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2019 Alexander L. Paskay Memorial Bankruptcy Seminar

Consumer Session

Consumer Bankruptcy Legal Update

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43rd Annual Alexander L. Paskay Memorial Bankruptcy Seminar
Consumer Bankruptcy Legal Update

Presented by:

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Consumer Bankruptcy Legal Update Materials
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May 21, 2018

Office of Postsecondary Education
U.S. Department of Education
Washington, D.C.

Re: Docket ID ED-2017-OPE-0085, Request for Information on Evaluating Undue Hardship Claims in Adversary Actions Seeking Student Loan Discharge in Bankruptcy Proceedings

On behalf of the American Bankruptcy Institute's Commission on Consumer Bankruptcy, we submit the attached comments in response to the Department of Education's request for information (RFI) on the evaluation of undue hardship claims in bankruptcy.

The American Bankruptcy Institute (ABI) is the world's largest association of insolvency professionals, made up of over 11,000 members in multi-disciplinary roles, including attorneys, bankers, judges, lenders, professors, turnaround specialists, accountants and others. These members represent debtor, creditor and other stakeholder interests. Founded in 1982, ABI is non-profit and non-partisan and organized under Internal Revenue Code section 501(c)(3). ABI also plays a leading role in providing congressional leaders and the general public with unbiased reporting and analysis of bankruptcy regulations, laws and trends. ABI is often called on to testify before Congress, analyze proposed bills, and conduct periodic briefings for congressional committees, legislative staff, other government regulators and the media.

In December 2016, the ABI's board of directors passed a resolution creating the Commission on Consumer Bankruptcy and charging the Commission with "researching and recommending improvements to the consumer bankruptcy system that can be implemented within its existing structure." The Commission and its three advisory committees are composed of fifty-two bankruptcy professionals. The commissioners and committee members represent all stakeholders in the bankruptcy system, including attorneys who primarily represent debtors and attorneys who primarily represent creditors as well as chapter 7 trustees, chapter 13 trustees, retired bankruptcy judges, government officials, and academics. As of the date of this letter, the Commission and its committees have conducted seven public meetings in which we have heard from seventy-eight witnesses. We have received 131 written comments. The Commission and its committees have

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held fifty-seven private meetings to debate possible reforms. More information, including the membership of the Commission and its committees, is available at our web site: <https://consumercommission.abi.org/>.

Many of the witnesses at our public meetings and the persons who sent us written comments urged the Commission to address the treatment of student loans in bankruptcy. The Commission has placed student loans on its publicly available list of topics to be studied.

We will release the Commission's final report in the coming year. The final report will set out comprehensive recommendations on student loans in bankruptcy, including recommendations for legislative changes about how student loans are treated in both chapter 7 and chapter 13 bankruptcies.

We had not intended to release any of the Commission's recommendations until the final report. However, in light of the Department of Education's request for information and the importance of the student-loan issue, the Commission agreed to release several recommendations that directly respond to the RFI. These recommendations focus on the regulatory reforms that are the subject of the RFI and should not be understood as the Commission's recommendations for possible legislative changes or any other reforms.

The Commission has debated and approved the attached recommendations, which state the conclusions of the Commission as a deliberative law reform group. As such, they do not necessarily reflect the views of any individual associated with the Commission. The Commission also has two non-voting, ex officio members as representatives of the U.S. Trustee Program and Internal Revenue Service. These two ex officio members provided technical assistance and institutional perspectives but took no position on proposals made by the Commission.

We hope that you find these comments helpful as you consider changes to the "Dear Colleague" letter mentioned in the RFI. The Department of Education plays an important role in the administration of the student-loan system. Action at the regulatory level could have a major effect in alleviating the growing burdens of student debt on everyday Americans and the overall economy. If the Commission can provide other helpful information or be of further assistance, please do not hesitate to reach out to us.

Sincerely,



William H. Brown
U.S. Bankruptcy Judge (retired), Western District of Tennessee
co-chair, ABI Commission on Consumer Bankruptcy



Elizabeth L. Perris
U.S. Bankruptcy Judge (retired), District of Oregon
co-chair, ABI Commission on Consumer Bankruptcy

American Bankruptcy Institute's Commission on Consumer Bankruptcy

Recommendations to the Department of Education: Evaluating Undue Hardship Claims in Adversary Actions Seeking Student Loan Discharge in Bankruptcy Proceedings

I. Promulgation and Interpretation of Regulations

Through regulations or interpretive guidance, the Department of Education should provide the following with respect to governmental student loans:

(a) *Bright-line Rules.* Creditors should not oppose discharge proceedings where the borrower meets any of a set of the criteria below. These criteria should be set out in federal guidelines that indicate household financial distress and therefore undue hardship:

(1) *Disability-based guidelines.* The borrower (i) is receiving disability benefits under the Social Security Act or (ii) has either a 100% disability rating or has a determination of individual unemployability under the disability compensation program of the Department of Veterans Affairs.

(2) *Poverty-based guidelines.*

(A) In the seven years before bankruptcy, the borrower's household income averaged less than 175% of the federal poverty guidelines.

(B) At the time of bankruptcy, the borrower's household income is less than 200% of the federal poverty guidelines and (i) the borrower's only source of income is from Social Security benefits or a retirement fund or (ii) the borrower provides support for an elderly, chronically ill, or disabled household member or member of the borrower's immediate family.

(b) *Avoiding Unnecessary Costs.* Creditors should accept from the borrower proof of undue hardship based on the above criteria without engaging in formal discovery.

(c) *Alternative Payment Plans.* Payment of the loans in bankruptcy should be effective (i) to satisfy any period of forgiveness or cancellation of the loans under an income driven repayment plan, (ii) to rehabilitate a loan in default, and (iii) in chapter 13 cases, to prevent the imposition of collection costs and penalties.

II. Best Interpretation of 11 U.S.C. § 523(a)(8)

(a) *Brunner Test*. The three-factor *Brunner* test should be understood to require the debtor to establish only that

(1) the debtor cannot pay the student loan sought to be discharged according to its standard ten-year contractual schedule while maintaining a reasonable standard of living,

(2) the debtor will not be able to pay the loan in full within its initial contractual payment period (10 years is the standard repayment period) during the balance of the contractual term, while maintaining a reasonable standard of living, and

(3) the debtor has not acted in bad faith in failing to pay the loan prior to the bankruptcy filing.

(b) *Standard of Proof*. Each of these factors should be understood to require proof by a preponderance of the evidence.

(c) *Appellate Review*. The determination of the bankruptcy court as to each of the factors should be recognized as a finding of fact subject to deference in appellate review and in the consideration of appeal by the Department of Education, any guaranty agency, eligible lender, or holder of a federal student loan, and any agent of these parties.

Discussion & Explanation

Student loan debt is one of the most significant economic problems facing the United States. According to Federal Reserve data, outstanding student loan debt has tripled since 2006, from under \$500 billion to over \$1.5 trillion.¹ In 2003, both credit card and auto loan indebtedness were several times the amount of student loan debt, but now student loan debt greatly exceeds them both.² Among all types of household debt, student loans have the highest delinquency rate.³ As a percentage of the balance, the most recent data show 11.0% of student loans as 90+ days delinquent as compared to 7.6% for credit card debt, 4.1% for auto loans, and 1.3% for home mortgages.⁴

Student loan overindebtedness causes overall economic activity to decline and constrains the post-college options that students have. Academic studies have associated student debt with

¹ These figures are from the Federal Reserve's G.19 release on consumer credit, available at <https://www.federalreserve.gov/releases/g19/current/default.htm>.

² See Federal Reserve Bank of New York, Quarterly Report on Household Debt and Credit (2017:Q4), at 3 (Feb. 2018) https://www.newyorkfed.org/medialibrary/interactives/householdcredit/data/pdf/HHDC_2017Q4.pdf.

³ See *id.* at 12-14.

⁴ *Id.* at 12.

(1) lower earnings of college graduates,⁵ (2) lower levels of homeownership,⁶ (3) lower automobile purchases,⁷ (4) increases in household financial distress,⁸ (5) lower probability of students to choose public-service careers,⁹ (6) poorer psychological functioning,¹⁰ (7) delayed marriage,¹¹ and (8) lower probability of continuing education through graduate school.¹² Student loans thus affect not only those who owe the loans but also have consequences that ripple through our communities and our nation. Because of its regulatory and oversight powers, the Department of Education can make substantial inroads in alleviating the student debt problem that will improve the lives of all Americans.

Repayment of federal student loans is in the best financial interest of the federal government. To further this purpose, the Department of Education has sensibly adopted programs that promote the responsible repayment of student loans. At the same time, federal bankruptcy law recognizes that highly distressed student loan borrowers may not be able to repay their loans even with these options. Those bankrupt debtors who can show “undue hardship” can have their student loans discharged in bankruptcy.¹³ Our comments seek to balance these competing interests.

Bright-line rules

The current options used by the Department of Education have not always proven to be the most sensible, cost-effective manner of addressing collection processes for student loan borrowers who have filed for bankruptcy. Costly and inefficient litigation both causes the federal

⁵ See Justin Weidner, “Does Student Debt Reduce Earnings” (Nov. 11, 2016) (unpublished manuscript) https://scholar.princeton.edu/sites/default/files/jweidner/files/Weidner_JMP.pdf.

⁶ See Alvaro A. Mezza, Daniel R. Ringo, Shane M. Sherlund & Kamilia Sommer, “Student Loans and Homeownership” (June 2017); Rajashri Chakrabarti, Nicole Gorton & Wilbert van der Klaauw, “Diplomas to Doorsteps: Education, Student Debt, and Homeownership,” Liberty Street Economics blog (Apr. 3, 2017) <http://libertystreeteconomics.newyorkfed.org/2017/04/diplomas-to-doorsteps-education-student-debt-and-homeownership.html>.

⁷ See Meta Brown & Sydnee Caldwell, “Young Student Loan Borrowers Retreat from Housing and Auto Markets,” Liberty Street Economics blog (Apr. 17, 2013) <http://libertystreeteconomics.newyorkfed.org/2013/04/young-student-loan-borrowers-retreat-from-housing-and-auto-markets.html>.

⁸ See Jesse Bricker & Jeffrey Thompson, *Does Education Loan Debt Influence Household Financial Distress? An Assessment Using the 2007-2009 Survey of Consumer Finances Panel*, 34 CONTEMP. ECON. POL’Y. 660 (2016).

⁹ See Erica Field, *Educational Debt Burden and Career Choice: Evidence from a Financial Aid Experiment at NYU Law School*, 1 AM. ECON. J.: APPLIED ECON. 1 (2009); Jesse Rothstein & Cecilia Elena Rouse, *Constrained After College: Student Loans and Early-Career Occupational Choices*, 95 J. PUB. ECON. 149 (2011).

¹⁰ See Katrina M. Walsemann, Gilbert C. Gee & Danielle Gentile, *Sick of Our Loans: Student Borrowing and the Mental Health of Young Adults in the United States*, 124 SOCIAL SCI. & MED. 85 (2015).

¹¹ See Dora Gicheva, *Student Loans or Marriage? A Look at the Highly Educated*, 53 ECON. EDUC. REV. 207 (2016).

¹² See Vyacheslav Fos, Andres Liberman & Constantine Yannelis, “Debt and Human Capital: Evidence from Student Loans” (Apr. 2017) (unpublished manuscript) <https://ssrn.com/abstract=2901631>.

¹³ 11 U.S.C. § 523(a)(8).

government to incur substantial costs in the bankruptcy collection process with little recovery and leaves bankrupt borrowers without effective relief. It is in the interest of the federal government and borrowers that the government uses a more cost-effective approach for collection from student loan borrowers who have filed bankruptcy cases. Having clear, objective bright-line rules would reduce the costs of undue hardship litigation for the borrowers, the creditors, and the courts, while encouraging the debtors who genuinely need bankruptcy relief (and their attorneys) to seek it.

Our recommendations suggest two sets of bright-line rules,¹⁴ one built around federal Social Security and veterans disability benefits and the other based on the federal poverty guidelines. Both require the borrower to have undergone eligibility screening by a federal administrative agency. More importantly, both indicate borrowers highly likely to be in severe financial distress and therefore highly likely to be incurring undue hardship.

To be eligible for disability benefits under the Social Security Act, an individual must have an “inability to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or which has lasted or can be expected to last for a continuous period of not less than 12 months.”¹⁵ Veterans disability benefits require either a 100% disability rating or a showing that includes the inability to hold “substantial gainful employment,” a threshold interpreted to mean an inability to earn more than the federal poverty guideline.¹⁶

Our second set of guidelines are built around the federal poverty guidelines. The most recently revised federal poverty guidelines are:¹⁷

Household Size	Poverty Guideline
1	\$12,140
2	\$16,460
3	\$20,780
4	\$25,100

We suggest two thresholds. First, any borrower whose household income averages less than 175% of the national poverty guidelines – currently \$21,245 for a household of one – for the seven years before a bankruptcy filing be considered to have undue hardship. We recommend increasing the figure to 200% of the national poverty guidelines at the time of a bankruptcy filing for two

¹⁴ Our recommendations for bright-line rules and cost-savings draw upon a 2014 letter from seven members of Congress. See Press Release, “Cohen, 6 Members of Congress Urge Education Secretary to Bring More Fairness to Struggling Students” (May 16, 2014) <https://cohen.house.gov/press-release/cohen-6-members-congress-urge-education-secretary-bring-more-fairness-struggling>.

¹⁵ 42 U.S.C. § 423(d)(1).

¹⁶ See, e.g., Faust v. West, 13 Vet. App. 342, 356 (Vet. App. 2000).

¹⁷ See Annual Update of the HHS Poverty Guidelines, 83 Fed. Reg. 2642 (Jan. 18, 2018) <https://www.federalregister.gov/documents/2018/01/18/2018-00814/annual-update-of-the-hhs-poverty-guidelines>.

situations to account for personal circumstances: retirees on fixed incomes and persons providing support for an elderly, chronically ill, or disabled household or family member.

The Department of Education's "Dear Colleague" letter, dated July 7, 2015, refers to certain factors, including determinations of disability by the Department of Veterans Affairs and Social Security Administration as "negat[ing] the need for discharge of their student loans in bankruptcy." A borrower may have reasons for filing bankruptcy that include but are not limited to student loan debt. A judicial remedy also sometimes can help solve problems that an administrative remedy might not, such as tax liability from the discharged debt. As the "Dear Colleague" letter notes, the administrative and judicial remedies can be "equally effective." Just as there is no reason for the Department's guidelines to deprive a borrower of an administrative remedy when an equally effective judicial remedy is available, there is no reason to deprive the borrower of the judicial remedy because an administrative remedy is available, especially when the judicial remedy can address other debt and legal issues the borrower might be facing. The "Dear Colleague" letter should respect the choice the borrower makes in addressing debt problems.

