Bankruptcy, Out-of-Court Options and the Student Loan Debt Problem

How Hard Is the "Hard" in "Hardship"? The Current State of § 523(a)(8)

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Student Loan Issues in Bankruptcy[1*]

I. Introduction

This paper discusses the treatment of student loan debt in bankruptcy. It starts by providing a background on student loan programs, how student loan debt has historically been treated in bankruptcy, and how debtors can obtain a discharge of their student loan debt. It then discusses section 523(a)(8), the student loan discharge provision, which provides that student loan debt is presumptively nondischargeable unless a debtor can prove that repaying such debt would constitute an "undue hardship." The term is not defined in the Code. The paper explains how courts have interpreted "undue hardship" under various tests, including the Johnson test, the Bryant poverty test, the totality of the circumstances test, and the Brunner three-prong test. Since the Brunner Test is the most popular of these tests, the paper discusses the three Brunner prongs and factors that courts often considering in determining whether repaying student loan debt would create an undue hardship. The paper then discusses another wrinkle in the student loan debate: whether courts can discharge some of a debtor's student loan debt. Finally, the paper concludes by discussing proposals regarding the treatment of student debt in bankruptcy.

I. Student loan programs

Congress first established a federal sponsored student loan program, the National Defense Student Loan Program (later known as the Perkins Loan Program), in 1958 as part of the National Defense Education Act. The program allowed students to obtain student loans from the government at five percent interest.[2]

Seven years later, Congress passed the Higher Education Act of 1965 which established the Guaranteed Student Loan Program (later called the Stafford Loan Program).[3] Stafford loans are primarily funded by private lenders and guaranteed by the United States Debarment of Education. The program was designed to reduce financial barriers and ensure that college students would have

1 * This paper was prepared by Alexandra CC Schnapp, law clerk to the Honorable C. Ray Mullins, Chief Judge of the United States Bankruptcy Court for the Northern District of Georgia.

2 Robert C. Cloud, *When Does Repaying a Student Loan Become an Undue Hardship?*, 185 EDUC. L. REP. 783, 786-87 (2004).

3 Higher Education Act of 1965, Pub. Law No. 89–329, § 430 (a), 79 Stat. 1219 (1965).

reasonable access to low-interest loans; it is based on the principle that a student should be able to obtain a higher education regardless of his financial resources. In 1972, the federal loan program was expanded to provide grants and loans for junior colleges, trade schools, and career colleges.[4]

In 1978, Congress made federal loans available to virtually all students without significant regard to need with the Middle Income Student Assistance Act.[5] The Middle Income Student Assistance Act of 1978 did not create any new programs, but it extended federal loan eligibility to virtually all students regardless of income. The previous Higher Education Act requirement that only families with incomes less than $25,000 were eligible was deleted. As a result, student borrowing increased rapidly and federal loan expenditures skyrocketed.

Today, millions of students depend on federal loans to finance their educations. Federal loans constitute about 85% of all outstanding education loan debt, and approximately 93% of all new loans.[6] Most institutions, both public and private, depend on revenue generated through the federal loan program.[7]

The federal government is authorized to make four types of direct loans at specified interest rates: Subsidized Stafford, Unsubsidized Stafford, PLUS, and Consolidation Loans.[8] The Subsidized Stafford loan offers the lowest interest rate and borrowers must meet a financial needs test to qualify; graduate and professional students are not eligible for these loans. All other loans are available to borrowers at any income level.[9] Unsubsidized Stafford loans are made without regard to

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4 Daniel A. Austin, *The Indentured Generation: Bankruptcy and Student Loan Debt*, 53 Santa Clara L. Rev. 329, 338 (2013) (citing Education Amendments Act of 1972, Pub. L. 92-318, § 302(a)(1), 86 Stat. 241-42 (1972)).

5 Middle Income Student Assistance Act, Pub. L. No. 95-566, § 2, 92 Stat. 2402 (1978).

6 Austin, *supra* note 3, at 339-40.

7 Cloud, *supra* note 1, at 786-87. Education lending is also an income-producing endeavor for the federal government. Profit is made on the spread between the government's borrowing rate, around 1%, and the subsidized lending rate, currently at 3.4% for the lowest rate Subsidized Stafford loan and increasing with other types of loans. There is also an origination fee of 1%. The Department of Education anticipates that federal subsidized student loan activity (including new loans and consolidation of existing loans) will generate $ 38.9 billion in revenue for the government in 2012, and approximately $ 36.8 billion in 2013. [98] The federal government expects to earn 20.08% on each dollar of loans originated in 2013. Austin, *supra* note 3, at 342-43

8 *See* 20 U.S.C. § 1087e (describing the terms and conditions of the federal direct loan program).

9 Austin, *supra* note 3, at 341 (citing U.S. Dep't of Educ., Student Loans Overview, Fiscal Year 2013 Budget Request, at R-18, available at http://www2.ed.gov/about/overview/budget/budget13/justifications/r-loansoverview.pdf.

financial need. PLUS Loans (Parents Plus) are available to parents with dependant undergraduate, graduate, and professional degree students. Plus Loan applicants may not have any adverse credit history. Consolidation Loans are available for borrowers with existing loans in order to combine the loans and extend payment schedules and terms based on their total existing loans. Interest rates for these loans are currently fixed but have historically been priced at a spread to Treasury bills.[10] Whether based on a fixed or variable rate, the interest rate does not reflect the borrower's risk – if the borrower is eligible for a loan, he or she will be charged the same rate as any other eligible borrower.[11]

In additional to federal education loans, private lenders also loan money to students. A student might take out a non-federal loan if he has reached the annual or aggregate federal loan cap. Unlike federal loans, most non-federal loans are priced according to creditworthiness standards, and there is no cap on interest rates.[12]

After graduation, Stafford loans allow for a grace period of six months after graduation; upon expiration of the grace period, it is time to repay.[13] There are different modes for doing so.[14] The standard repayment program gives students ten years to repay and requires student-loan debtors to pay a fixed amount per month of at least $50. Students with federal loans in excess of $ 30,000 may qualify for Extended Repayment, which allows up to twenty-five years for repayment with the option of either fixed or graduated repayment.[15] Under the Income Contingent Repayment Program,[16] students make monthly payments calculated on the basis of adjusted gross income, family size, and total amount of Direct Loans.[17] The maximum repayment period is twenty-five years and, if students do not fully repay their loans after twenty-five years, the unpaid portion is

10 Note, *Ending Student Loan Exceptionalism: The Case for Risk-Based Pricing and Dischargeability*, 126 HARV. L. REV. 587, 593-94 (2012) (hereinafter "Exceptionalism").

11 *Id.* at 594.

12 *See id.* at 594.

13 Austin, *supra* note 3, at 346-47.

14 *See Repayment Plans*, U.S. DEP'T OF EDUC., http://www.direct.ed.gov/RepayCalc/dlindex2.html (last visited Mar. 27, 2014) (discussing repayment options).

15 *Id.* Fixed payments are the same amount each month, while graduated payments start low and increase every two years.

16 Parent Plus loans are not eligible.

17 Students pay the lesser of: 1) the amount they would pay if the loan was repaid in 12 years multiplied by an annual percentage factor or 2) 20% of monthly discretionary income.

discharged. If a debtor qualifies for an Income-based Repayment plan, he will make monthly payments based on his income.[18] Such payments may be adjusted annually and payments may be $0. After a period of time, the outstanding balance may be cancelled. To participate in this program, a debtor must provide extensive medical and financial information to show he qualifies. There are also several specialized loan forgiveness programs.[19]

According to a 2010 report, thirty-seven million Americans owe approximately one trillion dollars in student loans.[20] The cost of a college education has risen by three times the cost of inflation since 1983.[21] Not surprisingly, the amount of debt per student and the percentage of students borrowing for education have expanded.[22] Compounding the problem is that new graduates are entering one of the worst job markets in decades.[23] Outstanding student loan debt is at an all-time high; it is approaching $ 1.2 trillion. Student loan debt now surpasses credit cards as the second-largest form of consumer debt behind home mortgages.[24]

A recent feature in the Fulton County Daily Report surveying new partners illustrates just how pervasive student loan debt is.[25] The survey asked fifty-nine new partners, the majority of whom had been practicing for eight or more years, whether they were still paying student loans. 76.6% of those surveyed reported that they were. Of those that were still paying student loans, the largest group of respondents (19.4%) reported that they owed $30,001 - $40,000; half of the partners still paying student loans owed more than $40,000.

Many recent articles have stated that while the student loan bubble has not yet reached

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18 A U.S. Department of Education on-line calculator allows borrowers to determine if they are eligible.

19 For example, members of the military may be eligible for loan forgiveness programs.

20 The Inst. for Coll. Access & Success, *Quick Facts About Student Debt*, The Project on Student Debt (Jan. 2010), http://projectonstudentdebt.org/files/File/Debt_Facts_and_Sources.pdf.

21 Austin, *supra* note 3, at 334 (citing *The College-Cost Calamity*, Economist (Aug. 4, 2012), http://www.economist.com/node/21559936)).

22 *Id.*

23 Austin, *supra* note 3, at 332.

24 Rohit Chopra, *Student Debt Swells, Federal Loans Now Top a Trillion*, Consumer Financial Protection Bureau (July 17, 2013), www.consumerfinance.gov/newsroom/student-debt-swells-federal-loans-now-top-a-trillion/.

25 *The New Partners Survey*, Fulton County Daily Report (Mar. 10, 2014), http://pdfserver.amlaw.com/dailyreport/Editorial/NewPartners_Charts_2014.pdf.

the tipping point, the reality is that this situation is unsustainable.[26] This is in part because as the amount of outstanding student debt climbs, so too does the student loan default rate. In 2010, the Secretary of Education announced that the average default in 2008 was 7%.[27] Secretary Arne Duncan explained, "This data confirms what we already know: that many students are struggling to pay back their student loans during very difficult economic times . . . ."[28]

While the Bankruptcy Code permits some homeowners to address underwater mortgages, student-loan debtors generally cannot discharge their student loans in bankruptcy and very few even attempt to do so. A recent study found that of the 169,774 debtors that filed bankruptcy in 2007 with student loan debt, only 217 filed an adversary proceeding in an effort to discharge their loans.[29] Interestingly, about half of those who did file adversary proceedings received relief, either in the form of full or partial discharges or repayment plans. This paper will now discuss how student loans are treated in bankruptcy and how a student-loan debtor seeking to discharge may do so.

