargas*, 2010 WL 5395142 (C.D. Ill. 2010).** The district court reversed the lower court's discharge, finding that the debtor failed the good faith prong because in the 8 years following consolidation of his loans he had never made a payment, never made an attempt to work out a reasonable payment schedule, and "did not explore, much less take advantage of, one of the alternative repayment plans available to him even when able to do so."The District Court further stated "[e]ven if no payment was required under the plan and the amount due would have essentially remained unchanged, signing up for one of the repayment alternatives would have demonstrated a continued acknowledgement of the debt and some intent to repay, as opposed to the deliberate obliviousness demonstrated by Vargas following his consolidation in 2001." Rather, "he simply sat back and let his consolidated loan lapse into default."

h. Eighth Circuit:

***In re Sederlund*, 440 B.R. 168 (B.A.P. 8th Cir. 2010).** The debtor's payment under either the ICR or IBR, at her current income level, would be zero. She refused to apply because of her believed tax consequences. The Court, citing *Jesperson*, rejected this, stating "while there is some question as to whether borrowers whose student loans are forgiven are subject to tax liability, the Eighth Circuit…appeared to reject the argument that such potential tax liability is a basis for a finding of undue hardship under §523(a)(8)."

***Educ. Credit Mgmt. Corp. v. Jesperson (In re Jesperson)*, 571 F.3d 775, 783 (8th Cir. 2009).** The Eighth Circuit found, "[w]hen a debtor is eligible for the ICR, the court in determining undue hardship should be less concerned that future income may decline. The ICR formula adjusts for such declines, without regard to the unpaid student loan balance, which in most cases will avoid undue hardship." The court further held that "a student loan should not be discharged when the debtor has 'the ability to earn sufficient income to make student loan payments under the various special opportunities made available through the Student Loan Program.'"*Jesperson*, 571 F.3d at 781.

i. Ninth Circuit:

***Educ. Credit Mgmt. Corp. v. Beattie*, 490 B.R. 581 (W.D. Wash. 2012).** The District Court reversed the bankruptcy court's ruling granting the debtor a partial discharge of her student loan debt. In so doing, the District Court evaluated the existence of undue hardship by applying the IBR payment amount, not the original, higher contract payment amount. The court stated that "almost every debtor would satisfy Prong 1 easily if courts were restricted to considering only the amount of their contract payment. Congress's creation of the flexible income-based repayment options . . . reflects an intent that debtors not be automatically or easily excused from their student loan obligations."

***In re Ristow*, No. 11-1376, 2012 WL 1001594 (B.A.P. 9th Cir. Mar. 26, 2012).** The Ninth Circuit BAP reversed the lower court's partial discharge based on the good faith prong, stating that there was no evidence that the debtor had considered employment for work paying less than $100,000 and consequently had not demonstrated that they had "sufficiently exerted themselves to maximize their income." Additionally, the court rejected the debtor's bases for refusing to take advantage of the IBR, claiming (1) she did not want her husband to become obligated for the payments, (2) they [debtors] could not afford the Income Based Plan payments currently, and (3) the 25-year payment term meant that they would be obligated to make payments under the IBR through their mid-eighties.

***Healy v. U.S. Dep't of Educ.,*, 2010 WL 2650438 (Bankr. N.D. Cal. June 30, 2010).** Debtor did not satisfy the first prong of the *Pena* test because she would be able to make the IBR payments on her debt to ECMC.

***In re Dimoyannis*, 2010 WL 1780098 (Bankr. N.D. Cal. Apr. 29, 2010)**. The debtor failed the first prong of the undue hardship test because of the availability of the IBR plan, under which debtor would be required to make payments of $0 to $47, amounts that were less than debtor's monthly surplus. Although the court held that the second and third prongs of the *Brunner* test were moot as a result of debtor's failure to satisfy the first prong, it went on to state that the debtor's "failure to renegotiate his debt through the Department of Education's IBR program would weigh against a finding that he has made a good faith effort to repay the debt."