Avoiding Unnecessary Costs

Current regulations require a determination of whether "the expected costs of opposing the discharge petition would exceed one-third of the total amount owed."¹⁸ If so, the discharge petition should not be opposed. Despite the direction in the regulation, it is the sense of the Commission that student loan collectors have often vigorously litigated student loan discharge proceedings regardless of the cost/benefit of the litigation.

Student loan creditors should accept and evaluate the borrower's evidence without reference to formal guidelines such as court discovery rules. We are not recommending that the student loan creditor simply accept any evidence on blind faith. Rather, the creditor should exercise good judgment and discretion about the reliability of the borrower's evidence. Using informal processes will lower costs for both creditor and borrower. Formal litigation discovery processes should be the last, not the first resort. If the borrower submits satisfactory evidence of undue hardship outside the litigation process, the student loan creditor should agree that the debtor is entitled to discharge of the student loan debt.

Alternative Repayment Plans

Regulations also should be considered to address how chapter 13 bankruptcy interacts with the student-loan repayment programs. The Department of Education already is authorized to accept alternative minimum payments for borrowers under "exceptional circumstances."¹⁹ The safeguards built into the confirmation of a chapter 13 plan set out statutory requirements more stringent than the Department's income-driven repayment plans, including a liquidation analysis

¹⁸ 34 C.F.R. § 682.402(i)(1)(iii).

¹⁹ *Id.* § 685.208(l)(1).

that is not otherwise considered by the Department. These safeguards should suffice for determining the amount necessary for an alternative repayment.

Also, outside of bankruptcy, borrowers can generally only cure a default on a student loan either through consolidation of their loans or rehabilitation.²⁰ 11 U.S.C. § 1322(b)(5), however, allows a chapter 13 plan to “provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim on which the last payment is due after the date on which the final payment under the plan is due.” Section 1322(b)(5) should be interpreted to apply to the cure and maintenance of student loan payments, and the Department of Education should accept this treatment under chapter 13 plans, both to increase student loan payments and avoid unnecessary collection costs.

These observations lead to the following specific proposals for reform. Pursuant to 20 U.S.C. § 1087e(d)(4), the regulations regarding alternative repayment plans at 34 C.F.R. § 685.208(l) should be amended to provide (1) that the payments under a confirmed chapter 13 plan constitute an “exceptional circumstance” sufficient for the Department of Education to accept any disbursements from a chapter 13 plan as an alternative repayment and (2) that, notwithstanding, the provisions of 34 C.F.R. § 685.219(c)(iv) and 34 C.F.R. § 685.221(f)(1), such payments apply towards any period of forgiveness or cancellation of the student loans under the applicable income driven repayment plan.

The Department of Education also should amend 34 C.F.R. § 685.211(f)(1) to provide that the amount “of a borrower’s reasonable and affordable payment based on the borrower’s financial circumstances” includes amounts paid through a borrower’s chapter 13 plan to “cure and maintain” payments under 11 U.S.C. §1322(b)(5). The Department also should amend 34 C.F.R. § 30.62 to provide that, if student loan payments are made through a chapter 13 plan, the Department of Education will forego administrative costs under 34 C.F.R. § 30.60 and penalties assessed under 34 C.F.R. § 30.61.

Best Interpretation of 11 U.S.C. § 523(a)(8)

As the Request for Information notes, many courts have interpreted the undue hardship standard using a three-factor test known as the *Brunner* test. This test provides that undue hardship exists only if—

- (1) 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) 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) the debtor has made good faith efforts to repay the loans.²¹

²⁰ *Id.* §§ 685.211(f), 685.220.

²¹ *Brunner v. New York State Higher Education Services*, 831 F.2d 395, 396 (2d Cir. 1987). As the Request for Information also notes, the Eighth Circuit uses a “totality of the circumstances” test. *See Long*

The second of these factors has often been described as requiring the debtor to establish a “certainty of hopelessness” regarding payment of the student loan sought to be discharged.²² With this strict judicial case law in place, very few debtors have sought to discharge student loans in bankruptcy.²³

The Commission believes the widely accepted *Brunner* test can be an appropriate standard for determining undue hardship, balancing consideration of the debtor’s present ability to pay student loan indebtedness, the debtor’s future ability to make the loan payments, and the debtor’s good faith in connection with the loan. However, as pointed out by the Seventh Circuit, the “glosses” that some decisions have added to the *Brunner* test do not always track the language of the statute itself.

The district judge did not doubt that [the debtor] has paid as much as she could during the 11 years since receiving the educational loans. Instead the judge concluded that good faith entails commitment to future efforts to repay. Yet, if this is so, no educational loan ever could be discharged, because it is always possible to pay in the future should prospects improve. Section 523(a)(8) does not forbid discharge, however; an unpaid educational loan is not treated the same as a debt incurred through crime or fraud. The statutory language is that a discharge is possible when payment would cause an “undue hardship”. It is important not to allow judicial glosses, such as the language in . . . *Brunner*, to supersede the statute itself.²⁴

We believe the best interpretation of the *Brunner* test will hew closely to the statute. In particular, we believe the Department should adopt the following interpretations:

(a) Courts and the Department should determine the degree of hardship based on the contractual terms of the loan itself, rather than alternatives offered by the creditor, such as federal income-based repayment plans.²⁵

v. Educational Credit Mgmt. Corp., 322 F.3d 549 (8th Cir. 2003). The Commission’s recommendations apply to whichever judicial test is used.

²²See, e.g., Educational Credit Mgmt. Corp. v. Frushour (In re Frushour), 433 F.3d 393, 401 (4th Cir. 2005); Olyer v. Educational Credit Mgmt. (In re Olyer), 397 F.3d 382, 386 (6th Cir. 2005).

²³ See Jason Iuliano, *An Empirical Assessment of Student Loan Discharges and the Undue Hardship Standard*, 86 AM. BANKR. L.J. 495, 499 (2012) (“[B]arely 0.1 percent of student loan debtors in bankruptcy sought to discharge their educational debts.”).

²⁴ Krieger v. Educational Credit Mgmt. Corp., 713 F.3d 882, 884 (7th Cir. 2013)

²⁵ See In re Engen, 561 B.R. 523, 548 (Bankr. D. Kan. 2016) (pointing out difficulties with these repayment plans).

(b) Undue hardship should be found if repayment of the loan according to its terms would prevent the debtor from paying reasonable living expenses, rather than requiring living at a poverty level.²⁶

(c) The factual determinations required by *Brunner* should be subject to the ordinary evidentiary burden, preponderance of the evidence. The debtor should not be required to prove that future repayment of the student loan is certain to be hopeless.²⁷

(d) The fact-findings of a bankruptcy court on the *Brunner* factors should be recognized as entitled to deference on appeal, and reversible only for clear error.²⁸

Our recommendations for regulatory reforms and the best interpretation of the *Brunner* test are presented as complementary parts of a more effective treatment of student loan debt. If the Department were not to adopt those regulatory reforms, we would advocate that those reforms – including the adoption of bright-line rules – be incorporated into decisions applying § 523(a)(8) case law.

²⁶ See *Ivory v. United States (In re Ivory)*, 269 B.R. 890, 899 (Bankr. N.D. Ala. 2001) (listing items necessary to maintain a minimal standard of living).

²⁷ See *Price v. DeVos (In re Price)*, 573 B.R. 579, 601 (Bankr. E.D. Pa. 2017) (“[T]he phrase ‘certainty of hopelessness’ carries a connotation that vastly overstates the debtor’s evidentiary burden under § 523(a)(8). . . . It is time to retire its use.”), *rev’d on other grounds* 2018 WL 558464 (E.D. Pa. 2018).

²⁸ See *ECMC v. Acosta-Conniff (In re Acosta-Conniff)*, 686 F. App’x 647, 649 (11th Cir. 2017) (“A bankruptcy court’s findings as to each of the three prongs of the Brunner test are factual findings that should be reviewed by the district court for clear error; not under a de novo standard of review.”).

April 16, 2016

Lower Courts Split on Nondischargeability of Education-Related Loans

New York judges narrowly define ‘educational benefit’ to discharge student loans.

Disagreeing with several other lower courts, two bankruptcy judges from the Eastern District of New York held within the last month that some types of education loans are not excepted from discharge as an “educational benefit” under Section 523(a)(8)(A)(ii).

The first case, decided on March 24 by Chief Bankruptcy Judge Carla E. Craig of Brooklyn, N.Y., held that a bar loan is an ordinary consumer loan, not an “educational benefit” that would be nondischargeable.

In her case, a student in law school got a \$15,000 bar loan in 2009 from a commercial lender. She paid the loan until 2012 and filed a chapter 7 petition in 2014. After receiving a discharge, she sued the lender, seeking a declaration that the loan was discharged. The lender filed a motion to dismiss and lost.

The loan would not have been nondischargeable under Section 523(a)(8)(A)(i) because it was neither guaranteed by the government nor made by a nonprofit institution. Consequently, the lender contended that the loan was an “educational benefit” excepted from discharge under subsection (a)(8)(A)(ii).

Judge Craig said that some courts have held that an “educational benefit” includes “any loan which relates in some way to education.” She said such a “broad interpretation” would “render superfluous most of the other provisions in Section 523(a)(8).”

“Educational benefit,” she said, must be read in tandem with “scholarship or stipend,” the other descriptive words in the subsection, and that those words must refer to “something other than a loan.” In her view, subsection (a)(8)(A)(ii) refers to “types of conditional grants.”

Judge Craig disagreed with bankruptcy courts elsewhere that explicitly hold that bar loans are nondischargeable. She also disagreed with those courts holding that 2005 amendments to the subsection no longer limit nondischargeability to loans made or guaranteed by “governmental units or non-profits.”

Bankruptcy Judge Robert E. Grossman of Central Islip, N.Y., agreed with Judge Craig’s analysis in his opinion on April 4. Judge Grossman’s case involved a woman with \$160,000 in loans incurred to secure a “degree” from an unaccredited, unlicensed

foreign medical school. He held that the loan was dischargeable because it did not fall within the exception to discharge under subsection (a)(8)(A)(ii).

Judge Grossman read the statute to mean that an “educational benefit” excepted from discharge in the subsection “refer[s] to educational debts other than loans.” He said that the subsection “is not a ‘catch-all’ provision designed to encompass any educational claim arising out of any transaction that bestows an educational benefit on a debtor.”

The loan in Judge Grossman’s case did not fall within any of the other categories that would render the debt nondischargeable because the loan was not a “qualified education loan,” nor was it made or guaranteed by the government or a nonprofit institution.

Because she held that a bar loan is not an “educational benefit,” Judge Craig did not go so far as other courts by holding that obligations under subsection (ii) must meet one of the requirements in subsection (i).

On the Edge

BY VINCENT J. ROLDAN AND ELIZABETH L. GUNN

Trekking Through the Quagmire A Creative Discharge Solution to the Student Loan Crisis

Editor's Note: For more on this topic, purchase *Graduating with Debt: Student Loans* under the Bankruptcy Code (2nd Edition), now available in the ABI Store (store.abi.org). Members must log in first to obtain reduced pricing.



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There is about \$1.41 trillion in outstanding student loan debt — more than total credit card debt and more than auto loan debt, according to the Federal Reserve Bank of New York's quarterly report on household debt and credit.¹ More than 10 percent of this debt is delinquent or in default. There are about 44 million student loan borrowers, the average amount of debt per borrower is \$39,400,² and the level of debt has grown significantly in recent years. Since 2008, student loan debt relative to overall household debt has grown from 5 percent to 30 percent.³ This growth has some commentators predicting that the student loan industry is the next economic "bubble" that will burst.⁴

One congressman has introduced legislation to assist borrowers with burdensome student loan debt.⁵ For the time being, student loan borrowers must evaluate their repayment options in the context of the current environment in which bankruptcy and discharge is likely not an option for the large majority of these borrowers. However, bankruptcy courts might be increasingly willing to relax the standard to discharge governmental student loans, or at least a portion thereof. The recent case *In re Modeen*⁶ is an example.

The Standard

Although individuals with mounting debt might seek relief under the Bankruptcy Code and use the discharge provisions to help obtain a "fresh start," individuals with student loan debt face an uphill battle. Section 523(a)(8) of the Bankruptcy Code denies such individuals the benefit of a discharge.

Section 523(a)(8) provides that a bankruptcy discharge does not discharge "an educational ... loan made, insured or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution."⁷ Individual debtors generally receive no discharge for "any other educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986."⁸ As pointed out in *Modeen*, the Bankruptcy Code denies the discharge of student loan debt "unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor's dependents."⁹

The term "undue hardship" is not defined in the Bankruptcy Code. The *Modeen* court, like many other courts, cited to *Brunner v. New York State Higher Educ. Servs. Corp.*, which held that in order to support a finding of undue hardship, the court must find:

- (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.¹⁰

The debtor has the burden of establishing each element of the *Brunner* test by a preponderance of the evidence.¹¹

Modeen Facts

In *Modeen*,¹² the debtor was an individual in her mid-30s who worked full-time as an office manager and a few hours per week at a second job. She had an 18-year-old daughter whom she supported. Between her two jobs, she earned about \$688 per week net of taxes, and her 2017 adjusted gross income was \$40,997. She had \$34,231.55 in student loan debt, and her required monthly payments were \$694.47. She argued that her income and expenses

1 "Total Household Debt Rises for 15th Straight Quarter, Led by Mortgages, Student Loans," Federal Reserve Bank of New York (May 17, 2018), available at newyorkfed.org/newsevents/news/research/2018/rp180517 (unless otherwise specified, all links in this article were last visited on Oct. 29, 2018).

2 "A Look at the Shocking Student Loan Debt Statistics for 2018," Student Loan Hero (May 1, 2018), available at studentloanhero.com/student-loan-debt-statistics.

3 Noah Smith, "The Financial Crisis Isn't Over for Students," Bloomberg (March 27, 2018), available at bloomberg.com/view/articles/2018-03-27/financial-crisis-is-over-for-housing-but-not-for-student-loans.

4 Jim Rogers and Robert C. Baum, "This Economic Bubble Is Going to Wreak Havoc When It Bursts," *Fortune* (July 10, 2017), available at fortune.com/2017/07/10/higher-education-student-loans-economic-bubble-federal.