II. History of bankruptcy provisions re: student loans

Over the past three decades, Congress has curtailed the bankruptcy relief available to student-loan debtors.[30] Before the late 1970s, educational loans were treated like any other form of unsecured debt in bankruptcy and were generally dischargeable. In the early 1970s, federal student loan spending grew steadily (in part because the ever-increasing expense of higher education forced more students to turn to student loan programs to attend college). Student loans were not exempted from discharge and concern grew that debtors would file bankruptcy to avoid student loan repayments.

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26 *The Student Loan 'Debt Bomb': America's Next Mortgage-Style Economic Crisis?*, NACBA (Feb. 7, 2012), http://nacba.org/Portals/0/Documents/Student%20Loan%20Debt/020712%20NACBA%20student%20loan%20debt%20report.pdf; *see also Student Loan Affordability: Analysis of Public Input on Impact and Solutions*, Consumer Financial Protection Bureau, 7 (May 8, 2013), http://files.consumerfinance.gov/f/201305_cfpb_rfi-report_student-loans.pdf.

27 *Student Loan Default Rates Increase*, U.S. Dep't of Educ. (Sept. 13, 2010), http://www.ed.gov/news/press-releases/student-loan-default-rates-increase-0.

28 *Id.*

29 Jason Iuliano, *An Empirical Assessment of Student Loan Discharges & the Undue Hardship Standard*, 86 AM. BANKR. L.J. 495, 505 (2012).

30 Rafael I. Pardo & Michelle R. Lacey, *The Real Student-Loan Scandal: Undue Hardship Discharge Litigation*, 83 Am. Bankr. L.J. 179, 181 (2009).

In 1978, federal loans became available to most middle class Americans regardless of need. That same year, Congress added 523(a)(8) undue hardship exception, largely in response to the "fear that students might take advantage of the bankruptcy system by incurring large amounts of student debt, only to obtain a discharge of the debt on the eve of lucrative careers."[31] While there was no hard numerical evidence suggesting that any serious problem existed,[32] a Congressional Commission[33] nevertheless concluded that even a small percentage of discharges created a negative public image that discredited the system and eventually could threaten the existence of the programs.[34] Thus, the Commission recommended establishing a discharge limitation to prevent abuses and sustain the integrity of the student loan programs.[35] The Commission proposed that student debtors could receive a discharge of the loan debt only if a five-year period had passed since the loan first became due, or if an undue hardship would result if the loan were not discharged within the five-year period.[36]

Congress codified the Commission's recommendation in the Education Amendments of 1976.[37] Under this legislation, a student-loan debtor could discharge of student loan debt only if a

31 Kyle L. Grant, Note & Comment, *Student Loans in Bankruptcy and the "Undue Hardship" Exception: Who Should Foot the Bill?*, 2011 B.Y.U.L. Rev. 819, 825 (2011) (citing H.R. Rep. No. 95-595, at 536-537 (1977)).

32 A more careful examination of the numbers, however, shows that the student loan discharge rate was nominal. For example, a 1976 report submitted to Congress from the General Accounting Office stated that "less than one percent of all matured student loans [were] discharged in bankruptcy." H.R. Rep. No. 95-595, at 536-537 (1977) (The default rate on student loans was 18%, and of that group only 3-4% received a discharge in bankruptcy. Where student-loan debtors filed bankruptcy, most had "a true need for . . . relief rather than an abuse of the bankruptcy system."). Hence, ideas about substantial abuse of a bankruptcy loophole were founded more upon public relations hype than real evidence. Thad Collins, Note, *Forging Middle Group: Revision of Student Loan Debts in Bankruptcy as an Impetus to Amend 11 U.S.C. § 523(a)(8)*, 75 Iowa L. Rev. 733, 743 (1990). The public's perception of widespread abuse of the student loan program appeared to have a more significant impact on the treatment of student loans in bankruptcy than the nominal abuse that actually existed. *Id*.

33 Congress appointed the 1973 Congressional Commission on Bankruptcy Laws to evaluate and propose reformation of the then-existing bankruptcy laws. Collins, *supra* note 31, at 740 (citing Report of the Commission on the Bankruptcy Laws of the United States, H.R. Doc. No. 137, 93rd Cong., 1st Sess., pt. I, at 11, 170 (1973)).

34 *Id*.

35 *Id*.

36 Collins, *supra* note 31, at 740.

37 *Id*. (citing Education Amendments of 1976, Pub. L. No. 94-482, § 439A, 90 Stat. 2081, 2041 (codified at 20 U.S.C. § 1087-3 (1976) (repealed 1978))).

five-year period had passed since the loan first became due, or if an undue hardship would result if the loan were not discharged within the five-year period.[38] The provision was meant to prevent abusive discharges while still allowing an honest, financially burdened student debtor to obtain a financial fresh start.[39]

Two years later, Congress passed the Bankruptcy Reform Act of 1978 and, with it, section 523(a)(8)(B).[40] The provision merely carried over the standard from the 1976 Education Amendments, thus a student-loan debtor could receive a discharge of his student loan debt if five-years had passed since the loan first became due, or if an undue hardship would result if the loan were not discharged within the five-year period. Later amendments further limited the dischargeability of student loans. A 1979 amendment, for example, broadened the types of loans that were protected from discharge, and accorded loans made by nonprofit organizations and others the same protections accorded to federal student loans.[41]

In 1990, Congress further restricted the narrow instances in which debtors could discharge student loan debt. Up until 1990, section 523(a)(8) had only applied to chapter 7 cases, so chapter 13 debtors were able to discharge their student loans through their repayment plans. Congress amended the Code in 1990 to make section 523(a)(8) applicable in chapter 13 cases; as a result, student loans were no longer dischargeable in chapter 13 cases.[42] Congress also lengthened the five-year exception period to seven years.[43] In 1998, Congress eliminated the five- and seven-year exceptions altogether.[44] As a result, the only option left for debtors seeking to discharge student loan debt is to demonstrate that repaying their student loans would subject them to an undue hard-

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38 *Id.*

39 *Id.* at 743-44.

40 The Senate had proposed a bill that included the same limitations as included in the 1976 Education Amendment. The House bill treated student loans as any other unsecured loans and thus dischargeable at the close of a chapter 7 case. Congress settled on the Senate bill. 11 U.S.C. § 523 (1978).

41 Collins, *supra* note 31, at 743 n. 92 (citing Pub. L. No. 96-56 (Aug. 14, 1979)).

42 B.J. Huey, Comment, *Undue Hardship or Undue Burden: Has the Time Finally Arrived for Congress to Discharge Section 523(a)(8) of the Bankruptcy Code?*, 34 Tex. Tech L. Rev. 89, 100 (2002).

43 See Higher Education Amendments of 1998, Pub. L. No. 105-244, 112 Stat. 1837 (1998) (codified as amended at 11 U.S.C. § 523(a)(8) (2000)).

44 Huey, *supra* note 41, at 100.

ship.[45] In 2005, Congress overhauled the Bankruptcy Code and had the opportunity to review section 523(a)(8), but it chose not to do so.[46] In fact, Congress expanded the exception even further to apply to a larger set of loans.[47]

Commentators have suggested various theories for why student loans should be treated as nondischargeable debts.[48] First, there is the argument that without the exception, lenders would be unwilling to lend to students with little or no credit history.[49] Second, lenders argue that they need to ensure a pool of loan money for future students; if education loans were easily dischargeable, the pool of fund available for new student loans would shrink.[50] Third, there is the concern that student borrowers will abuse student loan programs by filing bankruptcy after graduation, getting a discharge, and then enjoying a lifetime of income that education provides without the expense of paying back loans. Fourth, some argue that the decision of whether to borrow for college lies with individuals and those students that have taken on a debt burden should be responsible for repaying that debt.[51] And finally, some contend that a debtor's misfortune should not be borne by creditors. While many of these arguments cannot be limited to educational loans, together they suggest why student loans receive special attention in bankruptcy.

III. How to obtain a discharge

The Code and Bankruptcy Rules set forth procedures for how a debtor can discharge of student loan debt. Education loan debt must be listed by the debtor on Schedule F along with other

45 *See id.*

46 Grant, *supra* note 30, at 829.

47 Congress expanded 523(a)(8) to cover "any other education loan that is a qualified education loan." *Id.* Prior to 2005, the "undue hardship" exception applied only to loans "insured, or guaranteed by a government unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution." *Id*. (citing 11 U.S.C. § 523(a)(8)(A)(i) (2000)).

48 *See* Austin, *supra* note 3, at 368-70; John A. E. Pottow, *The Nondischargeability of Student Loans in Personal Bankruptcy Proceedings: The Search for a Theory*, 2006 Can. Bus. L. J. 245, 264-65 (2005) (exploring six theories for why educational debt should be treated exceptionally).

49 *See* Austin, *supra* note 3, at 368-70

50 *See Pottow*, supra note 47, at 261 ("A different justification for treating student loans as nondischargeable in bankruptcy proceedings is couched in terms of 'protecting' the solvency of the public student loan programme").

51 *Id*. at 256 (discussing the theory of internalization which builds on the notion that the recipient of a private benefit (education) should have to bear its cost (the debt for tuition)).

general unsecured debt. In a chapter 7 case, education loan claims receive the same distribution as general unsecured debt. However, while general unsecured debt is discharged, student loan debt is not. After the chapter 7 case is closed, the debtor continues making payments to the creditor.

A typical chapter 13 is quite different. Payments to general unsecured creditors can extend for up to five years. The debtor's monthly plan payment is distributed pro rata to unsecured creditors, so education loan creditors will typically receive some money under the plan. However, unless the plan provides for 100% payment to unsecured creditors (which seldom happens), the education loan creditor will not receive the full amount it is owed each month. As a result, principal and interest may continue to accrue on student loan debt during the chapter 13 bankruptcy. At the end of the plan, while other unsecured debt is discharged, the student loan debt may have actually increased. Thus, debtors in chapter 7 generally fare better in regards to student loan payments.

In order to obtain a discharge of student loan debt, the debtor must file an adversary proceeding, during which debtors have the additional burden of proving that repaying their student loans would constitute an "undue hardship." Student-loan debtors must file and serve a complaint and summons on the student loan creditor in accordance with the Federal Rules of Bankruptcy Procedure.[52] In *United Student Aid Funds, Inc. v. Espinosa (In re Espinosa)*,[53] the Supreme Court made clear that debtors may only discharge student loan debts by establishing undue hardship through an adversary proceeding; attempting to discharge a student loan debt by a plan alone is improper and counsel may be subject to penalties. Accordingly, bankruptcy courts should not confirm a plan modifying student loan debt if the debtor has not established undue hardship in an adversary proceeding.[54]

IV. Section 523(a)(8)

Section 523(a)(8) allows the court to discharge an otherwise nondischargeable student loan

52 *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (U.S. 2010); *see also Stephens v. Educ. Credit Mgmt. Corp.*, Case No. 98-90875 (Bankr. N.D. Ga. July 20, 2004) (discharge of student loan cannot be done by motion).