***Joyner v. Educ. Credit Mgmt. Corp. (In re Joyner)*, 2007 WL 2819498 (Bankr. D. Ariz. Sept. 26, 2007).** The debtor failed all three prongs of the undue hardship test. With regard to the third prong, the court held that although Debtor demonstrated some good faith efforts by making $3,000 worth of payments on his student loans and maximizing his income, he also failed to minimize his expenses. The debtor had room in his budget

for cable television, high-speed internet service, and was recently able to take a vacation. Furthermore, the debtor did not attempt repayment under the William D. Ford Program. Therefore, the debtor failed to show that he had made good faith efforts to repay his loans.

j. Tenth Circuit:

***In re Brown,* 442 B.R. 776 (Bankr. D. Colo. 2010).** The 25-year-old single mother of three children was unable to prove good faith efforts towards repaying her student loan when (1) she did not make a single payment on the underlying loans or the consolidated loan, (2) she filed bankruptcy two years after consolidating, (3) 29% of her unsecured debt was student loans, (4) she failed to consider the ICR and IBR, and (5) she had repaid a post-petition debt to her mother which demonstrated she had some ability to repay debts.

***Buckland v. Educ. Credit Mgmt. Corp. (In re Buckland)*, 424 B.R. 883 (Bankr. D. Kan. 2010).** The debtor's refusal to consider the ICR or IBR supports a finding he did not make a good faith effort. The debtor's stated reasons for not entering the ICR – he would be 72 years old and the potential tax consequences – were rejected by the court.

***Robinson v. Educ. Credit Mgmt. Corp. (In re Robinson)*,390 B.R.727 (Bankr. W.D. Okla. 2008)**. A 52-year-old debtor had accumulated $120,000 in student loans earning a B.A, M.A., and an Ed.D. The court found that she had not made good faith efforts because she failed to minimize her expenses, failed to make any payments on her student loan since earning her doctoral degree, 81% of her total unsecured debt was student loan debt, and she failed to take advantage of the ICR. The court rejected the debtor's two excuses for refusing participation in the ICR: (1) she would be too old and still making payments; and (2) there was a potential for tax consequences. The court held that "while it is true that the ICR's 25-year term would result in the plaintiff's being obligated to make student loan payments until she is nearing the age of eighty, this result is simply a function of the plaintiff's age at the time she obtained her degrees and executed the Consolidation Note and her exercise of forbearances prior to filing her bankruptcy case." Second, "[w]hile the possible tax implications of the ICR are not to be ignored, they are of much lesser importance than the plaintiff's showing of good faith in repayment of her student loans."

k. Eleventh Circuit:

***In re Kidd*, 472 B.R. 857 (Bankr. N.D. Ga. 2012).** Debtor seeking undue hardship discharge of her student loan debt did not make good faith effort to repay debt where debtor had not actively sought employment for

approximately two years, debtor's expenditures showed discretionary spending for such items as storage fees, portrait fees, and dining and entertainment expenses, debtor made no payment on her loan, despite incurring such discretionary expenses, student loan debt accounted for approximately 70 percent of debtor's unsecured debt, debtor sought no repayment options other than litigation, and made no payment after she received substantial reduction of amount owed in settled state-court action.

***In re Nielsen*, 473 B.R. 755 (B.A.P. 8th Cir. 2012).** Chapter 7 debtor was not entitled to "undue hardship" discharge of his $48,361 in student loan debt, where debtor's household income was in excess of monthly expenses (after adjustment was made for public assistance benefits and the average annual tax refunds of about $8,000), debtor was eligible for ICR under which his monthly payments would be $0.00, and debtor's bankruptcy discharge would relieve him of the credit card debt that he had been servicing prepetition, at monthly cost of more than $1,000.

***Groves v. Citibank*, 398 B.R. 673 (Bankr. W.D. Mo. 2008).** The bankruptcy court, utilizing the loan-by-loan analysis of partial discharge, determined that Sallie Mae's loans imposed a greater hardship because they were not eligible for the ICR. Only a portion of the ECMC loans were discharged because they were eligible for the ICR. "[I]t is the availability of the income contingent option that makes a portion of the ECMC loans nondischargeable because that option allows the Debtor the ability to find employment with an annual salary in line with what she is capable of earning."