5 "Rep. Peter DeFazio Introduces Legislation to Improve Student Loan Assistance and Expand College Access," Press Release (April 18, 2018), available at defazio.house.gov/media-center/press-releases/rep-peter-defazio-introduces-legislation-to-improve-student-loan.

6 *In re Modeen*, 586 B.R. 298 (Bankr. W.D. Wis. 2018).

7 11 U.S.C. § 523(a)(8)(A)(i).

8 11 U.S.C. § 523(a)(8)(B).

9 *Modeen* at 302.

10 *Id.* (citation omitted).

11 *Id.* (citation omitted).

12 *Id.* at 301.

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were such that payment of her student loans would be an undue hardship on her and her dependent daughter. What made the debtor's loans unique was that she refinanced the loans with an individual lender. Due to the refinancing, the debtor was not able to take advantage of federal student loan repayment programs.

The *Modeen* court quickly considered the first and third *Brunner* prongs, and found that the debtor would not be able to maintain a minimal standard of living if compelled to make her monthly payments of \$694.47.¹³ Even without including her student loan payments, her monthly income enabled her to barely cover her living expenses. In addition, the court found that the debtor made a good-faith effort to repay her loans, her expenses were not outrageous, and she sought a second job, which indicated that she had made efforts to repay her creditors.¹⁴

The court then examined the second *Brunner* prong: whether there were "additional circumstances" making it improbable that she would ever be able to repay her student loans. The *Modeen* court pointed out that in the Seventh Circuit, the bar for the second prong was set rather high.¹⁵ Courts consider factors such as "psychiatric problems, lack of usable job skills, and severely limited education."¹⁶ Then the court referenced two examples:

In *Goulet*, a convicted felon with alcohol and substance abuse problems did not establish "additional, exceptional circumstances" necessary to satisfy this prong. Instead, he was "an intelligent man" who did not lack usable job skills and could "apply himself when he desire[d]." He had "simply failed to diligently pursue employment such that he would be able to alleviate his financial burdens." In *Roberson*, the debtor had "a bleak forecast for the near future" as he was unemployed, had lost his driver's license after a second drunk driving conviction, and had wrist and back injuries. However, those circumstances were only temporary, as his medical condition was not "insurmountable," he would be able to regain his driver's license, and neither the injuries nor the loss of license prevented him from finding employment in the future.¹⁷

The *Modeen* court then considered the debtor's circumstances and found that she had not shown "exceptional hopeless circumstances."¹⁸ She was employed, had held various jobs for the past five years, and had marketable skills in human resources and health care. She had an associate of arts degree from the University of Phoenix, a technical diploma, with honors, certificates in gerontology, and was qualified to provide care to aging adults.¹⁹ She showed persistence in finding and obtaining employment.²⁰

The *Modeen* court also noted that while there are many cases where a court discharges student loans of a debtor is near retirement age or is handicapped, the debtor in *Modeen* was neither.²¹ The debtor asserted that her dependent daughter made her circumstances unique.²² However, the court was persuaded by cases that criticize debtors who claim expenses for the care of adult live-in children.²³

Partial Discharge

Even though the debtor in *Modeen* did not meet the *Brunner* elements, the court analyzed whether the debtor was eligible for a partial discharge. Courts acknowledge that the Bankruptcy Code does not explicitly authorize a partial discharge, but they recognize that "an all-or-nothing approach to the dischargeability of student debt contravenes Congress's intent in granting bankruptcy courts equitable authority" to enforce the Code.²⁴ The *Modeen* court surveyed decisions in the Sixth, Seventh and Ninth Circuits and concluded:

There are no clear guidelines on when a court should grant a partial discharge on student loans. In general, it should be "reserved for appropriate circumstances" when "the equities of the situation weigh distinctly in favor of the debtor."²⁵

The *Modeen* court found that the equities favored the granting of a partial discharge. The debtor simply did not have enough "room in her budget" to repay the balance of the \$34,231.55 loan, nor could she reasonably be expected to pay \$694.47 per month.²⁶ Since the loans were refinanced, the loans were also no longer eligible for federal repayment programs.²⁷ Thus, the court distinguished *Modeen* from other cases where those repayment programs were available.²⁸ Without the ability to use a repayment program, "her plea to this Court [might] be her last chance to obtain relief from a crushing financial quagmire."²⁹

The court used federal repayment plans as a guideline for determining how much the debtor could reasonably pay.³⁰ Under one payment plan, the debtor's monthly payment would be determined by applying her tax-filing status, adjusted gross income, family size, geographic area and estimated income growth.³¹ The court also considered evidence of what the daughter could reasonably contribute toward expenses (even with the daughter's medical condition).³²

Ultimately, the court determined that the debtor must pay \$208 per month for 154 months, which would be recalculated each year based on income, tax-filing status and family size.³³

¹³ *Id.* at 302.

¹⁴ *Id.* at 305.

¹⁵ *Id.* at 303.

¹⁶ *Id.* (citation omitted).

¹⁷ *Id.* (citing *Goulet v. Educ. Credit Mgmt. Corp.*, 284 F.3d 773, 778 (7th Cir. 2002); *In re Roberson*, 999 F.2d 1132, 1135 (7th Cir. 1993)).

¹⁸ *Id.*

¹⁹ *Id.* at 303.

²⁰ *Id.*

²¹ *Id.* at 304.

²² *Id.*

²³ *Id.*

²⁴ *Id.* at 305.

²⁵ *Id.* at 306.

²⁶ *Id.*

²⁷ *Id.*

²⁸ *Id.* at 307.

²⁹ *Id.*

³⁰ *Id.* at 308.

³¹ *Id.*

³² *Id.*

³³ *Id.*

Any unpaid debt on the student loan would be discharged if the debt was not repaid in full after 20 years.³⁴

Practical Considerations

The court's discharge of the balance of the student loan debt in *Modeen* is dependent upon a 20-year period of repayment. However, what is not clear is how this discharge will be practically enforced or completed.

Can the debtor pre-pay the debt? What happens if a payment is late; can she cure the default? What is the process to certify the completion of the payments after 20 years; will she need to reopen her bankruptcy case and request entry of the discharge, or is it self-executing? What remedy would she have if the student loan lender continues to report the debt to reporting agencies after 20 years? Could the student loan lender request a modified review of the partial discharge after 10 years if the debtor's financial circumstances change, similar to a chapter 13 trustee's motion to modify a plan during the case for increased financial circumstances?

The *Modeen* decision suggests that had the debtor been able to use a federal repayment plan, she would have been denied even a partial discharge. However, the decision does not address the effectiveness of any particular program. The news is full of reports on the difficulties faced by student loan borrowers participating in federal repayment or forgiveness programs. For example, a recent NPR story highlighted the Public Service Loan Forgiveness (PSLF) program, which was promulgated in 2007.³⁵ The requirements appear to be simple:

The PSLF Program was established by Congress with the passage of the College Cost Reduction and Access Act of 2007, and was created to encourage individuals to enter lower-paying but vitally important public-sector jobs such as military service, law enforcement,

public education, and public health professions. The PSLF Program allows eligible borrowers to qualify for forgiveness of the remaining balance of their William D. Ford Federal Direct Loan ... Program loans after they have served full time at a public service organization for at least 10 years, while making 120 qualifying payments.³⁶

According to the NPR article, 99 percent of applicants under the PSLF program who have completed 10 years of public-service employment are denied any relief.³⁷ In many cases, the individuals completed all of the steps and made all 120 monthly payments, but were still denied any form of relief.³⁸ This issue is just now coming to the forefront because the PSLF program was passed in 2007, resulting in the first applications for relief being filed in the past approximately 12 months.

Conclusion

The *Modeen* decision is a recent case that, at first blush, appears to represent a trend toward a more relaxed standard for "undue hardship" under § 523(a)(8). The case might be of limited precedential value because the facts were unique: The debtor did not qualify for any federal student loan repayment program.

The mere existence of a possible repayment plan does not automatically disqualify a debtor from discharge. One court recognized that "[h]olding that eligibility for [an income-based repayment plan] *ipso facto* leads to denial of an undue hardship discharge would deprive the Court of the discretion granted by § 523(a)(8)."³⁹ It remains to be seen whether courts will be critical of programs such as PSLF such that in the future, decisions might become more lenient toward discharge. **abi**

³⁴ *Id.* The court did not articulate whether there would be any payments due between the 154-month mark (12 years and 10 months) and year 20. The court considered a similar payment plan under a particular federal repayment program, under which there was a 15-year repayment and any remaining debt would be forgiven after 25 years. *Id.* at 308.

³⁵ Cory Turner, "Why Public Service Loan Forgiveness Is So Unforgiving," NPR (Oct. 17, 2018), available at npr.org/2018/10/17/653853227/the-student-loan-whistleblower.

³⁶ "Public Service Loan Forgiveness Program," Federal Student Aid (November 2014), available at studentaid.ed.gov/sa/sites/default/files/public-service-loan-forgiveness-employment-certification-borrower-letter.pdf.

³⁷ See Turner, *supra* n.35.

³⁸ *Id.*

³⁹ *Fern v. Fedloan Servicing (In re Fern)*, 553 B.R. 362 (Bankr. N.D. Iowa 2016) (discharging student loans at issue even though debtor was eligible for plan under which debtor would pay \$0 per month, after considering mounting indebtedness due to unpaid interest and emotional burden on debtor).

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Income Driven Repayment Plans*

Borrowers must repay their loans even if they do not complete their education, cannot find a job related to their program of study, or are unhappy with the education they paid for with their loan. However, certain circumstances might lead to their loans being forgiven, canceled, or discharged. The list below is a quick view of the types of forgiveness, cancellation, and discharge.

*The following chart was adopted from: Student Loans: An Overwhelming Problem in Need of Some Solutions presented at 2018 Hon. Steven W. Rhodes Consumer Bankruptcy Conference the with permission from the authors: PAULA HALL and ALEXANDRA STAN; Brooks Wilkins Sharkey & Turco PLLC Birmingham, Michigan.

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Type of Forgiveness, Cancellation or Discharge	Direct Loans	FFEL Program Loans	Perkins Loans
Total and Permanent Disability (TPD) Discharge	x	x	x
Death Discharge	x	x	x
Discharge in Bankruptcy (in rare cases)	x	x	x
Closed School Discharge	x	x	
False Certification of Student Eligibility or Unauthorized Payment Discharge	x	x	
Teacher Loan Forgiveness	x	x	
Public Service Loan Forgiveness	x		
Perkins Loan Cancellation and Discharge (includes Teacher Cancellation)			x

OVERVIEW OF REPAYMENT PLANS

Repayment Plan	Eligible Loans	Monthly Payment and Time Frame	Quick Comparison
Standard Repayment Plan	<ul style="list-style-type: none"> • Direct Subsidized and Unsubsidized Loans • Subsidized and Unsubsidized Federal Stafford Loans • All PLUS loans 	<p>Payments are a fixed amount of at least \$50 per month.</p> <p>Up to 10 years.</p>	<p>You'll pay less interest for your loan over time under this plan than you would under other plans.</p>

Repayment Plan	Eligible Loans	Monthly Payment and Time Frame	Quick Comparison
Extended Repayment Plan	<ul style="list-style-type: none"> • Direct Subsidized and Unsubsidized Loans • Subsidized and Unsubsidized Federal Stafford Loans • All PLUS loans 	<p>Payments may be fixed or graduated.</p> <p>Up to 25 years.</p>	<ul style="list-style-type: none"> • Your monthly payments would be lower than the 10-year standard plan. • If you are a - <ul style="list-style-type: none"> ◦ Direct Loan borrower, you must have more than \$30,000 in outstanding Direct Loans. ◦ FFEL borrower, you must have more than \$30,000 in outstanding FFEL Program loans. ▸ For example, if you have \$35,000 in outstanding FFEL Program Loans, and \$10,000 in Direct Loans, you can use the extended repayment plan for your FFEL Program loans, but not for your Direct Loans. • For both programs, you must also be a new borrower as of October 7, 1998. • You'll pay more for your loan over time than under the 10-year standard plan.
Graduated Repayment Plan	<ul style="list-style-type: none"> • Direct Subsidized and Unsubsidized Loans • Subsidized and Unsubsidized Federal Stafford Loans • All PLUS loans 	<p>Payments are lower at first and then increase, usually every two years.</p> <p>Up to 10 years.</p>	<p>You'll pay more for your loan over time than under the 10-year standard plan.</p>

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Repayment Plan	Eligible Loans	Monthly Payment and Time Frame	Quick Comparison
Income-Contingent Repayment Plan	<ul style="list-style-type: none"> • Direct Subsidized and Unsubsidized Loans • Direct PLUS loans made to students • Direct Consolidation Loans 	<ul style="list-style-type: none"> • Payments are calculated each year and are based on your adjusted gross income, family size, and the total amount of your Direct Loans. • Your payments change as your income changes. • Up to 25 years. 	<ul style="list-style-type: none"> • You'll pay more for your loan over time than you would under the 10-year standard plan. • If you have not repaid your loan in full after making the equivalent of 25 years of qualifying monthly payments, any outstanding balance on your loan will be forgiven. • You may have to pay income tax on any amount that is forgiven.
Income-Based Repayment Plan (IBR)	<ul style="list-style-type: none"> • Direct Subsidized and Unsubsidized Loans • Subsidized and Unsubsidized Federal Stafford Loans • All PLUS loans made to students • Consolidation Loans (Direct or FFEL) that do not include Direct or FFEL PLUS loans made to parents. 	<ul style="list-style-type: none"> • Your maximum monthly payments will be 15 percent of discretionary income, the difference between your adjusted gross income and 150 percent of the poverty guideline for your family size and state of residence (other conditions apply). • Your payments change as your income changes. • Up to 25 years. 	<ul style="list-style-type: none"> • You must have a partial financial hardship. • Your monthly payments will be lower than payments under the 10-year standard plan. • You'll pay more for your loan over time than you would under the 10-year standard plan. • If you have not repaid your loan in full after making the equivalent of 25 years of qualifying monthly payments, any outstanding balance on your loan will be forgiven. • You may have to pay income tax on any amount that is forgiven.
Income-Sensitive Repayment Plan	<ul style="list-style-type: none"> • Subsidized and Unsubsidized Federal Stafford Loans • FFEL PLUS loans • FFEL Consolidation Loans 	<ul style="list-style-type: none"> • Your monthly payment is based on annual income. • Your payments change as your income changes. • Up to 10 years. 	<ul style="list-style-type: none"> • You'll pay more for your loan over time than you would under the 10-year standard plan. • Each lender's formula for determining the monthly payment under this plan can vary.