53 559 U.S. 260.

54 *See In re Kinney*, 456 B.R. 748, 753 (Bankr. E.D. N.C. 2010) ("inclusion of student loan discharge provisions as part of a Chapter 13 plan without filing an adversary proceeding . . . and without consideration of whether facts exist to support undue hardship, will not be allowed by this Court.").

if excepting the debt from discharge will impose an undue hardship on the debtor or the debtor's dependents. Section 523(a)(8)(B) provides:

> (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 –
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> (8) unless excepting such debt from discharge under this paragraph would impose an *undue hardship* on the debtor and the debtor's dependents, for
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> (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 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[.]

11 U.S.C. § 523(a)(8)(B) (emphasis added). Whereas most debts are dischargeable unless proven otherwise,[55] this section provides that student loan debts are nondischargeable unless the debtor can establish that paying such debt would constitute an undue hardship.[56] The student loan debtor bears the burden of proof,[57] and he must establish each of the elements by a preponderance of the evidence.[58] Section 523(a)(8) thus represents a conscious choice to override the normal "fresh start" goal of bankruptcy.[59]

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55 A presumption exists that all debts owed by the debtor are dischargeable unless the party contending otherwise proves non-dischargeability. 11 U.S.C. § 727(b). The purpose of this "fresh start" is to protect the "honest but unfortunate" debtor. *United States v. Fretz (In re Fretz)*, 244 F.3d 1323, 1326 (11th Cir. 2001).

56 Generally, the burden is on the creditor to prove the exception to discharge by a preponderance of the evidence. *Grogan v. Garner*, 498 U.S. 279, 287–88 (1991); *St. Laurent v. Ambrose (In re St. Laurent)*, 991 F.2d 672, 680 (11th Cir. 1993).

57 *Fabrizio v. U.S. Dep't of Educ. Borrower Servs. Dep't Direct Loans (In re Fabrizio)*, 369 B.R. 238, 244 (Bankr. W.D. Pa. 2007) (citations omitted).

58 *Id*.

59 *Johnson v. Edinboro State Coll.*, 728 F.2d 163, 164 (3d Cir. 1984) (section 523(a)(8) represents a conscious Congressional choice to override the normal "fresh start" goal of bankruptcy); *see also Hemar Ins. Corp. of Am. v. Cox (In re Cox)*, 338 F.3d 1238, 1243 (11th Cir. 2003) ("Congress intended to make it difficult for debtors to obtain a discharge of their student loan indebtedness.").

V. Defining "undue hardship"

Section 523(a)(8)(B) is difficult to apply because, while it requires a student-loan debtor to establish that repaying his student loan would impose an undue hardship, Congress did not define "undue hardship." The concept is an opaque one[60] that courts analyze on a case-by-case basis.[61] Commentators agree that the undue hardship requirement is a burdensome one that can be inconsistently applied.[62] Courts devised numerous tests to interpret the exception, namely the Johnson test, the Bryant poverty test, the totality of the circumstances test, and the Brunner Test. In recent years, the Brunner Test has been the dominant test.[63] It has been officially adopted in nine circuits.[64]

The Eighth Circuit uses a more holistic totality of the circumstances test.[65] Although the test is unique,[66] studies have found no statistically significant differences in the outcomes under the Brunner Test and that used in the Eighth Circuit.[67]

While the First Circuit has not settled the issue,[68] the Bankruptcy Appellate Panel for the

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60 Rafael I. Pardo & Michelle R. Lacey, *Undue Hardship in the Bankruptcy Courts: An Empirical Assessment of the Discharge of Educational Debt*, 74 U. Cin. L. Rev. 405, 509 (2005).

61 *Pennsylvania Higher Educ. Assistance Agency v. Faish (In re Faish)*, 72 F.3d 298, 302 (3d Cir. 1995) (citing Kurt Wiese, Note, *Discharging Student Loans in Bankruptcy: The Bankruptcy Court Tests of "Undue Hardship,"* 26 Ariz. L. Rev. 445, 447 (1984) ("The drafters said that bankruptcy courts must decide undue hardship on a case-by-case basis, considering all of a debtor's circumstances.")).

62 Iuliano, *supra* note 28, at 498; *see also* Huey, *supra* note 41.

63 Iuliano, *supra* note 28. For a description of the tests, see Huey, *supra* note 41, at 101-12.

64 *See Educ. Credit Mgmt. Corp. v. Frushour (In re Frushour)*, 433 F.3d 393, 400 (4th Cir. 2005); *Oyler v. Educ. Credit Mgmt. Corp. (In re Oyler)*, 397 F.3d 382, 385 (6th Cir. 2005); *Educ. Credit Mgmt. Corp. v. Polleys*, 356 F.3d 1302, 1309 (10th Cir. 2004); *U.S. Dep't. of Educ. v. Gerhardt (In re Gerhardt)*, 348 F.3d 89, 91 (5th Cir. 2003); *Hemar Ins. Corp. of Am. v. Cox (In re Cox)*, 338 F.3d 1238 (11th Cir. 2003); *United Student Aid Funds, Inc., v. Pena (In re Pena)*, 155 F.3d 1108, 1112 (9th Cir. 1998); *Pa. Higher Educ. Assistance Agency v. Faish (In re Faish)*, 72 F.3d 298, 306 (3d Cir. 1995); *In re Roberson*, 999 F.2d 1132, 1135 (7th Cir. 1993).

65 *See Long v. Educ. Credit Mgmt. Corp*. (*In re Long)*, 322 F.3d 549, 554 (8th Cir. 2003) (adopting the totality-of-the-circumstances test).

66 *See* Pardo & Lacey, *Empirical Assessment*, *supra* note 59, at 489 (explaining that the Brunner test and the totality of the circumstances test are not functional equivalents, in part because they cast the threshold of ability to repay in different terms).

67 *See* Iuliano, *supra* note 28, at 497; Pardo & Lacey, *Empirical Assessment*, *supra* note 59, at 487.

68 *See Nash v. Conn. Student Loan Found. (In re Nash)*, 446 F.3d 188, 190 (1st Cir. 2006) ("We see no need in this case to pronounce our views of a preferred method of identifying a case of 'undue hardship.'").

First Circuit has endorsed the totality of the circumstances test.[69] Some recent decisions have found that "[t]he appropriate test for assessing undue hardship remains an open question in the First Circuit[,]" and have analyzed whether a debtor is eligible for discharge under either the totality of the circumstances test or the Brunner Test.[70] Others have followed the Bankruptcy Appellate Panel and have analyzed the facts under the totality of the circumstances test.[71]

69 *See Bronsdon v. Educ. Credit Mgmt. Corp. (In re Bronsdon)*, 435 B.R. 791, 801 (B.A.P. 1st Cir. 2010) ("the Panel declines to adopt the Brunner test . . . . The Panel is persuaded that the totality of the circumstances test best effectuates the determination of undue hardship while adhering to the plain text of § 523(a)(8).").

70 *See e.g., Ayele v. Educ. Credit Mgmt. Corp.*, 490 B.R. 460, 462 (D. Mass. 2013) ("This Court agrees that Ayele has failed to meet his burden under either test.").

71 *See e.g., Smith v. United States Dep't of Educ. (In re Smith)*, 499 B.R. 55 (Bankr. D. Mass. 2013).

1. **Johnson and Bryant**

In one of the first cases to discuss the standard, *Pennsylvania Higher Educ. Assistance Agency v. Johnson*,[72] the bankruptcy court for the Eastern District of Pennsylvania set forth a three-pronged test. Under the Johnson Test, debtors must show: (1) a mechanical analysis of debtor's past resources and future probable resources, (2) the good faith of the debtor in attempting to pay back the student loan debt, and (3) a policy analysis focusing on the debtor's motives in filing for bankruptcy.[73] The first prong asks whether the debtor's future financial resources will be sufficient to allow the debtor to make student loan payments and maintain a minimal standard of living.[74] If the answer is no, the court would then turn to consider whether the debtor was irresponsible in managing his expenses, resources, and employment.[75] Finally, the third prong asks whether the debtor filed bankruptcy primarily to discharge his student loan debt and whether the debtor has benefitted from his education.[76] If the answer to these questions is no, discharge is appropriate.[77] Although the Johnson Test was riddled with complexity, it remained the leading approach in determining undue hardship for almost a decade.[78]

Eight years after *Johnson*, the same court decided *Bryant v. Pennsylvania Higher Educ. Assistance Agency*,[79] in which it acknowledged that the *Johnson* test was too complicated.[80] In *Bryant*, the bankruptcy court attempted to devise an objective test tying undue hardship to net income and poverty benchmarks. Under the test, often called the Bryant Poverty Test, debtors with an after-tax net income below the federal poverty level guidelines are entitled to discharge their student loan

72 5 Bankr. Ct. Dec. 532 (Bankr. E.D. Pa. 1979).
73 *Id.* at 544. For a discussion of how courts interpreted the three prongs, see Huey, *supra* note 41, at 102-104.
74 *Id.*
75 *Id.*
76 *Id.*
77 *Id.*
78 Franky Bayuk, *The Superiority of Partial Discharge for Student Loans Under 11 U.S.C. § 523(a)(8): Ensuring a Meaningful Existence for the Undue Hardship Exception*, 31 Fla. St. Univ. L. Rev. 1090, 1098 (2004).
79 72 B.R. 913 (Bankr. E.D. Pa. 1987).
80 *Id.* at 915.

debt.[81] In all other cases, a discharge may be granted if there are "unique" or "extraordinary" circumstances that would make repayment of student loans difficult for the debtor.[82] To be extraordinary, the circumstances must amount to more than mere unpleasantness. Under this test, a debtor's student loans are presumed dischargeable if the debtor's income is not "significantly greater than the poverty [level]."[83] However, the court did not define this phrase. Few courts adopted the Bryant test wholesale, but many courts following Bryant have considered the Federal Poverty Guidelines as part of their analysis.[84]

2. **Totality of the circumstances**

Some courts eschew adherence to any particular test and instead consider the totality of the circumstances surrounding the debtor's financial condition. Though this test is less restrictive than others, it is subjective and its application can be somewhat unpredictable particularly since courts consider different factors.[85] The Eighth Circuit has adopted[86] the totality of the circumstances test set out in *Andrews v. S. Dakota Student Loan Assistance Corp*.[87] The Eighth Circuit's test for undue hardship considers "(1) the debtor's past, present, and reasonably reliable future financial resources; (2) a calculation of the debtor's and her dependents' reasonable necessary living expenses; and (3) any other relevant facts and circumstances surrounding that particular bankruptcy case."[88] Courts applying this test will look at "the debtor's present employment and financial situation-including assets, expenses, and earnings-along with the prospect of future changes-positive or adverse-in the debtor's financial position."[89] The Eighth Circuit has stated that it prefers this less

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81 *Id.*

82 *Id.* at 917.