2. ICR/IBR Criticized:

a. First Circuit:

***Educ. Credit Mgmt. Corp. v. Bronsdon*, 435 B.R. 791 (B.A.P. 1st Cir. 2010).** In the second appeal for this case involving a 64-year-old debtor., the bankruptcy court discounted the ICR because of its potential tax implications and because it believed the ICR usurped the role of the bankruptcy court in determining undue hardships and fully discharged the loans. On appeal, the district court remanded, requiring the bankruptcy court to consider the impact participation in the ICR would have on the undue hardship analysis. The district court held that tax liability is "not certain to flow from the discharge of the remaining debt" at the end of 25 years and that consideration of the ICR would not impermissibly diminish the authority of the bankruptcy court. On remand, the bankruptcy court still rejected the ICR and stated that the debtor still met the good faith prong. ECMC then appealed to the BAP, which affirmed, stating, "a debtor's eligibility to participate in the ICR may be considered by the court when applying the totality of the circumstances test, but it is not

determinative" and found that the bankruptcy court's analysis of the ICR was sufficient this time.

b. Second Circuit:

***In re Bene*, 474 B.R. 56 (Bankr. W.D.N.Y. 2012).** The bankruptcy court discharged a 64-year-old debtor's student loan. In doing so, it offered a lengthy critique of the current applicability of *Brunner* in light of the development of the Ford Program, as well as the evolution of the Bankruptcy Code's provisions for discharge. The bankruptcy court praised Ford as "the *second* most important development in the history of the effort to make higher or specialized education broadly available in our nation." (most important was the guaranteed student loan program itself). The court also noted that Ford can implicate all three prongs of the *Brunner* test, but determined that the *Brunner* test should be analyzed first without regard to Ford, and *if* the debtor passed the *Brunner* test (without regard to Ford), then the court should take the next step and analyze the flexible options available within Ford under a "totality" test. In conclusion, the bankruptcy court stated that the ultimate question really is" how much personal sacrifice society expects from individuals who accepted the benefits of guaranteed student loans but who have not obtained the financial rewards they had hoped to receive as a result of their educational expenditures."

c. Third Circuit:

***In re Crawley*, 460 B.R. 421 (Bankr. E.D. Pa. 2011).** Fact that Chapter 7 debtor had elected not to participate in income contingent repayment plan (ICR), pursuant to which debtor's payment obligation would have been $0.00 per month, was irrelevant to whether debtor satisfied "minimal standard of living," prong of *Brunner*. "To hold otherwise would make eligibility in the ICR outcome determinative in undue hardship determinations under § 523(a)(8) and would result in the delegation to an administrative agency, the Department of Education, the authority to determine the dischargeability of certain student loans." As to the role of the ICR in the good faith analysis, the court stated "consideration of the significance, if any, of the debtor's failure to participate in the ICR must be tailored based on the individualized circumstances of the debtor who is before the court."

***In re Coco*, 335 Fed. Appx. 224 (3d Cir. 2009).** This was an unpublished decision reversing a bankruptcy court's grant of summary judgment for the creditor NJHESAA. The debtor's claim of undue hardship was largely based on the fact that her chronic medical problems made it difficult to earn a living. The bankruptcy court had granted summary judgment

because of the debtor's "utter failure" to demonstrate good faith efforts to repay. In reversing, the Third Circuit noted that she had attempted to contact NJHESAA to inquire about making a lower monthly payment and had allegedly been told she could only pay the balance in full or seek deferment. The Panel held that the bankruptcy court had placed too much weight on the debtor having made only one payment and on her refusal to participate in the ICR. It held that, given the debtor's financial and medical circumstances, her concerns that she would ultimately be trading a student loan debt for an IRS debt were reasonable and that she had shown enough good faith to survive summary judgment.

d. Fourth Circuit:

***In re Todd*, 473 B.R. 676 (Bankr. D. Md. 2012).** Mere fact that debtor declined the "meaningless gesture" of participating in ICR, under which her payment obligation would be $0.00, did not prevent her from satisfying "good faith" test. The court was very critical of the ICR and noted "[t]o hold that good faith will only be found if [debtor] agrees to a repayment program that will not require her to make any payments—$0.0 "monthly payments" for twenty-five years—would be the height of Kafka-esque logic."

e. Sixth Circuit:

***Marshall v. The Student Loan Corp. (In re Marshall)*, 430 B.R. 809 (Bankr. S.D. Ohio 2010).** Debtor's decision to not enroll in the IBR was reasonable. The court stated "There is more to student loan debt than merely the monthly payment to be made." First, the court held, even if the debtor was not required to make monthly payments, the "debt is still hanging over her head, it will affect her credit and cause a 'psychological and emotion toll.'" Second, there would be tax consequences at the end of the 25 years and these could be "devastating."

f. Seventh Circuit:

***Krieger v. Educ. Credit Mgmt. Corp.*, 713 F.3d 882 (7th Cir. 2013).** In reinstating the bankruptcy court's decision to grant a discharge, the Court of Appeals disagreed with the District Court's determination that the debtor was required to enroll in a 25-year repayment program to satisfy the good faith prong when the debtor "could not pay even $1 a year as now situated[.]" The court observed that the debtor had paid as much as she could since receiving the loans, rejecting the proposition that "good faith entails commitment to future efforts to repay." The court also emphasized that "undue hardship" is "a case-specific, fact-dominated standard, which implies deferential appellate review" of bankruptcy court determinations.

***Larson v. United States of Am.*, 426 B.R. 782 (Bankr. N.D. Ill. 2010)** The bankruptcy court spent time addressing why the ICR is only marginally relevant in undue hardship proceedings, explaining that (1) Congress could have easily drafted it into the legislation if it had desired for it to restrict the judge's discretion in 523(a)(8) actions; (2) the standards, while related are not the same because the ICR solely looks at income and the published poverty level, whereas the *Brunner* test compares the debtor's income to actual expenses (such as extensive medical expenses) that are not routinely considered in ICR calculations; (3) the ICR does not take into account the "emotional" and "social" toll caused by the debt remaining hanging over their heads and affecting their credit; and (4) the tax implications.

g. Eighth Circuit:

***Brown v. Am. Educ. Servs.,* 78 B.R. 623 (Bankr. W.D. Mo. 2010).** The bankruptcy court held the 64-year-old, unemployed debtor's student loans dischargeable despite the existence of the ICR payments which actually shortened the 30-year plan she was currently enrolled in. Even if the court imputed income to her at the level she was previously making, her payment would be $186.12/month, and the court determined she could not afford that payment with her expenses. In any case, the court found that if she remained unemployed with a $0 payment, "shackling her to the program would seem a pointless exercise since it would not entail the likelihood of any significant repayment."

***Wallace v. Educ. Credit Mgmt. Corp. (In re Wallace)*, 2007 WL 4210450 (Bankr. E.D. Mo. Nov. 27, 2007).** In this totality analysis, the argument that Debtor's failure to take part in the ICR precludes an undue hardship was rejected by the court for three reasons. First, the undue hardship analysis focuses on the debtor's reasonable and necessary expenses and the ICR ties payments to income in excess of federal poverty standards. "[B]ecause it is unlikely that a person could pay her reasonably necessary living expenses if her income is at the federal poverty level…the ICR is of limited probative value." Second, the Debtor was 58 years old and would be 83 when the payments would cease. Last, there was "a very real possibility of a significant tax liability" at age 83.

h. Ninth Circuit:

***Hedlund v. The Educ. Res. Inst.,* 718 F.3d 848 (9th Cir. 2013).** The bankruptcy court granted the debtor a partial discharge. On appeal, the district court reversed. Debtor appealed and the 9th Circuit held, as a threshold matter, that the District Court erred in reviewing the bankruptcy court's good faith finding *de novo.* "In a § 523(a)(8) proceeding, the good

faith finding should be reviewed for clear error." Under that standard of review, the 9th Circuit affirmed the bankruptcy court's ruling and reinstated the debtor's partial discharge. The 9th Circuit declined to disturb the bankruptcy court's finding of good faith despite the fact that the debtor made "minimal" efforts to consolidate his loans, "his research into ICR eligibility could have been more searching," and he declined other proffered repayment plans. The 9th Circuit ultimately concluded that "even though some might disagree with the bankruptcy court's good faith finding, it was not clearly erroneous. The [bankruptcy] court relied on substantial evidence in the record, and its factual inferences were permissible."

***In re Roth*, 490 B.R. 908 (B.A.P. 9th Cir. 2013).** The bankruptcy court denied debtor's student loan discharge, concluding that she failed to show she made a good faith effort under prong three. The BAP reversed, holding that debtor's refusal to enroll in the IBR should not be weighed against her where the evidence showed that she currently would not be required to make a payment under the IBR and that "it is more probable than not she would never be required to make a payment," especially given her age, poor health, and limited income or prospects." The BAP also noted the "[p]otentially disastrous tax consequences" awaiting the debtor at the conclusion of the 25-year IBR period and observed that the "IBR was set up to allow borrowers to pay an affordable amount toward retirement of their student loan debt. However, when absolutely no payment is forecast, the law should not impose negative consequences for failing to sign up for the program. This is consistent with the general maxim that the law does not require a party to engage in futile acts."

***In re Booth*, 410 B.R. 672 (Bankr. E.D. Wash. 2009).** In a denial of summary judgment, the bankruptcy court wrote a scathing criticism of the argument that a $0 monthly repayment could not be an undue hardship as a matter of law, as advanced by the AUSA. The court stated that "the focus of the ICR is on deferral, not discharge of debt. This is the antithesis of a fresh start." It went on to further state that $0 payments could not preclude a finding of undue hardship because it would otherwise usurp the Bankruptcy Code and "destroy the jurisdiction of the bankruptcy court."

V. *Brunner* v. Totality of Circumstances Tests

A. One Legal Standard: Two Tests: Because the bankruptcy code does not define "undue hardship," courts have developed two tests to construe what Congress intended debtors to prove before they were entitled to discharge of their federally-backed student loans:

1. The *Brunner* Test: Nine circuit courts of appeal have adopted the *Brunner* test,[5] which requires the debtor to demonstrate:

(1) an inability to maintain, based on current income and expenses, a "minimal" standard of living if forced to repay the loans;

(2) 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) good faith efforts to repay the loans.

See Brunner v. N.Y. State Higher Educ. Servs. Corp. (In re Brunner), 831 F.2d 395 (2d Cir. 1987), affirming *Brunner v. N.Y. State Higher Educ. Servs. Corp. (In re Brunner)*, 46 B.R. 752, 753 (S.D.N.Y. 1985).

2. The "Totality of the Circumstances" test:

a. Eighth Circuit: The Eighth Circuit rejected the *Brunner* test and instead adopted the so-called "totality of the circumstances" test to determine undue hardship under § 523(a)(8). The totality test requires a bankruptcy court to consider:

(1) the debtor's past, present, and reasonably reliable future financial resources;

(2) the debtor's and her dependent's reasonable necessary living expenses; and

[5]*See Frushour v. Educ. Credit Mgmt. Corp. (In re Frushour)*, 433 F.3d 393 (4th Cir. 2005); *Oyler v. Educ. Credit Mgmt. Corp. (In re Oyler)*, 397 F.3d 382 (6th Cir. 2005); *Educ. Credit Mgmt. Corp. v. Polleys (In re Polleys)*, 356 F.3d 1302 (10thCir. 2004*); Hemar Ins. Corp. of Am. v. Cox (In re Cox),*338 F.3d 1238 (11th Cir. 2003); *U.S. Dep't of Educ. v. Gerhardt* (*In re Gerhardt)*, 348 F.3d 89 (5th Cir. 2003);*United Student Aid Funds, Inc. v. Pena (In re Pena)*, 155 F.3d 1108 (9th Cir. 1998); *Pa. Higher Assistance Found. v. Faish* (*In re Faish),* 72 F.3d 298 (3d Cir. 1995); *In re Roberson,* 999 F.2d 1132 (7th Cir. 1993); *Brunner v. N.Y.State Higher Educ. Servs. Corp*., 831 F.2d 395 (2d Cir. 1987). The First Circuit is the only circuit that has not formally adopted a particular test for undue hardship determinations.