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Repayment Plan	Eligible Loans	Monthly Payment and Time Frame	Quick Comparison
Pay As You Earn Repayment Plan	<ul style="list-style-type: none"> • Direct Subsidized and Unsubsidized Loans • Direct PLUS loans made to students • Direct Consolidation Loans that do not include (Direct or FFEL) PLUS loans made to parents 	<ul style="list-style-type: none"> • Your maximum monthly payments will be 10 percent of discretionary income, the difference between your adjusted gross income and 150 percent of the poverty guideline for your family size and state of residence (other conditions apply). • Your payments change as your income changes. • Up to 20 years. 	<ul style="list-style-type: none"> • You must be a new borrower on or after October 1, 2007, and must have received a disbursement of a Direct Loan on or after October 1, 2011. • You must have a partial financial hardship. • Your monthly payments will be lower than payments under the 10-year standard plan. • You'll pay more for your loan over time than you would under the 10-year standard plan. • If you have not repaid your loan in full after making the equivalent of 20 years of qualifying monthly payments, any outstanding balance on your loan will be forgiven. • You may have to pay income tax on any amount that is forgiven.

STUDENT LOANIFY

Resolving a \$1.5 trillion student loan crisis is problematic in that the caselaw was developed during a period when the statutory regime allowed for discharge after five and later seven years. Litigation on student loan dischargeability has not been a solution in majority of cases because the “*Bruner*” test is hard to satisfy all three requirements, and litigation costs are beyond the reach of most debtors. Therefore, a new axis of attack is needed and a different mindset of treating student loans in bankruptcy, to better secure debtors a path forward.

This is where Student Loanify presents a possible solution for the federally guaranteed student loan programs, that can benefit the typical debtor.

The first step is to obtain a print out from the NSLDS website of what loans the debtor is responsible for. After entering basic information and uploading the NSLDS print out to Student Loanify, the software provides a list of different repayment options that are offered with federally guaranteed loans. These first few steps are free and at no cost to debtors.

Student Loanify will, for a small fee, fill out the necessary applications to consolidate the student loans and apply for an income-based repayment plan. These income-based repayment plans are based on the debtor’s income; some with zero monthly payments. Depending on the program, at the end of 10 or 25 years, these debts will be satisfied if the debtor maintains the repayment plan and recertifies annually.

The process assists law firms to analyze the client’s options and mail-merge the applications and communicate with the various student loan servicers. The student loan

mail-merge applications help fill a void, as attorneys for the student loan servicers have noted that debtor attorneys are not versed in filling out the necessary applications. It has helped our office with representing debtors in dealing with their federally guaranteed loans. Unfortunately, we are facing the same obstacles we did in the mortgage modification process, where documents and authorizations of representation are sent but servicers claim they were never received. Student Loanify also offers the use of a portal to exchange documents for the cost of \$40.00. The use of a portal will prevent student loan servicers from asking for the same documents multiple times and give recognition to the firm in the representation of the clients.

2016 WL 7011570

Only the Westlaw citation is currently available.
United States Bankruptcy Court,
D. South Carolina.

In re: Dorothy Marie Belton, Debtor(s).

C/A No. 16-03040-JW

Signed 10/13/2016

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ORDER OVERRULING OBJECTION TO
CONFIRMATION

John E. Waites, District Judge

*1 THIS MATTER comes before the Court for a hearing on the Trustee’s Objection to confirmation of the Chapter 13 Plan filed by Dorothy Marie Belton (“Debtor”) on June 29, 2016 (“Plan”). After considering the matters before the Court, including the Debtor’s testimony, the Plan, the parties’ Amended Joint Statement of Dispute, and the applicable code sections and case law, the Court overrules the Trustee’s objection and makes the following findings of fact and conclusions of law:¹

FINDINGS OF FACT

1. The Debtor filed a chapter 13 bankruptcy case *pro se* on June 17, 2016. She thereafter retained counsel, who filed the Plan and other documents on her behalf.

2. The Debtor’s schedules indicate that she is a below median debtor with a current monthly income of \$2,999.81, all of which is presently derived from voluntary family contributions.

3. The Debtor testified that she lives with her husband and adult son. The Debtor’s son contributes \$650 per month and her husband contributes a gross of \$2,740.21 per month. Her schedules I and J show a Disposable Monthly Income (“DMI”) of \$587.51 per month.

4. The Debtor is currently unemployed due to past health issues. However, as she is now medically fit for employment, she has been looking for a job as a paralegal.

5. The Debtor has four (4) long-term federal student loans—one (1) Stafford Loan, serviced by Navient, and three (3) federal student loans serviced by ECMC. Each servicer has filed a proof of claim indicating a balance owed of \$5,312.64 and \$17,435.22, respectively.

6. The Debtor has \$0 in nonexempt equity, so in a hypothetical liquidation there would be no distribution to any unsecured creditors.

7. The Plan provides for a monthly trustee payment of \$575 for the maximum term of sixty (60) months.

8. The Plan provides for separate classification of each of the Debtor’s student loans. Specifically, the Plan proposes to pay the Navient loan, which the Debtor believes is not in default and in deferment, by applying for enrollment in “any applicable income-driven or income-based repayment” program.² The Plan proposes to pay the ECMC serviced loans, which are long-term, unsecured loans and in default, by using the provisions of 11 U.S.C. § 1322(b)(3) and/or (5) to cure her default.³

*2 9. Other unsecured creditors are treated in section IV(E) of the Plan:

E. General Unsecured Creditors: General unsecured creditors shall be paid allowed claims *pro rata* by the trustee to the extent that funds are available after payment of all other allowed claims. The debtor **does not** propose to pay 100% of general unsecured claims.

(emphasis original).

10. The Plan also provides for payment of the Debtor's two secured creditors, and the Debtor's attorney fees in this case.

11. The Plan was properly served on all creditors and parties in interest.

12. On July 18, 2016, the Trustee filed his Objection, contending the Plan's proposed treatment of the defaulted student loan debt unfairly discriminated against the unsecured creditors who are not to be paid in full and therefore the Plan is not proposed in good faith. At the confirmation hearing, the Trustee represented that the Plan was otherwise confirmable.

13. No creditor (including any general unsecured creditor or student loan creditor or servicer) filed an objection to the Plan.

14. At the confirmation hearing, the Debtor testified that she is a paralegal by training and trade, having worked in this field for approximately twenty years. She was forced to quit her job and take medical leave in August 2015 due to a health issue. The Debtor has since been released from medical care and is free to resume employment.

15. The Debtor incurred the majority of her student loans while enrolled at Midlands Technical College's paralegal program.

16. The Debtor has been looking for a job in her field in both the private and public sector (state and federal agencies), as either a paralegal or administrative assistant, but has thus far been unsuccessful in her search efforts. She attributes this lack of success to her defaulted student loans—which she understands disqualifies her from many positions that involve the handling of money. She believes that the filing of her Chapter 13 case and confirmation of the Plan will help with her job prospects as it will allow the cure of her default under her student loans.

17. The Debtor presently has no income and is relying on contributions from her husband and adult son to make payments under the Plan. The family's motivation for making contributions to the Debtor to fund the Plan appears to be primarily to assist the Debtor's desire to cure her default under the student loans and improve her employment opportunities.

18. The Debtor and her husband fell behind on their payments to their creditors when the Debtor fell ill. Because of her unemployment and the family's financial issues, the Debtor and her family have cut back on their

household budget.

19. The Debtor's husband, who has not filed bankruptcy, is a co-debtor on one of her secured loans and on her tax debt owed to Fairfield County, but is not a co-debtor on any of the student loans. The husband is solely responsible for the debt on the parties' residence (which is in default) and he is attempting to obtain a loan modification with his mortgage lender.

20. The parties advised the Court that if confirmed, the Plan as currently filed would provide for an 11.3% distribution to the general unsecured creditors class (IV(E) of the Plan). If all of the general unsecured creditors, including all student loan debts, were put in one class and the Debtor's family maintained their contributions to the Debtor, the distribution to all general unsecured creditors would be 42.8%. If all of the general unsecured creditors were put into one class and the Debtor received no contributions from her family, the distribution to general unsecured creditors would be 2% in a 36 month plan, and 3% in a 60 month plan.⁴ If the Debtor filed a Chapter 7 case, it appears that the general unsecured creditors would receive no payment or dividend.

ISSUE

*3 Does the Debtor's separate classification of unsecured student loan debts in order to cure the default unfairly discriminate against the general unsecured creditor class so as to warrant denial of confirmation?⁵

CONCLUSIONS OF LAW

Unlike subsection (a) of 11 U.S.C. § 1322,⁶ which sets forth what a plan "shall" contain, subsection (b) contains a list of eleven (11) provisions that a plan may contain. Section 1322(b)(3) of the Code provides that a chapter 13 plan may, "provide for the curing or waiving of any default." While this subsection is usually used by debtors as a means to cure or waive defaults in short-term, secured debts, the power to use (b)(3) to cure or waive a default is not limited to any particular kind or term of debt. Keith M. Lundin & William H. Brown, *Chapter 13 Bankruptcy*, § 171.1, at ¶ 14 (4th Edition, 2d Rev. June

17, 2004).

Although normally used in the context of addressing long-term mortgage debt, the Code explicitly contemplates the Debtor's use of § 1322(b)(5) to resolve defaults in long-term unsecured debt. Specifically, this section provides that a plan may:

provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim ... on which the last payment is due after the date on which the final payment under the plan is due.

11 U.S.C. § 1322(b)(5). A number of jurisdictions routinely approve plans that provide for “cure and maintain” treatment for student loan debt. *See, e.g., In re Carrillo*, 421 B.R. 540, 545 (Bankr. D. Ariz. 2009) (noting that debtors are permitted to maintain regular student loan payments as part of a Chapter 13 plan); *In re Pageau*, 383 B.R. 221, 229 (Bankr. D.N.H. 2008) (“In this district, student loan debts may be paid directly and separately during a debtor’s chapter 13 plan in accordance with § 1322(b)(5) as long as payments are to maintain and keep current long-term student loan debt, i.e., loans that mature after plan completion, with no acceleration of [payments on] that debt.”); *In re Delbecq*, 368 B.R. 754, 759 and n.8 (Bankr. S.D. Ind. 2007) (“In this jurisdiction, the Court has historically allowed debtors to classify separately student loan indebtedness pursuant to 11 U.S.C. § 1322(b)(5).”); *In re Machado*, 378 B.R. 14, 16 (Bankr. D. Mass. 2007) (“It is clear the debtor may employ cure and maintain treatment under Section 1322(b)(5) for her student loan debt given the occurrence of prepetition defaults and original loan maturity dates after the final Plan payment date.”).

While it appears clear that a debtor may use subsection (b)(3) or (b)(5) to separately classify student loan debt for purposes of curing a default, in some courts there is a question whether, if a plan separately classifies the debt for purposes of curing a default, the unfair discrimination prohibition of § 1322(b)(1) would apply. Subsection (b)(1) provides in relevant part that a plan may:

*4 designate a class or classes of unsecured claims, as provided in section 1122 of this title, but may not discriminate unfairly against any class so designated

11 U.S.C. § 1322(b)(1). The case law on the use of § 1322(b)(3) in this context is scarce, and there appears to be little or no discussion of the interplay between § 1322(b)(1) and (b)(3). *See* Lundin, *supra*. In contrast, there is a split of authority on the issue of whether a debtor who utilizes subsection (b)(5) to separately treat long-term unsecured debt is also required to comply with the anti-discrimination provisions of § 1322(b)(1).

A minority of Courts addressing this issue have ruled that a debtor’s use of subsection (b)(5) to deal with long-term unsecured debt supersedes the provisions of subsection (b)(1). *See, e.g., In re Truss*, 404 B.R. 329, 332 (Bankr. E.D. Wis. 2009) (“Because section 1322(b)(5) is specific and clear in its language, statutory construction principles dictated that it trump the more general terms of section 1322(b)(1). In other words, if the provisions of section 1322(b)(5) for the cure of arrearages and maintenance of regular payments on long-term student loan indebtedness apply, then the specific provisions of section 1322(b)(5) supercede [sic] the general unfair discrimination provisions of section 1322(b)(1).”); *In re Williams*, 253 B.R. 220, 227 (Bankr. W.D. Tenn. 2000) (inclusion of unsecured creditors in (b)(5) indicates that it is a type of discrimination that is expressly contemplated and sanctioned by the Code); *In re Hanson*, 310 B.R. 131, 134 (Bankr. W.D. Wis. 2004) (specific statutory provision of § 1322(b)(5) trumps the general provisions of (b)(1)); *In re Johnson*, 446 B.R. 921, 925 (Bankr. E.D. Wis. 2011) (citing with favor *Truss* analysis, *supra*).⁷

In contrast, a majority of courts hold that each part of § 1322(b) must be harmonized with the others; therefore, a debtor who proposes to separately classify long-term student loan debt using § 1322(b)(5) must also satisfy subsection (b)(1) and prove to the court’s satisfaction that the separate classification does not unfairly discriminate. *See, e.g., In re Brown*, 500 B.R. 255, 265 (Bankr. S.D. Ga. 2013) (separate student loan classification must undergo unfair discrimination analysis); *In re Pracht*, 464 B.R. 486, 490 (Bankr. M.D. Ga. 2012) (subsection (b)(5) does not “trump” subsection (b)(1)); *In re Harding*, 423 B.R. 568, 571 (Bankr. S.D. Fla. 2010) (subsection (b)(5) cannot be read in isolation); *In re Edmonds*, 444 B.R. 898, 900 (Bankr. E.D. Wi. 2010) (same); *In re Webb*, 370 B.R. 418, 423 (Bankr. N.D. Ga. 2007) (without declaring the majority position correct, court finds it appropriate to

make a determination of whether the proposed plan unfairly discriminated); *In re Simmons*, 288 B.R. 737, 743 (Bankr. N.D. Tex. 2003) (code does not contain an exception to § 1322(b)(1), which must be considered when evaluating treatment of a debt under (b)(5)); *In re Chandler*, 210 B.R. 898, 904 (Bankr. D.N.H. 1997) (separate classifications under § 1322(b)(5) are subject to unfair discrimination prohibition of § 1322(b)(1)); *In re Counce*, 213 B.R. 344, 347 (Bankr. S.D. Ill. 1997) (same).