83 *Id.* at 915.

84 Robert F. Salvin, *Student Loans, Bankruptcy, and the Fresh Start Policy: Must Debtors Be Impoverished to Discharge Educational Loans?*, 71 TUL. L. REV. 139, 162 (1996).

85 *Id.* at 164 ("Since there is no uniformly accepted statement of the policy behind section 523(a)(8), the courts naturally differ in their interpretations.").

86 *See Long v. Educ. Credit Mgmt. Corp. (In re Long)*, 322 F.3d 549, 553 (8th Cir. 2003) ("we reaffirm the totality-of-the-circumstances test as set forth in *Andrews*); *see also Andresen v. Nebraska Student Loan Program, Inc., (In re Anderson)*, 232 B.R. 127, 139 (B.A.P. 8th Cir. 1999).

87 661 F.2d 702, 704 (8th Cir. 1981).

88 *Id.*

89 *Long*, 322 F.3d at 555.

restrictive approach to the undue hardship inquiry because it is more equitable.[90]

3. ***Brunner***

The most widely used test for evaluating dischargeability of a student loan under section 523(a)(8), the Brunner Test, states that a debt is dischargeable if three conditions are met. The test originated in *Brunner v. New York State Higher Educ. Servs. Corp.*.[91] The test is meant to analyze not the debtor's mere inability to pay, but that the debtor's inability to pay is likely to continue for a significant time.[92] The standard requires a three-part showing:

> (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 has made good faith efforts to repay the loans.[93]

Under this three-part test, the debtor must prove they have: 1) a current inability to repay, 2) future inability to repay, and 3) made a good faith effort to repay.[94] Because the test is written in the conjunctive, the debtor must prove all three elements; if the debtor fails to meet a requirement, the

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90 *Long*, 322 F.3d at 554 ("fairness and equity require each undue hardship case to be examined on the unique facts and circumstances that surround the particular bankruptcy.").

91 831 F.2d 395 (2d Cir. 1987). In *Brunner*, the debtor obtained a master's degree in social work and owed $9000 for undergraduate and graduate educations. Seven months after receiving her master's degree, the debtor filed for bankruptcy. The debtor was unemployed and received support in the form of Medicaid and food stamps. While the debtor had sent out over 100 resumes, she was unable to find employment. The bankruptcy court discharged the debtor's student loan debt pursuant to section 523(a)(8)(B). The loan guarantor appealed and, on appeal, the district court reversed the bankruptcy court's judgment. The district court found that the debtor satisfied the first prong of the test: she student loans accounted for 80% of her total debt, and she received public assistance. The debtor failed, however, to satisfy the requirements of the second prong. The debtor had no dependents and had employment-related job skills. The court thus found no evidence that her difficulties would persist. Finally, the court found that the debtor failed to meet the third prong since she filed bankruptcy just one month after her first loan payment became due and made to attempt to repay or defer payments on her loans. The court denied an undue hardship discharge of the debtor's student loans and remanded the action for the debts to be declared nondischargeable. *Brunner v. N.Y. State Higher Educ. Servs. Corp. (In re Brunner)*, 46 B.R. 752, 757-58 (S.D.N.Y. 1985), *aff'd*, 831 F.2d 395 (2d Cir. 1987) (stating that the debtor failed, under the second prong, to show her dire circumstances were likely to continue).

92 *See Hemar Ins. Corp. of Am. v. Cox (In re Cox)*, 338 F.3d 1238, 1242 (11th Cir. 2003).

93 *Brunner*, 831 F.2d at 396.

94 *See* Pardo & Lacey, *Scandal*, *supra* note 29, at 196-200 (summarizing the three *Brunner* prongs).

inquiry ends there and the student loan cannot be discharged.[95]

1) Current inability to repay

Under the first prong of the Brunner Test, the debtor must establish a current inability to repay his student loans by reference to a certain threshold quality of life.[96] A debtor is not expected to live in "abject poverty" to repay a student loan,[97] but student loan debt will not be discharged solely because the debtor may have to make personal and financial sacrifices.[98]

A court should examine the debtor's income and expenses in a manner that is sensitive to the particular circumstances of the case, taking into account the debtor's needs for care, including food, shelter, clothing, transportation medical treatment and a small source of recreation. In *Ivory v. United States (In re Ivory)*,[99] the bankruptcy court for the Northern District of Alabama articulated six specific needs: 1) shelter (including heating and cooling); 2) basic utilities such as electricity, water, natural gas, and telephones; 3) food and personal hygiene products (decent clothing and footwear and the ability to clean and replace those items when necessary); 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 pet.[100] Courts look to these elements in considering the debtor's income and expenses and whether there is anything left, after accounting for such needs, to pay towards student loans. This is a factual analysis that must be conducted on a case-by-case basis. Courts retain discretion over the methodological approach they use and may use different mechanisms to determine whether a debtor has satisfied the first prong of the Brunner Test. A review of cases shows that the calculation is quite fluid[101] and it can change with time. For example, courts have recently found that standard expenses for cell phones and Internet

95 *See id.* at 195 n.68 (collecting citations). It should be noted that the creditor initially bears the burden of establishing that the debt owed constitutes educational debt that is presumptively nondischargeable. Once the creditor makes that showing, the burden shifts to the debtor to prove undue hardship within the meaning of section 523(a)(8).

96 *Brunner*, 831 F.2d at 396.

97 *See Pennsylvania Higher Educ. Assistance Agency v. Faish (In re Faish)*, 72 F.3d 298, 306 (3d Cir. 1995).

98 *See Educ. Credit Mgmt. Corp. v. Howe (In re Howe)*, 319 B.R. 886, 889 (B.A.P. 9th Cir. 2005).

99 269 B.R. 890, 899 (Bankr. N.D. Ala. 2001).

100 *Id.*

101 Pardo & Lacey, *Scandal*, *supra* note 29, at 197.

are reasonable expenses.[102]

2) Future inability to repay

If a debtor satisfies the first element of the Brunner Test, he must then establish that, by virtue of additional circumstances, this state of affairs is likely to persist for a significant portion of the repayment period of the student loans.[103] In other words, the debtor must establish by a preponderance of the evidence that his financial situation is *not* likely to improve, that his inability to pay will persist.[104] The "additional circumstances test" requires that the court make a predictive judgment as to the likelihood that the debtor's financial hardship will continue for a significant portion of the repayment period.[105] This has been described as "the heart of the Brunner test," and it is often difficult to prove because it requires the debtor to show that he will be unable to repay his student loan debt in the future for reasons outside his control.[106] This prong has been equated to a debtor's showing of a certainty of hopelessness, an almost impossible burden to overcome.[107] Many commentators find that courts strictly construe this prong in a way that leads to harsh results that are unfavorable to debtors.[108]

The Court may consider the debtor's education, work history, health, and other circumstances. In *In re Nys*,[109] the Bankruptcy Appellate Panel for the Ninth Circuit compiled a nonexhaustive list of factors that may constitute "additional circumstances": 1) serious mental or physical disability of the debtor or the debtor's dependents which prevents employment or advancement; 2) the debtor's obligations to care for dependents; 3) lack of or severely limited education; 4) poor

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102 *See e.g., Nixon v. Key Educ. Ress. (In re Nixon)*, 453 B.R. 311, 329 (Bankr. S.D. Ohio 2011) (finding that telecommunications expenses are reasonable for entertainment, apply for employment online, and to communicate).

103 *Brunner*, 831 F.2d at 396.

104 There are two elements to the second prong: 1) whether the debtor's financial difficulties are "likely" to continue, and 2) that the duration of the debtor's financial hardship will be a significant portion of the repayment period.

105 *See* Pardo & Lacey, *Scandal*, *supra* note 29, at 197 (calling analysis under the second prong a "predictive exercise").

106 Austin, *supra* note 3, at 420; *see also Rifino v. United States (In re Rifino)*, 245 F.3d 1083, 1089 (9th Cir. 2001) (calling this requirement "instrumental" in effectuating congressional intent).

107 Huey, *supra* note 41, at 115-116.

108 *Id*.

109 308 B.R.436 (B.A.P. 9th Cir. 2004).

quality of education; 5) lack of usable or marketable job skills; 6) underemployment; 7) maximized income potential in the debtor's chosen education field and no other lucrative job skills; 8) a limited number of years remaining in the debtor's work life to allow repayment; 9) age or other factors that prevent restraining or relocation that would facilitate repayment; 10) lack of assets to repay the loans (whether exempt or not); 11) potentially increasing expenses that outweigh potential appreciation in value of the debtor's assets and/or likely increases in the debtor's income; and 12) lack of better financial options elsewhere.[110] The most important factor seems to be that the additional circumstances are beyond the debtor's control and not a result of the debtor's choice.

Many debtors who seek to discharge their student loan debt suffer from a medical condition or have a dependent who does,[111] and studies show that a medical condition greatly increases a debtor's odds of being granted a discharge.[112] This is often because medical conditions may interfere with a debtor's ability to work and generate income.[113] The debtor has the burden of proof to show the mental illness is severe enough to qualify for the discharge.[114] While medical records, depositions, and expert testimony can support the existence of a medical condition,[115] a debtor can testify about his medical problems and generally should not need to submit independent medical evidence to corroborate his testimony.[116] The most important factor when considering any mental illness under the Brunner Test is whether the medical condition is long-term, or extends into the

110 *Nys*, 446 F.3d at 946.

111 Pardo & Lacey, *Scandal*, *supra* note 29, at 205 (finding that the majority of debtors in their study – 55% - suffered from a medical condition or had a dependent who suffered from such a condition; 81% of those debtors had a work-limiting medical condition); *see also* Pardo & Lacey, *Empirical Assessment*, *supra* note 59, at 447 (finding that approximately 62% of the debtors in a study subset suffered from either a physical or mental condition).