(3) any other relevant facts and circumstances surrounding each particular bankruptcy case.

Long v. Educ. Credit Mgmt. Corp. (In re Long), 322 F.3d 549, 553, 554 (8th Cir. 2003). The Eighth Circuit summed up this test: "Simply put, if the debtor's reasonable future financial resources will sufficiently cover payment of the student loan debt—while still allowing for a minimal standard of living—then the debt should not be discharged." *Id.* at 554-55; *see generally* Julie Swedback & Kelly Prettner, *Discharge or No Discharge? An Overview of Eighth Circuit Jurisprudence in Student Loan Discharge Cases*, 36 Wm. Mitchell L. Rev. 1679 (2010).

b. First Circuit: The First Circuit has declined to adopt any formal test:

> 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 demonstratethat her disability will prevent her from working for the foreseeable future. Appellant has a formidable task, for Congress has made the judgment that the general purpose of the Bankruptcy Code to give honest debtors a fresh start does not automatically apply to student loan debtors. Rather, the interest in ensuring the continued viability of the student loan program takes precedence."

Nash v. Conn. Student Loan Found. (In re Nash), 446 F.3d 188, 190-91 (1st Cir. 2006).

B. *Brunner* v. Totality: Does Really It Matter?

Courts using the Totality test claim that "a 'case-by-case approach that is fact sensitive . . . affords a determination that contextually considers both the debtor's situation and the policies underlying § 523(a)(8) [and] ensures an appropriate, equitable balance [between] concern for cases involving extreme abuse and concern for the overall fresh start policy.'"***In re Hicks,* 331 B.R. 18 (Bankr.D.Mass. 2005)** (internal citations omitted)).

Courts using *Brunner* test claim "it provides a workable, easily articulated framework for courts and parties to follow while still allowing for a fact- and case-sensitive determination." Also, *Brunner* courts claim "that adopting the *Brunner* test will 'create[ ] more certainty and predictability by establishing concrete factors.'" *Id.*

Although two tests have emerged, both generally consider the same criteria: ability to pay now and in the future, whether the debtor has maximized income and minimized expenses, and attempts to repay the debt a/k/a the "good faith" prong, which requires both looking back and looking forward to decide if the debtor has made a good faith effort to repay the debt. In Totality of the Circumstances jurisdictions, courts will generally consider criteria related to *Brunner*'s "good faith" prong under the Totality's "any other relevant facts" prong. Ultimately, because there is one legal standard, it may not matter which test is applied.

C. The Demise of *Brunner*: Brave New World?

After nearly three decades of construing the statutory undue hardship legal standard and creating an epic body of case law, a few courts have begun questioning *Brunner*'s viability. Contributing to this growing dissent is the fact that Congress repealed the "time in repayment" provision of § 523(a)(8), leaving undue hardship as the only means of discharging student loan debt in bankruptcy and has increased the availability of administrative options, including flexible, income driven repayment plans.

Some courts view administrative options as improperly usurping their judicial authority. *See* Terrence L. Michael & Janie M. Phelps,"*Judges?!- - We Don't Need No Stinking Judges!!!": The* Discharge *of Student Loans in Bankruptcy Cases and the Income Contingent Repayment Plan,* 38 Tex. Tech L. Rev. 73 (Fall 2005); *see also In re Todd*, 473 B.R. 676 (Bankr. Md. 2012) (noting that § 523(a)(8) "allows debtors to discharge their student loans upon a showing that repaying them would be an 'undue hardship.' There is no indication that Congress intended to supplant this unambiguous directive with the Ford Program and its existence should not be treated as an implicit repeal of § 523(a)(8)").