*5 To address this split, and in consideration of the Trustee's objection, the Court must therefore analyze the general requirements of § 1322(b)(1).

On the specific issue of discrimination, a debtor who has proposed a separate classification has the burden of proving by a preponderance of the evidence that the separate classification does not unfairly discriminate. *In re Moore*, 31 B.R. 12, 16 (Bankr. D.S.C. 1983); *In re Prachet*, 464 B.R. at 489; *In re Kalfayan*, 415 B.R. 907, 909 (Bankr. S.D. Fla. 2009). "A debtor must be able to articulate a reason why the discriminatory treatment is being proposed, and be able to demonstrate that a lesser discriminatory means of treatment is not advisable." *In re Mason*, 456 B.R. 245, 252 (Bankr. N.D. W. Va. 2011).

The Code does not define either the term "discriminate"⁸ or the phrase "unfairly discriminate." As recognized by numerous courts, § 1322(b)(1) does not prohibit all discrimination—only "unfair" discrimination is barred. See *Bentley v. Boyajian (In re Bentley)*, 266 B.R. 229, 232 (1st Cir. B.A.P. 2001) ("Because § 1322(b)(1) distinguishes between discrimination that is unfair and discrimination that is not, we understand 'discriminate' to have no pejorative connotation here"); *In re Moore*, 31 B.R. at 17 ("What constitutes fair discrimination will vary from case to case, and we cannot offer a generally applicable definition. The court must examine the amounts proposed for each class in light of the debtor's reasons for classification, and exercise sound discretion."); *In re Cook*, 26 B.R. 187, 190 (D.N.M. 1982) ("A classification is not *ipso facto* unfairly discriminatory because it provides for a greater percentage of payment to some unsecured creditors than to others."). Indeed, discriminatory treatment that is not unfair is not prohibited. See, e.g., *In re Leser*, 939 F.2d 669, 672 (8th Cir. 1991) (importantly, not all discrimination among classes of claims is prohibited, it is only unfair discrimination that is impermissible); *Bentley v. Boyajian*, 266 B.R. at 237 ("Section 1322(b)(1) prohibits only such discrimination as is unfair to any class of unsecured claims and, conversely, sanctions such differences in treatment as are fair."); *In re Kalfayan*, 415 B.R. at 911 (subsection (b)(1) may be satisfied if the debtor can show

that creditors are benefitted by the discrimination); *In re Chandler*, 210 B.R. at 904 (the inclusion of long term unsecured debt in § 1322(b)(5) evidences congressional intent to allow for different treatment of long term unsecured debt).

*6 Historically in this district, the Court has utilized a five (5) factor test to determine whether a plan's classification is unfairly discriminatory:

- (1) Whether there is a reasonable basis for the classification;
- (2) Whether the classification is necessary to the debtor's rehabilitation under Chapter 13;
- (3) Whether the discriminatory classification is proposed in good faith;
- (4) Whether there is a meaningful payment to the class discriminated against; and
- (5) The difference between what the creditors discriminated against will receive as the plan is proposed, and the amount they would receive if there was no separate classification.

In re Moore, 31 B.R. at 17 (internal citations omitted); *In re Girardeau*, 35 B.R. 9 (Bankr. D.S.C. 1983);⁹ *In re Wallace*, Case No. 95-70780-JBD, slip op. (Bankr. D.S.C. June 22, 1995); *In re Wilmon*, Case No. 92-71900-WTB, slip op. (Bankr. D.S.C. 1992). This test is an example of the various multi-factor tests employed by other courts in this Circuit and across the country. See, e.g., *In re Leser*, 939 F.2d 669 (8th Cir. 1991); *In re Birts*, 2012 WL 3150384 (D. E.D. Va. 2012); *In re Linton*, 2011 WL 3207366, at *2 (Bankr. E.D. Va. July 27, 2011); *In re Kolbe*, 199 B.R. 569 (Bankr. D. Md. 1996); *In re Delauder*, 189 B.R. 639 (Bankr. E.D. Va. 1995); *In re Husted*, 142 B.R. 72 (Bankr. W.D.N.Y. 1992). But see *In re Mason*, 456 B.R. 245, 251 (Bankr. N.D. W. Va. 2011) (each plan should be adopted on a case by case basis in light of the twin aims of the code—providing the debtor with a fresh start and providing a mechanism for the collection of debts); *In re Lawson*, 93 B.R. 979, 984 (Bankr. N.D. Ill. 1988) (shunning a four-part test and determining that standard should be that a discriminatory treatment is fair and therefore permissible to the extent and only to the extent that it rationally furthers an articulated, legitimate interest of the debtor); *In re Hamilton*, 102 B.R. 498 (Bankr. W.D. W. Va. 1988) (adopting *Lawson* test); *In re McCullough*, 162 B.R. 506 (Bankr. N.D. Ill. 1993) (applying a balancing test).

Despite a desire for a bright line test, even in those courts

that employ a more formulistic approach, ultimately the analysis in each case is fact intensive. *In re Crawford*, 324 F.3d 539, 543-43 (7th Cir. 2003) (After failing in its efforts to identify a satisfactory bright line test, the court counseled “if without classification the debtor is unlikely to be able to fulfill the Chapter 13 plan and the result will be to make his creditors as a whole worse off than they would be with classification, then classification will be a win-win outcome.”); *In re Groves*, 39 F.3d 212, 214 (8th Cir. 1994) (recognizing that the application of the “discriminate unfairly” standard may “involve little more than exercise of the bankruptcy court’s broad discretion”); *In re Pracht*, 464 B.R. 486, 491 (Bankr. M.D. Ga. 2012) (recognizing that “the inevitable consequence of any multi-factored test ... is that it devolves into a ‘totality of the circumstances’ or ‘case-by-case’ analysis, thereby running the risk of being depicted as an *ad hoc*, potentially purely subjective determination”).

*7 In this case, as a result of the separate classification for the purpose of curing a default, the Debtor is proposing to pay the separately classed student loan creditors more than what is being paid to other unsecured creditors. “By its very nature, this treatment is discriminatory; however, just because treatment is discriminatory does not mean that it is unfairly discriminatory.” *In re Mason*, 456 B.R. at 249–50. The critical issue under § 1322(b)(1) is not merely the difference in payment amount, but the reason for the difference in treatment.¹⁰

While the undersigned is unwilling to abandon the framework established by my predecessors on the Court, it appears that factor five, the difference in payment percentage, has been unduly emphasized in prior cases. Therefore, in my view, the following streamlined test better reflects the balance of factors pursuant to which a debtor must submit evidence to enable the Court to analyze the separate classification of unsecured debt:

- (1) Is there a good faith, rational basis for the separate classification;
- (2) Is the separate classification necessary to the debtor’s rehabilitation under Chapter 13; and
- (3) Is there a meaningful payment to the discriminated class.¹¹

Applying this test to the facts before the Court, the Court finds that the Plan’s separate classification of the Debtor’s student loans is permissible and that the proposed classification does not unfairly discriminate.

1. There is a good faith, rational basis for the proposed classification.

The evidence before the Court is that there is a good faith, rational basis for the proposed classification, with the reason being to cure the student loan default and to improve the Debtor’s prospects for reemployment as a paralegal. The Debtor’s uncontroverted testimony was that despite her twenty-year career as a paralegal, she has not been employed since August 2015 and that, while her initial job loss was health related, her efforts to obtain new employment as a paralegal have been stymied by the default status of her student loans. The Debtor testified that she cannot obtain either a state or federal job as a paralegal or administrative assistant while her student loans are in default because as a paralegal, this default status is perceived by employers to impact her reliability in the handling of funds.

Additionally, while the Debtor is currently unemployed with no income from wages with which to make payments to creditors, the Debtor, through her family’s voluntary contribution, has proposed the Plan to enable the Debtor to pay a dividend to all creditors with a primary goal of curing the default in her student loans.¹² The Debtor has committed to 60 monthly payments of \$575. This, in and of itself, is notable because as a below median debtor, the Debtor is only required to file a 36 month plan. 11 U.S.C. § 1322(d)(2). The voluntary commitment to submit herself to 24 additional months of payments is evidence of the Debtor’s good faith. The Debtor could convert this case to chapter 7, discharge the general unsecured debt, and then file a new chapter 13.¹³ Under such a “chapter 20” procedure, the Debtor could reorganize her student loan debt and pay nothing to the other (then discharged) unsecured creditors. Instead, the Debtor has chosen to propose the Plan which provides for better treatment of both her student loan debt and her general unsecured debt.

2. The separate classification is necessary to the Debtor’s rehabilitation.

*8 The evidence indicates that a continuation of the default status on the Debtor’s student loans impairs her ability to regain employment and meet her and her family’s financial needs. The rehabilitation proposed in the Plan would enable her to both cure her default in her student loans and enable her to address her debts for which her non-filing spouse is a co-debtor. Merely filing Chapter 7 will not resolve the Debtor’s current difficulties with her student loan creditors and may limit her family’s ability to retain essential secured property.

3. There is a meaningful payment to the class discriminated against.

It is undisputed that under the Plan, the separately classed general unsecured creditors will receive 11.3%. This is a meaningful distribution, and more than general unsecured creditors would receive either in a Chapter 7 liquidation case or in many of the typical Chapter 13 cases filed in this district. Although the Trustee has indicated that if the separate classification were eliminated, general unsecured creditors would receive 42.8%, this calculation does not take into consideration the fact that if the Plan is not confirmed, the assistance from the Debtor’s family will likely be withdrawn. Without the family’s contribution, the combined class of general unsecured creditors would receive only 2% over 36 months.

Although the Plan does not propose to pay the separately classed general unsecured creditors the same dollar amount as the student loan creditors, it is clear that the Plan is paying all general unsecured creditors more and in a better manner than they would receive if the Plan were not confirmed. The financial differential resulting from the separate classification and treatment is not excessive, and the benefit to the general unsecured creditors is meaningful.

Based on the facts presented, the Court finds that the discrimination caused by the separate classification of student loans proposed by the Debtor is not unfair and is proposed in good faith. The Plan uses the funds contributed to the Debtor by her family to fund 100% of the Plan, to remedy the student loan default so she can apply for state and federal jobs in her field, and to provide creditors with more than they would receive in a hypothetical chapter 7 case or a chapter 13 case without her family’s contribution. The proposed Plan promotes the policy of paying student loans and curing student loan default so the Debtor can achieve a fresh start and her goals of reorganization, of obtaining employment, and of paying her creditors to the best of her ability.

THEREFORE, this Court holds the plan does not unfairly discriminate and meets the requirements of § 1322. The Trustee’s objection is overruled.¹⁴ The Plan shall be confirmed by separate order.¹⁵

*9 Finally, according to the undersigned’s Chambers Guidelines, inasmuch as Counsel has expended additional time and effort to represent the Debtor in this contested matter, Counsel is hereby awarded an additional \$1,500 in attorney’s fees to be paid through the Debtor’s plan by the Trustee or directly by the Debtor.

AND IT IS SO ORDERED.

All Citations

Slip Copy, 2016 WL 7011570

CONCLUSION

Footnotes

- 1 To the extent any of the following findings of fact constitute conclusions of law they are adopted as such, and to the extent any of the following conclusions of law constitute findings of fact, they are so adopted.
- 2 The relevant Plan provision is as follows:
F. Student Loans—Debtor shall be allowed to seek enrollment in any applicable income-driven or income-based repayment (known commonly as “IDR” plan with the U.S. Department of Education and/or other student loan servicers, guarantors, etc. or public service loan forgiveness programs (sometimes referred to as “PSLF”) (with such servicer or agency referred to hereafter as “Ed”), without disqualification due to bankruptcy. Ed shall not be required to allow enrollment in any repayment or forgiveness program unless the Debtor otherwise qualifies for such plan. Debtor may, if necessary and desired, seek a consolidation of her student loans by separate motion and subject to subsequent court order. Upon determination by Ed of qualification for enrollment in an IDR and calculation of any payment required under such by the Debtor, the Debtor shall, within 30 days, notify the Chapter 13 Trustee of the amount o f such payment. At such time, the Trustee or the Debtor may, if necessary, file a Motion to Modify the Chapter 13 Plan to allow such direct payment o f the student loan(s) and adjust the payment to other general unsecured claims as necessary to avoid any unfair discrimination. Debtor shall re-enroll in the applicable program annually or as otherwise required and shall, within 30 days following a determination of her updated

payment, notify the Chapter 13 Trustee of such payment. At such time, the Trustee or the Debtor may, if necessary, file a Motion to Modify the Chapter 13 plan to allow such direct payment of the student loan(s) and adjust the payment to other general unsecured claims as necessary to avoid any unfair discrimination. During the pendency of any application by the Debtor to consolidate student loans, to enroll in an IDR or related program, direct payment of student loans under an IDR or similar program, or during the pendency of any default in payments of the student loans under an IDR or other program, it shall not be a violation of the stay or other State or Federal Laws for Ed to send Debtor normal monthly statements regarding payments due and any other communications including, without limitation, notices of late payments or delinquency. These communications may expressly include telephone calls and e-mails. Debtor's attorney may seek additional compensation by separate applications and court order for services provided in connection with the enrollment and performance under an IDR or PSLF.

3 Specifically, the Plan provides:

[Am Std Asst] Arrearage payments. The trustee shall pay the arrearage as stated in the creditors allowed claim or as otherwise ordered by the Court to **Am Std Asst (student loan)** at the rate of **\$120.00** or more per month, for **student loan ending in 9957**, along with **0%** interest. The creditor shall apply trustee payments solely to those designated arrearages, i.e., those arrearages accruing before the month specified in (b.) below. For so long as the debtor complies with this plan, a creditor may not declare a default based on any payment delinquency to be cured by this paragraph and the creditor shall not impose any post-petition fee on account of any arrearage paid by the trustee.

Maintenance of regular non-arrearage payments. Beginning **n/a—loan is fully in arrears**, the Debtor shall pay directly to the creditor non-arrearage payments arising under the agreement with the secured creditor. The creditor shall apply each payment under this paragraph solely to post-petition obligations that accrue during or after the month specified herein.

[US Dept. Ed] Arrearage payments. The trustee shall pay the arrearage as stated in the creditors allowed claim or as otherwise ordered by the Court to **US Dept. of Ed (student loan xxx7056)** at the rate of **\$99.00** or more per month, for **student loan ending in 7056**, along with **0%** interest. The creditor shall apply trustee payments solely to those designated arrearages, i.e., those arrearages accruing before the month specified in (b.) below. For so long as the debtor complies with this plan, a creditor may not declare a default based on any payment delinquency to be cured by this paragraph and the creditor shall not impose any post-petition fee on account of any arrearage paid by the trustee.