112 Rafael Pardo, *Illness & Inability to Repay: The Role of Debtor Health in the Discharge of Educational Debt*, 35 Fla. St. U. L. Rev. 505 (2008) (revisiting data from his 2005 study with Michelle Lacey and finding that a medical condition increased a debtor's odds of being granted a discharge by 140%); *see also* Comment, *Student Loan Discharge – An Empirical Study of the Undue Hardship Provision of § 523(a)(8) under Appellate Review*, 30 Emory Bankr. Dev. J. 147, 190 (finding that while few characteristics impact a debtor's success appealing an undue hardship decision, the presence of a medical condition appears to be a differentiating factor).

113 Additionally, such debtors may have the financial burden of significant medical costs. *See* Pardo & Lacey, *Scandal*, *supra* note 29, at 205.

114 Kevin J. Smith, *Defining the Brunner Test's Three Parts: Time to Set a National Standard for All Three Parts to Determine When to Allow the Discharge of Federal Student Loans*, 58 S.D. L. REV. 250, 263 (2013) (citations omitted).

115 *Mosley v. Gen. Revenue Corp. (In re Mosley)*, 330 B.R. 832, 842-43 (Bankr. N.D. Ga. 2005).

116 *See Educ. Credit Mgmt. Corp. v. Mosley (In re Mosley)*, 494 F.3d 1320, 1325 (11th Cir. 2007) (following *Barrett v. Educ. Credit Mgmt. Corp.*, 487 F.3d 353 (6th Cir. 2007)).

future long enough, to prevent employment possibilities and thus render the ability to repay the federal student loan impossible.[117] While a debtor's health may play a role in determining whether a debtor's inability to repay will persist, commentators counsel that courts should be cautious not to rely too much on a debtor's health as a proxy for repayment ability.[118]

It is unclear whether a debtor's older age constitutes an additional circumstance that would satisfy the second prong of the Brunner Test. Age relates to a debtor's ability to repay because an individual's earning capacity plateaus, and may even decline, with age.[119] The *Brunner* opinion itself found that there were no additional circumstances noting that the debtor "was not disabled nor elderly,"[120] thus suggesting that advanced age may constitute an additional circumstance in some cases.[121] It seems to be a factor that courts will at least consider.[122]

3) **Good faith efforts to repay**

Finally, if a debtor has established both a current and future inability to repay, the debtor must show that he has made a good faith effort to repay the student loans.[123] Courts look to whether the debtor has acted responsibly toward his creditors and whether he is responsible for creating the hardship. This prong asks courts to consider a debtor's pre-bankruptcy conduct to determine whether he should be eligible for relief. Some argue that this factor should get more attention.[124]

Failure to make a payment, standing alone, does not establish lack of good faith.[125] The debtor must show that his failure to make payments results from factors "beyond his reasonable

117 Smith, *supra* note 113, at 263 (citing *King v. Vt. Student Assistance Corp. (In re King)*, 368 B.R. 358, 371 (Bankr. D. Vt. 2007)).

118 Pardo, *supra* note 111, at 522 (explaining that reference to a debtor's medical condition as part of the undue hardship inquiry may result in the improper sorting of debtors).

119 Pardo & Lacey, *Empirical Assessment*, *supra* note 59, at 443-44. The authors explain that health problems, and related costs, also increase with age which can contribute to reduced productivity and lower earnings. *Id*. at 444 n.173.

120 *Brunner*, 831 F.2d at 396.

121 *See e.g., Hinckle v. Wheaton Coll. (In re Hinckle)*, 200 B.R. 690, 694 (Bankr. W.D. Wash. 1996) (concluding that it was unlikely that the debtor, who was over the age of fifty, would be able to afford increased payments).

122 *See e.g., Gordon v. U.S. Dep't of Educ. (In re Gordon)*, No. 07-9049-MGD, 2008 Bankr. LEXIS 3878 (Bankr. N.D. Ga. Oct. 10, 2008) (noting that the debtor was 62-years-old in concluding that repaying the debtor's student loan debt would constitute an undue hardship).

123 *Brunner*, 831 F.2d at 396.

124 *See* Smith, *supra* note 113, at 266.

125 *Educ. Credit Mgmt. Corp. v. Polleys*, 356 F.3d 1302, 1311 (10th Cir. 2004).

control."[126] Courts often consider the debtor's payment history and efforts to negotiate a plan, as well as the debtor's efforts to obtain employment, maximize income, and minimize expenses.[127] Generally, the longer it is between the student's graduation, or leaving school, and the filing of a bankruptcy petition, the more this factor weighs in favor of the debtor.[128]

While courts often consider whether the debtor has negotiated a repayment plan, such as an Income Contingent Repayment Plan, a debtor is not *per se* required to apply for such a plan.[129] Courts recognize that such programs are not always viable options for debtors – while payments under such plans may be zero, interest of the debt continues to accrue and the amount forgiven at the end of twenty-five years can be treated as taxable income.[130] Other courts have found that if a debtor's failure to enroll in a repayment plan is almost prima facie evidence that it will be considered a lack of good faith.[131] Often, the record before the court may not indicate whether the debtor and the student loan creditor explored alternative repayment options, deferment, or forbearance.[132]

This final prong turns on several considerations including the debtor's efforts to make his payments by obtaining employment, maximizing income, reducing expenses, and/or participating in alternative payment options. These factors try to capture whether a debtor has used his best efforts to repay his student loan debt and are often hard to quantify.

VI. Studies

There are several studies that have reviewed student loan discharge proceedings to see how

126 *Roberson*, 999 F.2d 1132, 1136 (7th Cir. 1993).

127 Pardo & Lacey, *Scandal*, *supra* note 29, at 199.

128 Smith, *supra* note 113, at 266.

129 *Educ. Credit Mgmt. Corp. v. Mosley (In re Mosley)*, 494 F.3d 1320, 1327 (11th Cir. 2007).

130 Thus, such plans essentially require debtors to trade one nondischargeable debt for another. *See Educ. Credit Mgmt. Corp. v. Mosley (In re Mosley)*, 494 F.3d 1320, 1327 (11th Cir. 2007); *In re Barrett*, 487 F.3d 353, 364 (6th Cir. 2007); *see also Bronsdon v. Educ. Credit Mgmt. Corp. (In re Bronsdon)*, 435 B.R. 791, 802 (B.A.P. 1st Cir. 2010) ("The [income contingent repayment program] might be beneficial for a borrower whose inability to pay is temporary and whose financial situation is expected to improve significantly in the future. Where no significant improvement is anticipated, however, such programs may be detrimental to the borrower's long-term financial health." (citations omitted)).

131 *See, e.g., Pa. Higher Educ. Assistance Agency v. Birrane (In re Birrane)*, 287 B.R. 490, 500 (B.A.P. 9th Cir. 2002) (failing the "good faith" prong of the Brunner Test because debtor did not apply for the ICR plan).

132 *See e.g., Mosley v. Gen. Revenue Corp. (In re Mosley)*, 330 B.R. 832, 847 n.14 (Bankr. N.D. Ga. 2005).

often debtors obtain a discharge from their student loans and what factors make a debtor more likely to succeed. Three empirical studies that warrant discussion are: Rafael Pardo and Michelle Lacey's study of published court opinions spanning a ten-year period; Pardo and Lacey's examination of student loan discharges in the Western District of Washington over a four-year period; and Jason Iuliano's study of student loan adversary proceedings filed nationwide in 2007.

1. **Rafael I. Pardo & Michelle R. Lacey, *Undue Hardship in the Bankruptcy Courts: An Empirical Assessment of the Discharge of Educational Debt*, 74 U. Cin. L. Rev. 487 (2005)**

Pardo and Lacey set out to systematically analyze the decision-making process of bankruptcy judges who make undue hardship determinations. The authors looked at 261 hardship opinions issued by bankruptcy courts from October 1993 to October 2003. They concluded that nearly half of the debtors (45%) who filed an adversary proceeding to discharge student loan debt were successful in obtaining some relief.[133] Pardo and Lacey found that a court's assessment of a debtor's future inability to repay was often determinative,[134] but found very few statistically significant differences in the factual circumstances of those debtors who were granted a discharge and those who were denied a discharge.[135] The authors found that debtors who obtained a student loan debt discharge generally had: 1) lower monthly incomes, 2) lower monthly expenses, and 3) were more likely to have a medical problem or a dependent with a medical problem.[136] Pardo and Lacey also suggested that the judge's personal sentiments and the experience of the debtor's attorney were important variables in the outcome. The authors concluded that the opinion that student-loan debtors with an ability to repay will abuse the bankruptcy system by seeking to discharge student loans is unfounded; rather, cases shows that debtors who do seek to discharge their student loan debt are generally struggling under the weight of oppressive educational debt.

2. **Rafael I. Pardo & Michelle R. Lacey, *The Real Student-Loan Scandal: Undue Hardship Discharge Litigation*, 83 Am. Bankr. L.J. 179, 196-200 (2009)**

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133 Pardo & Lacey, *Empirical Assessment*, *supra* note 59, at 479.

134 *Id*. at 503.

135 *Id.* at 433.

136 *Id*. at 481-86. They also found that women predominated the group seeking relief from educational debt and that debtors in the study tended to be middle-aged. *Id*. at 441-445. The majority of debtors also had at least one dependent.