The bankruptcy court in the Western District of New York, recently indicted *Brunner* with these observations:

- The "bargain" has changed. In 1987, student loans were dischargeable under a "time in repayment" provision as well as undue hardship. Students whose loans pre-date the changes in the Bankruptcy Code cannot be said to have agreed to this bargain.
- The *Brunner* decision used words like "poverty" and "minimal standard of living," words which have a different meaning today.
- The term "repayment period" as used in *Brunner* envisioned a maximum repayment term of 10 years—not the 25 years contemplated under income-driven repayment terms.
- Repayment options under William D. Ford Direct Loan Program were not available when the *Brunner* case was decided.
- "Satisfaction" of the debt after 25-years of successful payments under the ICR/IBR is not the same as "repayment" of the debt.
- "But if Congress ever were to require this writer to instruct a student loan debtor that he or she must carry the burden of proving that he or she has a 'certainty of hopelessness,' this writer would retire."
- The case of Marie Brunner did not require the court to apply all three prongs of what is now referred to as the "*Brunner* test" because Marie Brunner failed the first prong. "[F]ormulation of a three-prong test applicable to *every* student loan debtor who has ever sought relief in the bankruptcy courts of the Second Circuit since *Brunner* was not *required* under the facts of Ms. Brunner's case."
- Marie Brunner was pro se—and the holding is now binding upon every student loan borrower who ever sought bankruptcy relief in the 2nd Circuit since 1987. "It is time for a student loan debtor's counsel to present these matters to the Circuit Court."

In re Bene, 474 B.R. 56 (Bankr. W.D.N.Y. 2012); *see also In re Roth*, 490 B.R. 908 (B.A.P. 9th Cir. 2013) (Pappas, J., concurring) (comparing *Brunner*'s harshness to lesson learned from "America's experience in the recent 'mortgage crisis'" and urging the 9th Circuit to re-visit its adherence to the *Brunner* test, specifically the "good faith" prong.); *In re Cummings,* 2007 WL 3445912 (Bankr. N.D.Cal.2007) ("This court has long been spitting into the wind by noting that the [*Brunner*] test is a terrible example of judge-made law which gives no real guidance to a court in determining what undue hardship is. . . . "The worst part of the *Brunner* test is the requirement that a debtor has to have made a good faith effort to pay the loans. Congress said nothing about such a requirement in the Bankruptcy Code, and Congress knows how to draft a good faith requirement when it wants one. An effort to repay has absolutely nothing to do with hardship.").

VI. PRACTICE TIPS

A. Who's Got My Loans? The single most important inquiry in the student loan industry is "who's got my loan?" ED maintains an information repository called National Student Loan Data Systems (NSLDS). NSLDS is a database that contains information, including chain of custody, interest rate, loan type, loan status, etc., regarding every federal student loan a person has borrowed. Lenders, servicers, and guarantors have access to borrower NSLDS reports if they hold the loan. Borrowers may access their own NSLDS reports by going to www.nslds.ed.gov. They must first obtain a PIN at www.pin.ed.gov.

B. Industry resources:

- National Student Loan Data System (www.nslds.ed.gov)
- ED PIN website: (www.pin.ed.gov)
- Federal Student Aid (government website): (http://studentaid.ed.gov)
- Finaid (consumer financial aid website): (www.finaid.org)
- Department of Education (www.ed.gov)
- Department of Education Ombudsman Office (www.ombudsman.ed.gov)
- William D. Ford Direct Loan Program (www.loanconsolidation.ed.gov)
- National Counsel of Higher Education Resources (www.ncher.us)
- Educational Credit Management Corporation (www.ecmc.org)
- FFEL Forms: (http://www.ecmc.org/topic/mainForms.html)
- Direct Loan (Ford program) Forms: (https://www.dl.ed.gov/borrower

VII. CONTACT INFORMATION

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