Maintenance of regular non-arrearage payments. Beginning **n/a—loan is fully in arrears**, the Debtor shall pay directly to the creditor non-arrearage payments arising under the agreement with the secured creditor. The creditor shall apply each payment under this paragraph solely to post-petition obligations that accrue during or after the month specified herein.

[US Dept. Ed] Arrearage payments. The trustee shall pay the arrearage as stated in the creditors allowed claim or as otherwise ordered by the Court to **US Dept. of Ed (student loan xxx7059)** at the rate of **\$35.00** or more per month, for **student loan ending in 7059**, along with **0%** interest. The creditor shall apply trustee payments solely to those designated arrearages, i.e., those arrearages accruing before the month specified in (b.) below. For so long as the debtor complies with this plan, a creditor may not declare a default based on any payment delinquency to be cured by this paragraph and the creditor shall not impose any post-petition fee on account of any arrearage paid by the trustee.

Maintenance of regular non-arrearage payments. Beginning **n/a—loan is fully in arrears**, the Debtor shall pay directly to the creditor non-arrearage payments arising under the agreement with the secured creditor. The creditor shall apply each payment under this paragraph solely to post-petition obligations that accrue during or after the month specified herein.

4 Because she is below-median, the Debtor is only required to propose a 36 month plan. See 11 U.S.C. § 1322(d)(2).

5 It does not appear from his objection that the Trustee is asserting that the Plan's proposed classification and treatment of the Navient student loan debt (submission of an IDR plan and, upon qualification, direct payment) is unfairly discriminatory. See *infra* n.14.

6 Hereinafter, all references to provisions under the United States Bankruptcy Code, 11 U.S.C. §§ 101, et seq., shall be by section number only.

7 As recognized by the *Johnson* court, "A literal interpretation of both subsections [(b)(1) and (5)] leads to a mathematical impossibility for a vast majority of Chapter 13 debtors who cannot afford to pay unsecured claims in full, because the payment in full to long-term debts appears to discriminate against other unsecured creditors who may be paid less than 100%." *Johnson*, 446 B.R. at 925.

8 As explained by one court:

"To discriminate," in its broadest sense, is to make a distinction or to note a difference between two things. Derivatively, it is

to treat two things differently on account of a distinction between them. Accordingly, in § 1322(b)(1), to discriminate is simply to treat two classes differently on the basis of a difference between them; the difference in treatment need not be unfair, wrongful, or even adverse to a class in order to constitute discrimination within the meaning of this statute. The treatment need only be different.

Bentley v. Boyajian (In re Bentley), 266 B.R. 229, 237 (1st Cir. B.A.P. 2001) (internal citations omitted).

- 9 Both *Moore* and *Girardeau* were decided in 1983 and involved a debtor's attempt to use § 1322(b)(5) to separately classify consumer debts that were co-signed by a non-filing co-debtor. In the years following these rulings, the Bankruptcy Code has been overhauled and amended several times. Among the amendments that have occurred is the inclusion of language in § 1322(b)(1) that expressly permits the separate classification denied by the *Moore* and *Girardeau* courts. 11 U.S.C. § 1322(b)(1) ("the plan may ... designate a class ... of unsecured claims ... but may not discriminate unfairly against any class so designated; **however, such plan may treat claims for a consumer debt of the debtor if an individual is liable on such consumer debt with the debtor differently than other unsecured claims**") (emphasis added).
- 10 To the extent that *Moore* and its progeny could be interpreted to say that a classification that merely results in a payment of a higher percentage to the separately classified debt (in this case a student loan debt) is a *per se* violation of § 1322(b)(1) that precludes confirmation of a plan, I disagree.
- 11 Helpful, but not controlling to this analysis, is evidence indicating whether the proposed distribution is greater than would be received by the unsecured creditors in a Chapter 7 liquidation, and the degree of difference in distributions between a plan containing separate classifications and one without.
- 12 The family's voluntary contribution appears to be the equivalent of excess disposable income. Because she is below median, the Debtor does not have to offer all of her projected disposable income into the plan for the benefit of unsecured creditors. See *In re Abaunza*, 452 B.R. 866, 876 (Bankr. S.D. Fla. 2011) (recognizing that paying student loans with discretionary funds did not unfairly discriminate).
- 13 This is commonly termed a "chapter 20."
- 14 It does not appear from his objection that the Trustee is asserting that the Plan's proposed classification and treatment of the Navient student loan debt (submission of an IDR plan and, upon qualification, direct payment) is unfairly discriminatory. However, to the extent that the Trustee has such an objection, the Court overrules it, adopting the reasoning of *In re Knowles*, 501 B.R. 409 (Bankr. D. Kan. 2013) as it relates to the permissibility of a debtor's use of assets not required by the Code to be contributed to the plan, towards direct payment of student loans. *Id.* at 417-418. With its proposal to restructure the Navient debt to a more affordable level through the use of an IDR plan, and with payments under the approved IDR plan to be made from the "discretionary income" provided by the Debtor's family members, the proposed treatment of Navient does not unfairly discriminate against other general unsecured creditors.
- 15 Inasmuch as the requirements of § 1322(b)(1) are met in this case, the Court does not need to determine the issue of whether use of § 1322(b)(3) and/or (5) also requires compliance with the requirements of § 1322(b)(1). Additionally, it appears from the Plan that the Debtor does not propose to pay interest to the separately classified student loan creditors, and § 1322(b)(10) was not raised as a ground for objection; therefore subsection (b)(10) does not need to be addressed.

580 B.R. 443
United States Bankruptcy Court, D. South Carolina.

IN RE, Jeffery Richard KINDLE and Aislinn
Sabrina Kindle, Debtors.

Case No. 17-01245-dd
|
Signed 11/01/2017

Synopsis

Background: Trustee objected to confirmation of debtors’ proposed Chapter 13 plan, under which debtors would continue making their regular monthly payments on their student loan debt outside plan.

Holdings: The Bankruptcy Court, David R. Duncan, Chief Judge, held that:

[1] no adjustments to above-median-income Chapter 13 debtors’ “means” test “disposable income” were necessary, in calculating the “projected disposable income” that debtors would have to devote to payment of unsecured creditors under plan, and

[2] debtors’ proposed cure-and-maintenance plan, under which debtors’ proposed to continue making their regular monthly student loan payments outside the plan, which would result in the student loan creditors receiving a 44.51% distribution on their claims while general unsecured creditors received only a 33% distribution under plan, did not discriminate unfairly.

Objection overruled; plan confirmed.

West Headnotes (8)

- [1] **Bankruptcy**
 - ☛ Protection Against Discrimination or Collection Efforts in General; "Fresh Start."
 - Bankruptcy**
 - ☛ Distribution

Twin aims of bankruptcy are to provide an equitable distribution of assets for creditors, and

to provide a fresh start for debtor.

[Cases that cite this headnote](#)

- [2] **Bankruptcy**
 - ☛ Distribution

Bankruptcy concept of equitable distribution of assets does not mean all creditors must receive an equal distribution, but merely that there must be an equal distribution with respect to similarly situated creditors.

[Cases that cite this headnote](#)

- [3] **Bankruptcy**
 - ☛ Classification and discrimination

Any separate classification of claims in Chapter 13 plan is “discrimination”; however, such discrimination may be permissible, unless it is unfair. 11 U.S.C.A. § 1322(b)(1).

[1 Cases that cite this headnote](#)

- [4] **Bankruptcy**
 - ☛ Claims and assets; propriety and feasibility in general

For an above-median-income Chapter 13 debtor, debtor’s “means” test “disposable income” is the starting point for determining the “projected disposable income” that debtor must devote to payment of unsecured creditors under the plan, to which adjustments should be made only to account for those changes to debtor’s income or expenses that are very likely or certain to occur. 11 U.S.C.A. § 1325(b)(1)(B), (b)(3).

[Cases that cite this headnote](#)

^{15]} **Bankruptcy**
 📌 Claims and assets; propriety and feasibility in general

No adjustments to above-median-income Chapter 13 debtors’ “means” test “disposable income” were necessary, in calculating the “projected disposable income” that debtors would have to devote to payment of unsecured creditors in order to obtain confirmation of plan that provided for less than a 100% distribution on creditor claims over objection of trustee or unsecured creditor, where trustee presented no evidence indicating that changes to debtors’ income or expenses were likely to occur, and where student loan payments to which trustee objected, to extent made outside plan, were payments that debtors had been making for at least six months prior to their bankruptcy filing. 11 U.S.C.A. § 1325(b)(1)(B), (b)(3).

[Cases that cite this headnote](#)

^{16]} **Bankruptcy**
 📌 Classification and discrimination

To determine whether a proposed Chapter 13 plan is unconfirmable, as “unfairly discriminating” against or in favor of class of creditors, courts must consider the totality of the circumstances in each case. 11 U.S.C.A. § 1322(b)(1).

[1 Cases that cite this headnote](#)

^{17]} **Bankruptcy**
 📌 Classification and discrimination
Bankruptcy
 📌 Payments outside plan

Above-median-income Chapter 13 debtors’ proposed cure-and-maintenance plan, under which debtors’ proposed to continue making their regular monthly student loan payments outside the plan, which would result in the

student loan creditors receiving a 44.51% distribution on their claims while general unsecured creditors received only a 33% distribution under plan, did not discriminate unfairly against general unsecured creditors and in favor of student loan creditors, so as to prevent court from confirming proposed plan, where this 33% distribution to unsecured creditors was in excess of distribution to which they were entitled based on debtors’ projected disposable income, and where allowing debtors to continue making regular student loan payments outside plan would minimize accrual of interest on debtors’ student loan debt and facilitate debtors’ fresh start. 11 U.S.C.A. § 1322(b)(1).

[1 Cases that cite this headnote](#)

^{18]} **Bankruptcy**
 📌 Payments outside plan

Bankruptcy court could confirm Chapter 13 plan that provided for debtors to continue making their regular monthly payments on their student loan debt outside plan, despite difficulties of monitoring whether student loan payments were actually being made, where debtors indicated that their certificate of completion of all plan payments would include certification of their having made payments to student loan creditors, and that trustee, if necessary, could seek verification of student loan payments at that time.

[Cases that cite this headnote](#)

Attorneys and Law Firms

*444 [Lex Rogerson, Jr.](#), Lexington, SC, for Debtors.

ORDER CONFIRMING CHAPTER 13 PLAN

David R. Duncan, Chief US Bankruptcy Judge

This matter is before the Court to consider confirmation of a chapter 13 plan filed by debtors Jeffery Richard Kindle and Aislinn Sabrina Kindle (“Debtors”) on July 26, 2017 [Docket No. 21]. Pamela Simmons–Beasley, the chapter 13 trustee (“Trustee”), objected to confirmation of Debtors’ plan [Docket No. 17].¹ A hearing was held on September 18, 2017. At the conclusion of the hearing, the Court took the matter under advisement and gave the parties an additional ten (10) days to submit supplemental briefs. Both parties submitted briefs on September 28, 2017 [Docket Nos. 32, 33]. The Court now issues this order.

FACTS

1. Debtors filed their chapter 13 case on March 14, 2017 and filed their schedules on the same date.

2. Their Schedule F lists student loans owed to Navient in the total amount of \$64,249.05. Navient filed proofs of claim for both Debtors’ student loans, reflecting that Mrs. Kindle owes a total of \$19,574.01, and Mr. Kindle owes a total of \$44,622.19, for a total amount owed of \$64,196.20. Mr. Kindle’s student loans were consolidated in 2002, and Mrs. Kindle’s loans were consolidated in 2013. The proofs of claim filed by *445 Navient reflect that Debtors made payments on both consolidated student loans for at least the six months preceding their bankruptcy filing. Interest totaling approximately \$200.00 per month accrues on the student loans. The last payment on the student loans is due after the date of Debtors’ proposed final plan payment.

3. Mr. Kindle testified that his student loans are not eligible for deferment, but that Mrs. Kindle’s are. However, Mr. Kindle testified that Debtors had not attempted to defer her student loan payments because interest would continue to accrue on the loans while they were in deferment. Mr. Kindle further testified that deferring the student loans would not have an effect on his employment or on Debtors’ lifestyle or financial circumstances.

4. Debtors enjoy income above the South Carolina median. Debtors’ initial Form 122C, the means test form,

filed on March 14, 2017, showed monthly disposable income of \$855.09. Debtors filed an amended means test form on August 28, 2017, showing monthly disposable income of \$830.09. There is no contention that the form is not correctly completed. There is no liquidation value that must be paid to creditors.

5. Debtors’ Schedule I and J list combined monthly income of \$6,408.08 and monthly expenses of \$5,430.92, leaving Debtors with \$977.16 per month. Listed as an expense on Schedule J is a student loan payment in the amount of \$476.21.

6. Debtors have three children, ages 13, 16, and 18. Mrs. Kindle does not work outside the home; however, Debtors’ Schedule I indicates that she is considering seeking part-time at-home employment. At the time of the hearing, Mrs. Kindle had not located any employment, and Mr. Kindle testified that it did not appear she would be likely to obtain employment in the near future due to ongoing medical issues.

7. Mr. Kindle testified that Debtors did not anticipate any significant changes to their income or expenses in the next few years.

8. Debtors owe general unsecured claims in addition to their student loans in the amount of \$90,097.69.

9. Debtors’ July 26 plan proposes total trustee payments of \$900.00 per month for 5 months, followed by payments of \$975.00 per month for 55 months. Debtors’ July 26 plan also proposes that Debtors will continue to directly pay the student loans, making payments of \$476.21 per month. Over the course of the 60-month plan, this will result in Debtors’ student loan creditors receiving 44.51% of their claims. Under this proposed plan, other general unsecured creditors will receive 33.30% of their claims.

10. If Debtors’ student loan creditors were paid through the plan along with the other general unsecured creditors, the unsecured creditors would receive approximately 36.48% over the course of the plan. Because of the standard order in which trustees in South Carolina distribute payments to creditors,² according to the parties’ stipulation of facts filed on September 15, 2017, disbursements to general unsecured creditors would not begin until approximately month thirty (30) of the plan.

11. Interest and fees will continue to accrue on the student loans during the term of the bankruptcy case, including during the time that unsecured creditors are awaiting distribution.

the general unsecured creditors is fair.” Because here, the difference is approximately 11%, Trustee argues that unfair discrimination exists.