Pardo and Lacey conducted a second empirical study based on a dataset of 115 student-loan discharge proceedings that were filed in the Bankruptcy Court for the Western District of Washington from 2002 – 2006. Pardo and Lacey found that granting a debtor a discharge from student loan debt was the rule rather than the exception – approximately 57% of adversary proceedings resulted in an undue hardship discharge – but that relief was granted in a haphazard fashion.[137] They examined the cases and found that seven variables weighed in favor of discharge: 1) the debtor's annual household income was below the poverty line; 2) the debtor failed to attain the education pursued with the borrowed funds; 3) the debtor or a dependent suffered from a medical condition; 4) the debtor suffered from a work-limiting medical condition; 5) the debtor was more than 55 years old; 6) the debtor obtained the student loans on behalf of a third-party (as a co-signing parent for example); and 7) the debtor was unemployed.[138] Most of these variables relate to the debtor's future inability to repay,[139] thus underscoring the prominence of the second prong of the Brunner Test in student loan discharge decisions. Additionally, Pardo and Lacey found that debtors with "highly experienced" attorneys were more likely to obtain discharges.[140] They also found that discharge decisions depended upon which judge presided over the case.[141] While they found that the typical debtor seeking to discharge student loan debt is "in horrible financial shape,"[142] the authors ultimately concluded that financial hardship is a less significant factor than it should be. Pardo and Lacey conclude that congressional reform is necessary to allow debtors access to a fresh start.[143]

3. **Jason Iuliano, *An Empirical Assessment of Student Loan Discharges & the Undue Hardship Standard*, 86 Am. Bankr. L.J. 495 (2012)**

A more recent study shows that 99.9 of bankrupt student-loan debtors do not even try to discharge their student loans. Jason Iuliano examined 207 student loan cases filed in 2007 and found

137 Pardo & Lacey, *Scandal*, *supra* note 29, at 183.
138 *Id.* at 223.
139 *Id*. (explaining that the first variable relates to the debtor's current inability to repay, while the last variable speaks to the debtor's good faith efforts to repay).
140 *Id*. at 233.
141 *Id*. at 234. Pardo and Lacey posit that this may be because some judges more actively attempt to facilitate settlement than others. *Id*.
142 *Id.* at 207. Debtors in their study had an annual household income of approximately $20,800. *Id.*
143 *Id*. at 235.

that eighty-one debtors (39%) discharged some portion of their student loans.[144] When debtors do seek to discharge their student loan debts, he found that three variables are predictive of discharge: 1) whether the debtor has a medical hardship; 2) whether the debtor is employed; and 3) the debtor's income the year before filing bankruptcy. Medical hardship is positively correlated with receiving a discharge; being employed and having a larger income in the year preceding bankruptcy are negatively correlated.[145]

First, at to a medical hardship, it appears that just having a medical condition is a strong predictor of whether a debtor will receive a discharge. This variable is indicative of one's future inability to repay. Second, Iuliano found that unemployed debtors are significantly more likely to receive discharges. This variable relates to both the current and future inability to repay prongs. Third, the debtor's income the year before filing bankruptcy is indicative of a debtor's current inability to repay student loan debt. These three factors match the first two prongs of the Brunner Test quite closely and show that debtors in bad economic positions are more likely to get relief. Iuliano found that judges will consider a number of factors in determining whether a debtor has made a good faith effort to repay his student loans, such as whether he has pursued administrative remedies or is actively seeking employment, none of which are particularly easy to quantify. Iuliano found that whether a debtor hires an attorney appears to have little correlation with discharge outcome.[146] Thus, according to Iuliano's data, a debtor who proceeds *pro se* is just as likely to receive a discharge as a debtor who is represented by counsel.[147]

Iuliano's main conclusion, that debtors overwhelming do not even attempt to discharge student loan debt in bankruptcy, is supported by other recent studies.[148] Iuliano posits that so few student-loan debtors attempt to discharge their student debt in part because the view that student loans are nearly impossible to discharge is a self-fulfilling process – debtors who hear that it is

144 *Id.* at 512. Most commonly, in fifty-six cases, debtors settled with their student loan creditors. In twenty cases, judges entered a judgment that the student loan debt was dischargeable. Four cases ended with default judgment and one case ended in summary judgment. *Id.*

145 *Id.* at 518.

146 *Id.*

147 *Id.* at 521-22.

148 *See* Austin, *supra* note 3, at 399-400 ("Even in seemingly plausible cases the debtors did not attempt to have the debt discharged. . . . A number of cases I reviewed showed debtors with five-figure or six-figure student loan debt and modest income, but they did not attempt to have the debt discharged."); *see also* Exceptionalism, *supra* note 9, at 589 (noting that few debtors even attempt to make use of section 523(a)(8)).

nearly impossible to meet the undue hardship standard believe that their chances of success are minimal and are less likely to attempt to discharge their student loans.[149] Some debtors may also not pursue an adversary proceeding if they believe that they need an attorney but cannot afford one.[150]

These studies show that debtors rarely attempt to discharge their student loan debt. When they do, certain factors (such as medical hardship, employment status, and income) have a bearing on whether the student loan debt will be discharged. These studies all show that debtors seeking to discharge their student loan debt generally do so while experiencing significant financial distress, and many are destitute. As Pardo and Lacey explain, this contrasts sharply with the image of an opportunistic debtor seeking to avoid repayment of student loans on the eve of a lucrative career.[151]

VII. Partial discharge

Further complicating the student loan discharge issue is that some courts permit a debtor to discharge a part of an educational debt while others do not. Some courts permit partial discharges, others do not, and some courts take a "hybrid," or loan-by-loan, approach where the debtor has multiple student loan debts by declaring some of the individual loans dischargeable. The courts are split and the debate over whether a court may partially discharge a debtor's student loan has grown over the past two decades.[152]

1. Partial discharge allowed

Because of the harsh outcomes most debtors face as a result of the undue hardship tests, some courts allow partial discharges of student loans as a way to "promote[] fairness by affording some relief to the debtor, while ensuring that the government is not unjustly deprived by a complete discharge of student loans that could be repaid in part without imposing 'undue hardship.'"[153]

Some courts in favor of partial discharges infer their authority from the equitable powers codified in section 105(a) of the Bankruptcy Code. Section 105(a) provides that "the court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions

149 Iuliano, *supra* note 28.
150 *Id.* at 523.
151 Pardo & Lacey, *Empirical Assessment*, *supra* note 59, at 405.
152 Scott Pashman, Note, *Discharge of Student Loan Debt Under 11 U.S.C. § 523(A)(8): Reassessing "Undue Hardship" After the Elimination of the Seven-Year Exception*, 44 N.Y.L. SCH. L. REV. 605, 617-18 (2001).
153 *Id.*

of this title."[154] Some courts rely on this provision, in connection with section 523(a)(8), to grant a partial discharge of student loan debt by discharging part of the principal, accrued interest, or attorney's fees.[155] For example, the Sixth[156] and Ninth[157] Circuits, have held that bankruptcy courts may exercise their equitable authority under section 105(a) to partially discharge student loan debt. Some commentators have argued that granting partial discharges comports with the legislative history of section 523(a)(8) while ensuring fairness.[158]

2. **No partial discharges**

Courts in other circuits have held that the Bankruptcy Code does not allow for partial discharge.[159] These opinions adopt the view that Congress's silence in 523(a)(8) should foreclose that possibility. These courts reason that if Congress intended for courts to revise or partially discharge student loans, Congress could have expressly provided for those options in 523(a)(8) or included broader language revealing such equitable solutions as a policy objective.[160] Although the argument for allowing partial discharges is that they seem like a fair and equitable solution to the strict application of the undue hardship exception, this is an argument better made to Congress than to the bankruptcy courts.[161] Several commentators have argued that, until Congress specifically amends section 523(a)(8) to allow for partial discharges, courts must take an all-or-nothing approach.[162]

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154 11 U.S.C. § 105(a).

155 *See e.g., Griffin v. Eduserv (In re Griffin)*, 197 B.R. 144, 147 (Bankr. E.D. Okla. 1996) ("It would be an 'undue hardship' for the Debtors to pay any of the accrued interest and attorneys' fees associated with . . . student loans.").

156 *See Tenn. Student Assistance v. Hornsby (In re Hornsby)*, 144 F.3d 433, 440 (6th Cir. 1998); *Miller v. Pa. Higher Assistance Agency (In re Miller)*, 377 F.3d 616, 620 (6th Cir. 2004) ("When a debtor does not make a 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.").

157 *Saxman v. Educ. Mgmt. Corp. (In re Saxman)*, 325 F.3d 1168, 1173 (9th Cir. 2003).

158 *See* Bayuk, *supra* note 77.

159 *See e.g., Pa. Higher Educ. Assistance Agency v. Faish (In re Faish)*, 72 F.3d 298, 307 (3d Cir. 1995); *Educ. Credit Mgmt. Corp. v. Carter*, 279 B.R. 872, 876 (M.D. Ga. 2002) (concluding that section 523(a)(8) does not allow the bankruptcy court to grant a partial discharge of student loan debt).

160 *See* Pashman, *supra* note 151, at 617 (citing *Andresen v. Nebraska Student Loan Program, Inc. (In re Andresen)*, 232 B.R. 127, 130 (B.A.P. 8th Cir. 1999)).

161 Huey, *supra* note 41, at 114 (stating that partial discharges portray an obvious case of judicial lawmaking and add to the unpredictability in this area of bankruptcy law.).

162 Huey, *supra* note 41, at 114; *see also* Amanda M. Foster, *All or Nothing: Partial Discharge of Student Loans Is*

Critics of a partial discharge also argue that section 105(a) of the Bankruptcy Code does not provide authority for partial discharge or revision of student loans; rather, the equitable powers of bankruptcy courts may only be exercised within the enumerations of the Code. This argument seems particularly relevant in light of the recent Supreme Court decision, *Law v. Siegel*,[163] in which the Supreme Court emphasized that section 105(a) has its limits. The Court explained, "It is horn-book law that §105(a) 'does not allow the bankruptcy court to override explicit mandates of other sections of the Bankruptcy Code.'"[164] Section 105(a) confers authority to "carry out" the provisions of the Code, but it is quite impossible to do that by taking action that the Code prohibits.[165] This suggests that courts should not necessarily rely on section 105(a) to partially discharge student loan debt.

3. **Loan-by-loan approach**

Finally, some courts take a "hybrid," or loan-by-loan, approach where the debtor has multiple student loan debts by declaring some, but not all, of the individual loans dischargeable. For example, in *Hinkle v. Wheaton Coll. (In re Hinkle)*,[166] the debtor sought to discharge her student loan debt, consisting of six separate loans. The court found that while it could not bifurcate a single loan into dischargeable and nondischargeable portions, it could conduct an analysis for each separate loan and discharge those loans that would create an undue hardship. The court discharged three of the debtor's six loans, but it failed to provide reasoning as to which three loans should be discharged.

The current debate over partial discharges adds another wrinkle to the student loan issue and shows that bankruptcy courts often struggle with how they should to fairly treat student-loan debtors in the face of harsh "undue hardship" standard.[167]

Not the Answer to Perceived Unfairness of the Undue Hardship Exception, 16 Widener L.J. 1053, 1084 (2007) (asserting that partial discharge is not permitted because under § 523(a)(8), "the entire debt must create an undue hardship.").

163 134 S. Ct. 1188 (2014).

164 *Id*. at 1194 (citing 2 Collier on Bankruptcy ¶105.01[2], p. 105–6 (16th ed. 2013)).

165 *Id.* The Court continued: "We have long held that 'whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of' the Bankruptcy Code." *Id.* at 1196 (internal citations omitted).

166 200 B.R. 690 (Bankr. W.D. Wash. 1996).