*446 ARGUMENTS OF THE PARTIES

Debtors argue that their proposed chapter 13 plan does not unfairly discriminate against non-student loan unsecured creditors, because Debtors propose to pay more than their means test disposable income into the plan for non-student loan unsecured creditors. Therefore, Debtors argue, even though their student loan creditor is receiving a slightly higher percentage than other general unsecured creditors by being paid outside the plan, the classification does not unfairly discriminate because the non-student loan unsecured creditors are receiving all they are entitled to under the means test. Debtors also argue that the separate classification of the student loan has a good faith, reasonable basis because requiring Debtors to pay the student loan with their other general unsecured creditors would result in substantial interest and late fees accruing on the student loans, increasing the amount owed on the loans at the conclusion of the bankruptcy case and interfering with the purpose of Debtors’ bankruptcy case, obtaining a fresh start.

Trustee responds that the separate classification of the student loan creditor does in fact unfairly discriminate against other general unsecured creditors, because the student loan creditor will receive more favorable treatment than other unsecured creditors. Trustee also asserts that Debtors’ means test disposable income is merely a starting point, and that the income listed on Schedules I and J, along with judicial discretion and common sense, should be used to determine a debtor’s projected disposable income. Trustee points out that Debtors have options for lowering Mrs. Kindle’s student loan payments, such as deferment, which have not been taken advantage of, and that Debtors also have the option of raising their plan payments even further to pay non-student loan creditors at the same rate as the student loan creditor.

Trustee argues that the purpose of chapter 13 is to ensure that debtors pay their creditors the maximum that they can afford to pay, not whatever figure results from means test calculations. Trustee concedes that all separate classification of student loans should not be disallowed, but proposes a bright line rule that, in situations similar to Debtors’, “where Debtors are above median, employed, and have shown no exceptional circumstances for why the student loan should be paid, that a difference of less than 10 percent between student loan creditor treatment versus

ANALYSIS

^[1] ^[2] ^[3]“The twin aims of bankruptcy are to provide equitable distribution of assets for creditors, and to provide a fresh start for a debtor.” *In re Shelton*, 370 B.R. 861, 868 (Bankr. N.D. Ga. 2007) (citing *Burlingham v. Crouse*, 228 U.S. 459, 472–73, 33 S.Ct. 564, 57 L.Ed. 920 (1913)). However, the bankruptcy concept of equal distribution does not mean all creditors must receive equal distribution; instead, this concept means that there must be equal distribution with respect to similarly situated creditors. One exception to this general concept is set forth in 11 U.S.C. § 1322(b). Section 1322(b)(1) states that a plan may “designate a class or classes of unsecured claims, as provided in section 1122 of this title, but may not discriminate unfairly against any class so designated.” Any separate classification under section 1322(b) is “discrimination”; however, such discrimination may be permissible, unless it is unfair. See *447 *Bentley v. Boyajian (In re Bentley)*, 266 B.R. 229, 237 (1st Cir. BAP 2001) (“Discrimination among classes of creditors, on the other hand, *is* subject to limitation. The plan ‘may not discriminate unfairly against any class so designated.’ Before determining what this phrase prohibits, we note first that it tacitly *permits* some measure of discrimination between different classes. In prohibiting only such discrimination as is unfair against any class, § 1322(b)(1) signals that a plan may, to an extent, treat different classes differently. So a plan may discriminate, but not unfairly.”). Section 1322(b)(5) expressly allows a debtor to cure a default and maintain direct payments on certain claims, such as the student loan debts at issue here, stating that a plan may “provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due.” Thus, the Bankruptcy Code expressly allows the discrimination proposed here—the remaining issue then, is whether the discrimination is unfair.

I. Projected Disposable Income

Before determining whether the proposed separate classification unfairly discriminates, the Court must address the parties’ arguments regarding how to calculate Debtors’ projected disposable income. 11 U.S.C. § 521 sets forth a variety of documents a debtor must file, including:

- (B)(ii) a schedule of current income and current expenditures;
- ...
- (iv) copies of all payment advices or other evidence of payment received within 60 days before the date of the filing of the petition, by the debtor from any employer of the debtor;
- (v) a statement of the amount of monthly net income, itemized to show how the amount is calculated; and
- (vi) a statement disclosing any reasonably anticipated increase in income or expenditures over the 12-month period following the date of the filing of the petition.

Additionally, Fed. R. Bankr. P. 1007(b)(6) provides:

A debtor in a chapter 13 case shall file a statement of current monthly income, prepared as prescribed by the appropriate Official Form, and, if the current monthly income exceeds the median family income for the applicable state and household size, a calculation of disposable income made in accordance with § 1325(b)(3), prepared as prescribed by the appropriate Official Form.

Section 1325(b) provides, in relevant part:

- (b)(1) If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, as of the effective date of the plan—
- ...
- (3) Amounts reasonably necessary to be expended under paragraph (2), other than subparagraph (A)(ii) of paragraph (2), shall be determined in accordance with

subparagraphs (A) and (B) of section 707(b)(2), if the debtor has current monthly income, when multiplied by 12, greater than –

- (A) in the case of a debtor in a household of 1 person, the median family income of the applicable State for 1 earner;
- (B) in the case of a debtor in a household of 2, 3, or 4 individuals, the highest median family income of the applicable State for a family of the same number or fewer individuals; or
- *448 (C) in the case of a debtor in a household exceeding 4 individuals, the highest median family income of the applicable State for a family of 4 or fewer individuals, plus \$700 per month for each individual in excess of 4.

In sum, then, a chapter 13 debtor is required to file schedules of current income and current expenditures—Schedules I and J—as well as, if the debtor’s income exceeds the median family income for South Carolina, complete a “means test” calculation of disposable income using the formula established for chapter 7 cases. Debtors, who are above-median, have filed all required forms and documentation in their chapter 13 case.

11 U.S.C. § 1325, discussing the requirements for confirmation of a chapter 13 plan, provides, in relevant part:

- (b) (1) If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, as of the effective date of the plan—
- (A) the value of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or
- (B) the plan provides that all of the debtor’s projected disposable income to be received in the applicable commitment period beginning on the date that the first payment is due under the plan will be applied to make payments to unsecured creditors under the plan.

(2) For purposes of this subsection, the term “disposable income” means current monthly income received by the debtor (other than child support payments, foster care payments, or disability payments for a dependent child made in accordance with applicable nonbankruptcy law to the extent reasonably necessary to be expended for such child) less amounts

reasonably necessary to be expended—

(A)(i) for the maintenance or support of the debtor or a dependent of the debtor, or for a domestic support obligation, that first becomes payable after the date the petition is filed; and

(ii) for charitable contributions (that meet the definition of “charitable contribution” under section 548(d)(3)) to a qualified religious or charitable entity or organization (as defined in section 548(d)(4)) in an amount not to exceed 15 percent of gross income of the debtor for the year in which the contributions are made; and

(B) if the debtor is engaged in business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business.

In *Hamilton v. Lanning*, 560 U.S. 505, 130 S.Ct. 2464, 177 L.Ed.2d 23 (2010), the United States Supreme Court considered how to calculate a chapter 13 debtor’s projected disposable income. In *Lanning*, the debtor had received a one-time buyout from her former employer in the six months prior to the filing of her chapter 13 petition. *Id.* at 511, 130 S.Ct. 2464. This caused her means test disposable income to be \$1,114.98 per month. *Id.* However, the debtor only received income of \$1,922.00 per month from her new job, leaving her, after expenses, with disposable income listed on Schedule J of \$149.03 per month. *Id.* As a result of the debtor’s means test disposable income, the chapter 13 trustee argued that the debtor was required to make plan payments of \$756.00 per month for 60 months; however, both the debtor and the trustee conceded that the debtor’s actual income was insufficient to allow her to make payments in that amount. *Id.* at 512, 130 S.Ct. 2464. The debtor proposed a plan that would require *449 payments of \$144.00 per month for 36 months. *Id.* at 511, 130 S.Ct. 2464. The Supreme Court held that the best approach in determining an above-median debtor’s projected disposable income is to use the debtor’s disposable income from the means test as a starting point, and then make any necessary adjustments for “changes in the debtor’s income or expenses that are known or virtually certain at the time of confirmation.” *Id.* at 524, 130 S.Ct. 2464.

After *Lanning*, the Fourth Circuit twice considered the question of how to calculate projected disposable income. First, in *Morris v. Quigley (In re Quigley)*, 673 F.3d 269 (4th Cir. 2012), the debtor proposed a chapter 13 plan that surrendered two all-terrain vehicles. The payments on the ATVs were included as expenses in the debtor’s means test calculation of disposable income, as were payments

on a truck that were actually being made by the debtor’s ex-boyfriend. *Id.* at 270. The trustee objected on the basis that the debtor’s proposed plan did not allot all of the debtor’s projected disposable income to plan payments, since the debtor had deducted the amount of the ATV and truck payments. *Id.* at 271. The bankruptcy court found that the truck payments should not have been deducted from the calculation of the debtor’s income, because the debtor’s ex-boyfriend was already making those payments. *Id.* at 271. However, the bankruptcy court found that the ATV payments could be deducted because projected disposable income could only be based on the six months prior to the bankruptcy filing. *Id.* The district court affirmed. *Id.* However, the Fourth Circuit reversed, citing *Lanning*. The Fourth Circuit found that when calculating projected disposable income, *Lanning* requires adjustments be made to disposable income to account for any known or virtually certain changes in either income or expenses. *Id.* at 273.

The Fourth Circuit again considered the issue of the calculation of projected disposable income after *Lanning* in *Mort Ranta v. Gorman*, 721 F.3d 241 (4th Cir. 2013). The primary issue in *Mort Ranta* was whether Social Security income should be included in the calculation of projected disposable income. The Fourth Circuit found that Social Security income is excluded from projected disposable income. *Id.* at 251. In doing so, the Fourth Circuit again discussed *Lanning*, and stated:

Following *Lanning*, a debtor’s “projected disposable income” is based on the debtor’s “disposable income,” give or take any adjustments necessary to account for foreseeable changes in that income. Because the Code expressly excludes Social Security income from “current monthly income,” and thus, “disposable income,” it follows that Social Security income must also be excluded from “projected disposable income.” Indeed, every other circuit to address this issue has arrived at the same conclusion.

Id.

^[4] ^[5]In sum, it appears that the law in the Fourth Circuit is that for an above-median debtor, the debtor's means test disposable income is the starting point for determining projected disposable income, and that adjustments should be made only to account for those changes to the debtor's income or expenses that are very likely or certain to occur. Debtors made the student loan payments listed on their schedules for at least the six months prior to their bankruptcy filing. They propose to continue these payments, as [section 1322\(b\)\(5\)](#) allows. Accordingly, including these payments in Debtors' forward-looking budget does not constitute a change to Debtors' income or expenses that is likely or certain to occur in the future—these expenses were part of Debtors' budget *450 well before their bankruptcy case was filed and are permitted as part of Debtors' plan. Trustee presented no evidence indicating that changes to Debtors' income or expenses were likely to occur, and in fact, Mr. Kindle testified that he did not anticipate any significant changes to Debtors' income and expenses. The existence of additional disposable income using Schedules I and J in the event student loan payments are not continued by Debtors is not a change in circumstances. As a result, under [Lanning](#) and the Fourth Circuit's subsequent opinions, no adjustments to Debtors' means test disposable income are necessary in order to arrive at Debtors' projected disposable income. Debtors' projected disposable income, and the amount Debtors are required to pay to unsecured creditors, is \$830.09 per month, the amount reflected on their means test.

II. Unfair Discrimination

The Court has determined that Debtors' projected disposable income in this case is limited to the amount set forth in their means test. The Court must next determine whether Debtors' separate classification of their student loan creditor unfairly discriminates against Debtors' other unsecured creditors. As set forth above, [section 1322\(b\)\(1\)](#) provides that a debtor's chapter 13 plan may "designate a class or classes or unsecured claims ... but may not discriminate unfairly against any class so designated." Historically, South Carolina has used the following five factor test to determine whether a chapter 13 plan's proposed classification unfairly discriminates:

- (1) whether there is a reasonable basis for the classification;
- (2) whether the classification is necessary to the debtor's rehabilitation under Chapter 13;

(3) whether the discriminatory classification is proposed in good faith;

(4) whether there is a meaningful payment to the class discriminated against; and

(5) the difference between what the creditors discriminated against will receive as the plan is proposed, and the amount they would receive if there was no separate classification.

In re Belton, C/A No. 16-03040-JW, 2016 WL 7011570, at *6 (Bankr. D.S.C. Oct. 13, 2016) (citations omitted). However, in *Belton*, Judge Waites stated:

While the undersigned is unwilling to abandon the framework established by my predecessors on the Court, it appears that factor five, the difference in payment percentage, has been unduly emphasized in prior cases. Therefore, in my view, the following streamlined test better reflects the balance of factors pursuant to which a debtor must submit evidence to enable the Court to analyze the separate classification of unsecured debt:

(1) Is there a good faith, rational basis for the separate classification;

(2) Is the separate classification necessary to the debtor's rehabilitation under Chapter 13; and

(3) Is there a meaningful payment to the discriminated class.

Id. at *7. Judge Waites also stated that "[h]elpful, but not controlling to this analysis, is evidence indicating whether the proposed distribution is greater than would be received by the unsecured creditors in a Chapter 7 liquidation, and the degree of difference in distributions between a plan containing separate classifications and one without." *Id.* at *7, n.11. Other courts have developed a variety of tests. See *451 *Labib-Kiyarash v. McDonald* (*In re Labib-Kiyarash*), 271 B.R. 189, 192 (9th Cir. BAP 2001) (utilizing four part test from *Amfac Distribution Corp. v. Wolff* (*In re Wolff*), 22 B.R. 510 (9th Cir. BAP 1982): "(1) whether the discrimination has a reasonable basis; (2) whether the debtor can carry out a plan without the discrimination; (3) whether the discrimination is proposed in good faith; and (4) whether the degree of discrimination is directly related to the basis or rationale for the discrimination."); *In re Pracht*, 464 B.R. 486, 492 (Bankr. M.D. Ga. 2012) (citing *In re Harding*, 423 B.R. 568, 575 (Bankr. S.D. Fla. 2010) (adopting test that requires a "fair balancing of: (1) the Debtor's fresh start; (2) the clear legislative objective of student loan repayment; and (3) fair treatment of creditors as a

whole.”); *In re Orawsky*, 387 B.R. 128, 146–47 (Bankr. E.D. Penn. 2008) (adopting framework using four “baselines” warranting consideration: 1. Equality of distribution, 2. Nonpriority of student loans, 3. Mandatory versus optional contributions, and 4. A fresh start for honest debtors; stating that the degree of departure from the baseline is relevant in determining whether discrimination is unfair); *In re Kolbe*, 199 B.R. 569, 575 (Bankr. D. Md. 1996) (after discussing various tests employed by courts, adopting a test which requires consideration of the same five factors historically used in South Carolina); *In re Furlow*, 70 B.R. 973, 978 (Bankr. E.D. Penn. 1987) (“[D]ifferent treatment is permissible if and only if the debtor is able to prove a reasonable basis for the degree of discrimination contemplated by the Plan.”).