167 *See* Huey, *supra* note 41, at 115 ("the current debate over partial discharges is one dilemma that has developed as a result of another problem: the current undue hardship tests provide too harsh a burden for most student loan debtors to overcome.").

VIII. The future and alternatives

For years, commentators have derided the undue hardship requirement as too burdensome and have attacked the courts for applying the standard in an inconsistent manner.[168] There are many different suggestions for how to change the treatment of student loans in bankruptcy. For example, critics have advocated for: repealing section 523(a)(8) so that student loan debt is treated as any other general unsecured debt; excluding private student loans from the exception (thereby making private student loans dischargeable); reinstating the time-lapse discharge; defining undue hardship with a clear national standard; creating a new claims process for educational loan creditors; encouraging student-loan debtors to pursue federal loan repayment programs; and, finally, risk-based student loans.

1. Repealing section 523(a)(8)

Many commentators and consumer advocates have argued that Congress should repeal section 523(a)(8) to allow student-loan debtors to discharge their student loans.[169] By repealing the undue hardship exception, student loans would be treated like other unsecured debts and would be presumptively dischargeable.[170] This is a fairly popular argument and, in 1997, the National Bankruptcy Review Commission[171] recommended that all educational loans be treated no differently than other unsecured debts.[172] Advocates argue that repealing 523(a)(8) would resolve much of the confusion surrounding the undue hardship exception while also providing student-loan debtors with some recourse.[173] This proposal recognizes that if debtors cannot discharge their student loan ob-

168 Iuliano, *supra* note 28, at 525.

169 *See e.g.,* Linda E. Coco, *Mortgaging Human Potential: Student Loan Indebtedness & the Practices of the Neoliberal State*, 42 SW. L. Rev. 565, 599-600 (2013); Huey, *supra* note 41, at 119 ("Congress should repeal 523(a)(8) to enable student loans to be dischargeable under the Bankruptcy Code once again."); Exceptionalism, *supra* note 9, at 598-600 (urging the federal government to begin risk-rating its student loans and to repeal section 523(a)(8)); *see also The Student Loan "Debt Bomb": America's Next Mortgage-Style Economic Crisis?*, National Association of Consumer Bankruptcy Attorneys, www.nacba.org.

170 Austin, *supra* note 3, at 415 (explaining that many commentators have recommended that student debt be returned to the list of nonpriority general unsecured debt).

171 The National Bankruptcy Review Commission is an independent commission established pursuant to the Bankruptcy Reform Act of 1994.

172 *See* Coco, *supra* note 168, at 599-600 (citing *Nat'l Bankr. Review Comm'n, Bankruptcy: The Next Twenty Years*, National Bankruptcy Review Commission 6-17 (Oct. 20, 1997)).

173 Huey, *supra* note 41, at 119.

ligations they often have little hope of every getting out from under their debt.[174] Pardo and Lacey emphasize this point in writing: "If Congress is actually serious about restoring the social safety net for student-loan debtors, all fingers point for wholesale repeal of the Bankruptcy Code's student-loan discharge provision."[175] A bill has been introduced in Congress to do just that.[176]

2. **Making private student loans dischargeable**

Some have argued that private student loans should be dischargeable. Prior to 1984, student loans obtained from an entity other than a "non-profit institution of higher education" were treated the same in bankruptcy as other unsecured debt, and many believe that private loans should be dischargeable to the same extent as other unsecured debt.[177] Supporting this proposal is the fact that eligibility for a private educational loan is already based on the borrower's creditworthiness.

H.R. 5043, the Private Student Loan Bankruptcy Fairness Act of 2010, would have reversed the amendments of 2005 and removed bankruptcy protections for private/for-profit student lenders. A similar companion bill was introduced in the senate. The house bill was sent to committee but never made it to a vote on the floor; the Senate bill also stalled.[178] The student loan industry opposed the legislation.[179] While H.R. 5043 did not succeed, it did incite interest in student loan reform.[180]

3. **Reinstating the time-lapse discharge**

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174 Exceptionalism, *supra* note 9, at 604.

175 Pardo & Lacey, *Scandal*, *supra* note 29, at 182.

176 Austin, *supra* note 3, at 415 n.567 (citing H.R.J. Res. 365, 112th Cong. (2011), 2011 CONG. U.S. H.RES. 365 (Westlaw)).

177 Aaron N. Taylor, *Undo Undue Hardship: An Objective Approach to Discharging Federal Student Loans in Bankruptcy*, 38 J. LEGIS. 185, 234 (2012).

178 Brendan Baker, Comment, *Deeper Debt, Denial of Discharge: the Harsh Treatment of Student Loan Debt in Bankruptcy, Recent Developments, & Proposed Reforms*, 14 U. PA. J. BUS. L. 1213, 1221-22 (2012).

179 Interestingly, a spokeswoman for Sallie Mae indicated that the while the company wanted to private student loans to receive the same protections as federal student loans, the company would support "reform that would allow federal and private student loans to be dischargeable in bankruptcy for those who have made a good-faith effort to repay their student loans over a five-to-seven-year period and still experience financial difficulty." It thus seems that the loan industry might be somewhat willing to reinstate the time lapse rule that was eliminated in 1998. *Id*. at 1222-23.

180 *Id*. at 1223.

Another possibility is that Congress could reinstate a time-lapse discharge. From 1978 to 1990, unless he could prove undue hardship, a debtor had to wait five years after a loan first became due before the debt could be discharged in bankruptcy.[181] From 1990 to 1998 that time was extended to seven years. One commentator has likened time-lapse discharge to the discharge of tax debt, noting that most tax debt can be discharged after three years of its accrual thus mitigating the soft fraud of new graduates filing for bankruptcy promptly upon graduation.[182]

4. **A national standard for undue hardship**

If section 523(a)(8) is to stay, Congress could define the term "undue hardship." Some have argued that Congress should adopt a national standard for undue hardship that would test whether the debtor is able to afford to pay the debt. Such a standard would allow bankruptcy courts to take a more uniform approach in determining whether to discharge a debtor's student loan debt.[183] One author suggests using the current "means test" for the chapter 7 and 13 bankruptcy petitions in order to determine a debtor's ability to maintain a minimal standard of living under the first prong of the Brunner Test.[184] Another has argued that the Brunner Test does a good job of analyzing "undue hardship" and should stay, but that the test should be modified to shift the burden of proof regarding "additional circumstances" from the debtor to the party opposing dischargeability.[185]

5. **New claim of an education loan or education benefit creditor**

One author has proposed that the Code be amended to include a new claim of an education loan or education benefit creditor: if the debtor wants any of his education debt discharged, then instead of filing an adversary proceeding to establish undue hardship under section 523(a)(8), the debtor would file a motion to determine the fair market value of his student loan debt.[186] The mo-

181 Austin, *supra* note 3, at 416.

182 *Id.*; *see also* Abbye Atkinson, *Race, Education Loans, & Bankruptcy*, 16 MICH. J. RACE & L. 1, 36-37 (2010).

183 Smith, *supra* note 113, at 257.

184 *Id.*

185 Grant, *supra* note 30, at 847.

186 Austin, *supra* note 3, at 417-19. The author suggests that fair market value means the amount that an investor would pay to purchase the respective student loan obligation. He states that it would not be difficult to determine the fair market value of student loans because there is an active secondary market in bonds backed by bundles of student loans. *Id.*

tion would be similar to a motion to determine the value of a secured interest under section 506.[187] The amount of the claim equal to the fair market value would be nondischargeable; the remaining balance would be treated as dischargeable, general unsecured debt.[188] While this is a unique idea (it has yet to be embraced by others), it suggests that there may be other ways to deal with student loan debt in bankruptcy.

6. Restricting access on the front end: risk-based pricing

Others have proposed changes to the student loan process that would make access to loans more difficult.[189] According to these proposals, the Government should price its student loans by looking at a student's post-graduation employment prospects.[190] Risk-based pricing of student loans would signal the long-term financial risks inherent in different courses of study. A fully risk-based approach to loan limits would focus on expected debt-service- payment-to-income ratios.[191] The relevant question would not simply be how much students borrow each year; instead, the focus would be on whether students' incomes at graduation and beyond will be sufficient to repay their debts over the next ten to thirty years.[192] According to one paper, the Government should consider 1) the institution the borrower plans to attend and 2) the course of study the borrower pursues.[193] Risk-based pricing would help students understand the links between educational choices, such as picking a major, and employment opportunities.[194]

This proposal seems somewhat likelier than others. In August 2013, President Obama proposed a college rating system that would rate colleges on value and performance. The Education Department plans to circulate a draft proposal this spring; it would then put a system into effect

187 *Id.*
188 *Id.*
189 Exceptionalism, *supra* note 9, at 598-600 (urging the federal government to begin risk-rating its student loans and to repeal section 523(a)(8)).
190 *Id.*
191 *See* Michael Simkovic, *Risk-Based Student Loans*, 70 WASH. & LEE L. REV. 527 (2013).
192 *Id.*
193 *Id.* at 599. The article also argues that Congress should repeal section 523(a)(8). *Id.* at 603-610.
194 *See id.*

in 2015. High-scoring colleges would receive more federal student aid or better interest rates on federal loans. Education Secretary Arne Duncan has defended the idea, saying that "helping young people and families have more information and make better choices."[195] While this proposal has several proponents, there are still many who are skeptical.[196]

7. **Encourage students to pursue remedies available through federal programs**

Finally, some argue that student-loan debtors struggling to repay their educational debt should strongly consider alternative repayment programs. While these programs are no silver bullet, they may provide a debtor some breathing room and flexibility while he attempts to repay student loan debt. A debtor's efforts to explore an income contingent repayment plan or loan consolidation options may also be relevant if the status quo does not change and bankruptcy courts continue to apply the Brunner Test – such efforts often indicate that a debtor is putting forth his best efforts to repay the loan obligations in light of her financial circumstances.

IX. Conclusion

While debtors can generally use bankruptcy to deal with insurmountable debts, student-loan debtors encounter tough obstacles to discharge. Academics have argued that the undue hardship standard is burdensome and applied in a harsh and inconsistent manner. Recent studies suggest that debtors facing that difficult burden often do not even attempt to discharge their student loans. Commentators recognizing that many debtors may have a very real need for relief have proposed a variety of remedies, from simply encouraging debtors to file adversary proceedings to repealing 523(a)(8).

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195 Nick Anderson, *Duncan defends Obama's college rating plan*, The Washington Post (Dec. 13, 2013), http://www.washingtonpost.com/local/education/duncan-defends-federal-college-rating-plan-one-week-after-napolitano-voiced-skepticism/2013/12/13/9b9f4af0-640e-11e3-a373-0f9f2d1c2b61_story.html.

196 *Id.*

11 U.S.C. §523(a)(8) and "UNDUE HARDSHIP" UNDER THE "TOTALITY OF THE CIRCUMSTANCES" TEST

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I. "Totality of the Circumstances" test

Bankruptcy courts in the Eighth Circuit use a "totality of the circumstances" test in which the court considers (1) the debtor's past, present, and reasonably reliable future financial resources; (2) a calculation of the reasonable living expenses of the debtor, and her dependants; and (3) "any other relevant facts and circumstances surrounding each particular bankruptcy case."[1] Thus, a debtor established undue hardship where she cared for five children, including two autistic children, and where 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.[2]

A key difference between the three-part *Brunner* test and the "totality of the circumstances" test is that efforts to repay the debt can be a factor in determining discharge, but is not an essential element. Thus, where the debtor's' monthly payment in an income-based student loan repayment program ("IBR") would be zero, the court will not require the debtor to participate in the program as a condition of finding undue hardship.[3] On the other hand, if the debtor's reasonable future financial resources will sufficiently cover payment of student loan debt, while still allowing for a minimal standard of living, then the debt will not be discharged.[4]

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1 . 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).

2 . *In re Walker*, 650 F.3d at 1234–35.

3 Grimes v. ECMC (*In re* Grimes), 2013 WL 5592913 (Bankr. Neb. 2013) at *2 (debtor's age, level of education, work experience, and health condition establish that the debtor is unable to pay the student loan debt).

4 Nielsen v. ACS, Inc. (*In re* Nielsen), 473 B.R. 755, 759 (8th Cir. B.A.P. 2012).

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."[5]

In absence of specific instructions from the First Circuit Court of Appeals, bankruptcy courts in Massachusetts typically employ a totality of the circumstances test.[6] In Bronsdon v. Educational Credit Management Corp. (*In re* Bronsdon),[7] the First Circuit BAP held that neither the second prong of *Brunner* (the debtor's state of affairs is likely to persist) nor the third prong (good faith effort to repay the loan) was required under the Code:

> 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 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.[8]

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, 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.[9] In addition, federal loan forgiveness effectively trades nondischargeable loan debt for nondischargeable tax debt.[10] Accordingly, many loan repayment programs may not be suitable for debtors, and the court should not consider them when determining whether the debtor should be allowed a discharge.[11]

Despite its differences with the three-prong *Brunner* test, proof of undue hardship under the "totality of circumstances test" is a heavy burden and depends upon the debtor's particular circumstances.[12] Thus, where debtor had occasional medical issues but, by participating in the Ford Repayment program would have sufficient income to meet his needs, the debtor did not qualify for discharge of student loans.[13]

5. Nash v. Connecticut Student Loan Found. (*In re* Nash), 446 F.3d 188, 190–91 (1st Cir. 2006).

6. *See, e.g.*, Bronsdon v. Educ. Credit Mgmt. Corp. (*In re* Bronsdon), 435 B.R. 791 (B.A.P. 1st Cir. 2010).

7. *Id.* at 802.

8. *Id.* at 800, (citing Hicks v. Educ. Credit Mgmt. Corp. (*In re* Hicks), 331 B.R. 18, 27–28 (Bankr. D. Mass. 2005)).

9. *Id.* at 802.

10. *Id.* at 802–03.

11. *Id.*

12 Ablavsky v. U.S. Dept. of Educ. (*In re* Ablavsky), 504 B.R. 709, 721 (Bankr. Mass. 2014).

13 Ayele v. Educ. Credit Mgmt. Corp. (*In re* Ayele), 490 B.R. 460 (D. Mass. 2013).

II. Partial Discharge of Education Debt

A number of courts have allowed debtors to discharge part of their student loan debt, using either the three *Brunner* factors or the totality of the circumstances test. For example, the Sixth Circuit has held that partial discharge is permitted under § 105 (a)[14] using the three-part *Brunner* criteria.[15] The debtor must satisfy each prong of the *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.[16] In one case, a bankruptcy court found that the debtor's circumstances satisfied the *Brunner* test for discharge of all but $8,045.02 of her total student loan debt of $36,284.81.[17] The debtor had cancer, and therefore thus "it is highly likely that [the debtor's] financial predicament will persist for many years, and possibly the rest of her life."[18]

Courts in the Tenth Circuit,[19] Eleventh Circuit,[20] and lower courts in the Ninth Circuit[21] also grant partial discharge of student loans using the *Brunner* criteria.

Other courts have granted 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.[22] The court held that if the debtor participated in an income-based repayment program, then she would receive a bankruptcy discharge for the portion of the debt remained at the expiration of the 25-year repayment period.[23]

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14. 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) ("[W]hen a debtor does not make a 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.").

15. *In re* Oyler, 397 F.3d 382, 385 (6th Cir. 2005); *In re* Nixon, 453 B.R. 311, 336 (Bankr. S.D. Ohio 2011) (stating that a court may grant partial discharge of student loan debt).

16. *In re Nixon*, 453 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).

17. Jorgensen v. Educ. Credit Mgmt.. Corp., 2012 Bankr. LEXIS 254 *17 (Bankr. D. Haw, 2012).

18. *Id.* at *13.

19. *See* Alderete v. Educ. Credit Mgmt. Corp. (*In re* Alderete), 412 F.3d 1200 (10th Cir. 2005).

20. *See* Hemar Ins. Corp. v. Cox (*In re* Cox), 338 F.3d 1238, 1243 (11th Cir. 2003) ("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).").

21. *See* Saxman v. Educ. Mgmt. Corp. (*In re* Saxman), 325 F.3d 1168, 1173 (9th Cir. 2003) ("[B]ankruptcy courts may exercise their equitable authority under 11 U.S.C. § 105(a) to partially discharge student loans."); Educ. Credit Mgmt. Corp. v. 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).

22. Stevenson v. Educ. Credit Mgmt. Program (*In re* Stevenson), 463 B.R. 586 (Bankr. D. Mass. 2011).

23. *Id.* at 599.

There is nothing in the Code that expressly permits partial discharge of student loan debt. Section 523(a)(8) provides for discharge of "an educational benefit overpayment or loan."[24] This appears to mean discharge of a loan in its entirety, not just a part of the loan. In contrast, other sections of the Code specifically provide for adjustment of a portion of a debt. For example, § 506(a)(1) allows secured debts to be bifurcated into secured and unsecured components "to the extent of the value of such creditor's interest in [the collateral]."[25] In consumer Chapter 7 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."[26] In these provisions, the words *to the extent* show that partial treatment of the claim is allowed. There is no such language in connection with education debt.

In absence of specific language allowing for partial discharge of education debt, some courts grant partial discharge pursuant to § 105 (a), which provides that "[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title."[27] Courts have even cited § 105 (a) to grant discharge of accrued interest or attorney's fees in connection with a student loan debt,[28] institute a repayment schedule, defer repayment, and to allow a debtor to reopen bankruptcy proceedings to revisit the question of undue hardship.

However, a number of courts have held that the Bankruptcy Code does not allow for partial discharge. These include the Third Circuit[29] and many bankruptcy courts.[30] Some commentators have likewise criticized the use of § 105(a) to grant partial discharge.[31]

In cases where a debtor has multiple education loans, some courts have granted full discharge of some of the debtor's loans, while leaving the others non-dischargeable. In one case where the debtor had 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 was able to pay the three remaining loans totaling $10,014.[32] In another case, the debtor failed to prove that repaying a loan

24 . 11 U.S.C. § 523(a)(8) (2012).

25 . *Id.* § 506(a)(1).

26 . *Id.* § 522(f)(1)(A).

27 . *Id.* § 105(a).

28 . Griffin v. Eduserv (*In re* Griffin), 197 B.R. 144, 147 (Bankr. E.D. Okla. 1996) ("[I]t would be an 'undue hardship' for the Debtors to pay any of the accrued interest and attorneys' fees associated with . . . student loans.").

29 . Pa. Higher Educ. Assistance Agency v. Faish (*In re* Faish), 72 F.3d 298, 307 (3d Cir. 1995).

30 . *See, e.g.*, *In re Pincus*, 280 B.R. at 311 ("The Bankruptcy Code clearly does not permit a court to discharge in part a single student loan obligation.").

31 . *See* Daniel B. Bogart, *Resisting the Expansion of Bankruptcy Court Power Under Section 105 of the Bankruptcy Code: The all Write Act and an Admonition from Chief Justice Marshall*, 35 Ariz. St. L.J. 793 (2003); *see also* Amanda M. Foster, *All or Nothing: Partial Discharge of Student Loans Is Not the Answer to Perceived Unfairness of the Undue Hardship Exception*, 16 Widener L.J. 1053, 1084 (2007) (asserting that partial discharge is not permitted because under § 523(a)(8), "the entire debt must create an undue hardship.").

32 . Hinkle v. Wheaton Coll. (*In re* Hinkle), 200 B.R. 690, 694 (Bankr. W.D. Wash. 1996); *see also* Gharavi v. U.S. Dep't. of Educ. & Educ. Mgmt. Corp. (*In re* Gharavi), 335 B.R. 492, 501 (Bankr. D. Mass. 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).

that the debtor had obtained for own education would result in undue hardship, however, having to repay a parent PLUS loan she obtained for the benefit of her son would result in undue hardship, and so the second loan was discharged.[33] Other courts use a similar loan-by-loan approach.[34] But there is nothing in the Bankruptcy Code that provides for this type of prioritization, and several courts have held that loan-by-loan discharge is inappropriate.[35]

33 Smith v. U.S. Dept. of Educ. (In re Smith), 499 B.R. 55 (Bankr. Mass. 2013) (the court utilized the "totality of the circumstances" test).

34 . *E.g.*, Conway v. National College Trust (*In re* Conway), 495 B.R. 416, 423 (8th Cir. B.A.P. 2013) (directing bankruptcy court to review each of debtor's 15 separate loans for undue hardship); *In re* Gharavi, 335 B.R. 492 (discharging three out of four student loans, but debtor remained liable on one of them); Hollister v. Univ. of N.D. (*In re* Hollister), 247 B.R. 485 (Bankr. W.D. Okla. 2000); Ledbetter v. U.S. Dept. of Educ. (*In re* Ledbetter), 254 B.R. 714 (Bankr. S.D. Ohio 2000).

35 . *See* Pincus v. Graduate Loan Ctr. (*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).