¹⁶Although courts employ a variety of different tests and approaches in considering what constitutes unfair discrimination, nearly all tests involve considering the totality of the circumstances in each case. A totality of the circumstances approach is, and, based on the tests adopted in South Carolina and other districts, has always been, the proper framework for determining whether a classification unfairly discriminates against other creditors.

¹⁷In this case, the totality of the circumstances indicate that Debtors’ proposed treatment of their student loan creditor does not unfairly discriminate against their other general unsecured creditors. As discussed above, non-student loan unsecured creditors are actually receiving more than a strict application of the means test would yield—Debtors are voluntarily contributing their discretionary income (the difference between their means test disposable income and their Schedule J disposable income) to increase the amount paid to those creditors. This voluntary contribution above and beyond what Debtors are required to pay under the means test indicates good faith on the part of Debtors in seeking to repay their creditors. Debtors’ voluntary contribution results in non-student loan unsecured creditors receiving approximately 33% on their claims—a significant percentage in a chapter 13 case.

Additionally, and importantly, there are reasonable bases for the proposed discrimination. Interest on Debtors’ student loans equals nearly \$200.00 per month. If Debtors are not allowed to continue making regular payments on their student loans, interest will continue to accrue at this significant rate. In addition, because distributions to general unsecured creditors will not begin until about thirty (30) months into the plan, default charges will also be added to the loans until the student loan creditor begins

receiving payments from the trustee. Even once trustee payments to the creditor begin, the payments may not be sufficient to cover the default charges, much less the regular payments. All of this will likely result in Debtors *452 owing more on their student loans at the end of their bankruptcy case than they did when the bankruptcy began. Because student loans are nondischargeable, Debtors’ successful completion of their bankruptcy case will have put them in no better position—at least with respect to their student loans—than they were in prior to their bankruptcy filing. This result is not consistent with the Bankruptcy Code’s purpose of providing debtors with a fresh start. Although the fact that student loans are nondischargeable alone does not justify separate classification of those types of claims,³ their nondischargeable character, taken with the rest of the circumstances present, indicate that the student loans in this case may be separately classified.

Trustee argues that the Court should adopt a bright line rule that in situations where Debtors are above-median, employed, and have not shown exceptional circumstances relating to their student loans, any difference in payment between student loan creditors and other unsecured creditors of more than ten percent should be considered unfair discrimination. First, as set forth above, whether a classification discriminates unfairly should be determined on a case by case basis using a totality of the circumstances approach. Further, even if a bright line rule were appropriate, using a percentage to determine what constitutes unfair discrimination would not be proper. In some cases, even a five percent difference between the amounts a student loan creditor and other general unsecured creditors are receiving could be large. However, in other cases, such as this one, a ten percent difference may be much less significant. In this case, non-student unsecured claims will receive a total of approximately 33%, or \$30,003, over the life of the plan. If Debtors’ student loan creditor were to be paid with other general unsecured creditors, the unsecured creditors, including the student loan creditor, would receive a total of approximately 36.48%, or \$56,289.79 over the life of the plan. This means that, excluding the student loan creditor, general unsecured creditors would receive approximately \$32,867.64 over the life of the plan—only \$2,864.64 more than they would receive if the student loan creditor is paid outside the plan. In the circumstances of this case only, the Court finds that the separate classification of Debtors’ student loan creditor does not unfairly discriminate against other unsecured creditors.

¹⁸Concern was also raised that if the student loan creditor is being paid directly, it may be difficult to monitor whether the student loan payments are actually being

made. While [Federal Rule of Bankruptcy Procedure 3002.1](#) was recently adopted to impose various reporting requirements relating to claims secured by a debtor's principal residence and being paid directly to the creditor, no such rule exists for other types of creditors, including student loan creditors. The parties note that [11 U.S.C. § 1328\(a\)](#) provides that a debtor is only entitled to a discharge after completion of "all payments under the plan". Mr. Kindle testified that Debtors understand if they do not continue to make their student loan payments, they will not be entitled to a discharge at the end of their chapter 13 case. Debtors indicate that their certificate of completion of all plan payments will include certification of making the payments to the student loan creditor. If necessary, the trustee may seek verification of these payments at that time. The Court was not asked to, and is not ruling on, the [section 1328\(a\)](#) issue in the context of student loan payments. This order simply reports *453 the agreement of Debtors and Trustee.

CONCLUSION

For the reasons set forth above, Trustee's objection to confirmation is overruled, and Debtors' chapter 13 plan filed July 26, 2017 is confirmed. A separate order will issue.

AND IT IS SO ORDERED.

All Citations

580 B.R. 443

Footnotes

- 1 Debtors' original chapter 13 plan was filed on March 14, 2017 [Docket No. 7]. Trustee filed her objection to confirmation on May 4, 2017 [Docket No. 17]. Debtor's amended plan filed July 26, 2017 contained numerous changes, but the basis for Trustee's objection remained, and so her objection remained outstanding despite the filing of the amended plan.
- 2 Distributions are typically made first to administrative claims and secured claims, then to priority claims. Unsecured creditors only begin to receive distributions after these claims are fully paid.
- 3 See *In re Kalfayan*, 415 B.R. 907, 910 (Bankr. S.D. Fla. 2009) ("Most courts have concluded that discrimination based solely on nondischargeability is unfair.").

586 B.R. 1
United States Bankruptcy Court, E.D. Michigan,
Southern Division,
Flint.

IN RE: Robert QUINN and Lea Quinn, Debtors.

Case No. 17-32180-dof
|
Signed June 5, 2018

Synopsis

Background: Chapter 13 trustee objected to confirmation of debtors’ proposed plan.

[Holding:] The Bankruptcy Court, Daniel S. Opperman, J., held that proposed plan unfairly discriminated in favor of student loan creditor.

Objection sustained.

West Headnotes (3)

^[1] **Bankruptcy**
🔑 Educational loans

If a Chapter 13 debtor does not affirmatively secure an “undue hardship” determination, the discharge order will not include a student loan debt. 11 U.S.C.A. § 523(a)(8).

[Cases that cite this headnote](#)

^[2] **Bankruptcy**
🔑 Classification and discrimination

Debtors’ proposed Chapter 13 plan discriminated unfairly by proposing to pay their nondischargeable student loan obligations a minimum of \$850 and possibly as much as \$1,112.40 per month, but to pay remaining

unsecured creditors nothing, which was similar to what they would likely receive in a Chapter 7 bankruptcy.

[Cases that cite this headnote](#)

^[3] **Bankruptcy**
🔑 Classification and discrimination

A totality of the circumstances inquiry is appropriate when making determining whether the favorable treatment of a student loan debt in a Chapter 13 plan is unfairly discriminatory. 11 U.S.C.A. § 1322(b)(1).

[Cases that cite this headnote](#)

Attorneys and Law Firms

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OPINION SUSTAINING TRUSTEE’S OBJECTION TO CONFIRMATION OF AMENDED CHAPTER 13 PLAN

Daniel S. Opperman, United States Bankruptcy Judge

Introduction

Before the Court is the objection raised by the Chapter 13 Trustee in this case, Carl L. Bekofske, to confirmation of Debtors Robert and Lea Quinn’s proposed Amended Chapter 13 Plan. Debtors’ proposed plan treats their student loan debt favorably—too favorably according to

the Trustee who argues this treatment constitutes unfair discrimination under 11 U.S.C. § 1322(b)(1). The Court agrees and sustains the Trustee's objection to Debtors' Amended Chapter 13 Plan.

Facts

Debtors filed their voluntary petition under Chapter 13 of the Bankruptcy Code on September 21, 2017. Unsecured creditors filed claims in the amount of \$227,193.33. Of that amount, \$192,936.15 is owed to the federal government for student loans incurred by Debtor Lea Quinn. Debtors filed their Amended Chapter 13 Plan on November 29, 2017. The plan proposes a sixty month term with payments of \$1,200 per month. Debtors propose separately classifying their student loan debt as a Class 4 continuing claim, while the remaining unsecured creditors are classified as Class 9. Debtors' plan also states that the Class 4 creditor will receive a minimum of \$850.00 per month and "shall be paid all available funds prior to disbursements on any subsequent level."

The Court held a hearing regarding confirmation of the plan on January 16, 2018. The Trustee objected to the special treatment *2 given to the student loan debt in the plan. No creditors objected to the plan. Because there was some uncertainty regarding there possibly being a co-debtor, the case was set for a status conference on February 7, 2018. On that date, the absence of a co-debtor was confirmed, but the Court required briefing regarding Debtors' separate classification of their student loan debt. Debtors filed their brief on March 2, 2018, arguing that their plan should be confirmed due in part to the unique nature of student loans. They pointed to the fact that the contractual obligation on their student loan claim is \$1,894.00 per month. Under their proposed plan, they estimate that they would pay \$56,800.00 on this claim.¹ However, because of the accumulating interest and penalties, at the end of the sixty month term, they would still owe \$192,720.37 in student loan debt, which is \$215.78 less than what they owed on the date they filed their bankruptcy petition. In contrast, if Trustee's objection is sustained, Debtors argue that they will owe at least \$6,006.22 more on their student loan debt after their Chapter 13 plan is completed. The Trustee filed his brief on March 30, 2018, arguing that Debtors' proposed plan violates § 1322(b)(1) and § 1322(b)(10). The Trustee suggested several ways to amend the plan so that it would no longer be unfairly discriminatory. The first suggestion was to remove the language from the plan requiring the

Class 4 creditor be paid "all available funds prior to disbursements on any subsequent level."² According to the Trustee's calculation, this would allow the student loan creditor to receive \$56,950.00 or a 29% dividend on its claim and the remaining unsecured creditors a 34% dividend. The other suggestion was to place the student loan creditor in Class 9 along with the remaining creditors. Based on the Trustee's calculations, this would allow the student loan creditor to receive approximately \$58,423.91 and the remaining unsecured creditors would receive a 30.3% dividend. In their reply brief filed on April 6, 2018, Debtors disputed the Trustee's calculations because they are based on the amounts owed as of the date of the bankruptcy filing and do not take into account the interest that would continue to accumulate during the term of the plan.

After reviewing the briefs, the Court requested further briefing on specific issues of fact regarding the education Debtor Lea Quinn received as a result of her student loan debt and the employment obtained as a result of that education. Debtors filed their supplemental brief on May 25, 2018. Debtors noted that Debtor Lea Quinn had a bachelor's degree in social work and a master's degree in public administration. Since 2008, she has been a director at a non-profit organization and earns \$71,000 per year. The Trustee filed his supplemental brief on June 1, 2018. A confirmation hearing is set for June 12, 2018.

Jurisdiction

This Court has subject matter jurisdiction over this proceeding under 28 U.S.C. § 1334(b), 28 U.S.C. § 157, and E.D. Mich. LR 83.50(a). This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(L) (confirmation of plans).

Law and Analysis

^[1]In what has been termed a "crisis" for our country, the national student debt *3 has tripled in the past decade to more than \$1.3 trillion. See *In re Engen*, 561 B.R. 523, 544-45 (Bankr. D. Kan. 2016) (citations omitted). There is no statute of limitations for student loans, and thus the government can pursue debtors "to the grave." *Id.* at 546 (citation omitted). Moreover, student loans are

generally excepted from discharge. Under 11 U.S.C. § 523(a)(8), educational loans, scholarships and stipends are nondischargeable, “unless excepting such debt from discharge ... would impose an undue hardship on the debtor and the debtor’s dependents.” If a debtor does not affirmatively secure an undue hardship determination, the discharge order will not include a student loan debt. *Tenn. Student Assistance Corp. v. Hood*, 541 U.S. 440, 450, 124 S.Ct. 1905, 158 L.Ed.2d 764 (2004) (citation omitted). Congress enacted this exception to discharge “to prevent indebted college or graduate students from filing for bankruptcy immediately upon graduation, thereby absolving themselves of the obligation to repay their student loans.” *Barron v. Tex. Guaranteed Student Loan Corp. (In re Barron)*, 264 B.R. 833, 838–39 (Bankr. E.D. Tex. 2001) (quoting *Tenn. Student Assistance Corp. v. Hornsby (In re Hornsby)*, 144 F.3d 433, 436–37 (6th Cir. 1998)). Moreover,

because student loans are generally unsecured and recent graduates often have few or no assets, these debtors have an incentive to try to discharge their educational loans in bankruptcy. If successful, they can then enjoy the higher earning power the loans have made possible without the financial burden that repayment entails. Congress enacted § 523(a)(8) because there was evidence of an increasing abuse of the bankruptcy process that threatened the viability of educational loan programs and harm to future students as well as taxpayers. Congress recognized that this is an instance where a creditor’s interest in receiving full payment of the debt outweighs the debtor’s interest in a fresh start.

Cazenovia College v. Renshaw (In re Renshaw), 222 F.3d 82, 86–87 (2d Cir. 2000) (citations omitted).

This treatment of student loan debt by the Code presents a quandary for Chapter 13 debtors. Not only will the student loan debt survive the debtor’s discharge, but the amount owed in student loans may be more after completion of the plan than it was on the date of the bankruptcy filing. Thus, more and more debtors are

proposing that their student loan creditor be paid a greater amount than the other unsecured creditors in their Chapter 13 plan. Many courts allow debtors to do so,³ reasoning that such treatment is consistent with the Code for a number of reasons:

(1) a debtor will not be afforded a fresh start in bankruptcy if the debtor is defaulting on student loan payments over the term of a 3–5 year plan, considering that on-going monthly plan payments are likely to be less than the amount owed on the student loan debt, interest is accruing, and the debts survive the debtor’s discharge; (2) strong public policy supports the repayment of education loans; (3) Congress prefers Chapter 13 over Chapter 7, and debtors in Chapter 7 fare better with making post-bankruptcy payment on student loans debts because a Chapter 7 debtor will not have been in forced default of student loan *4 debt obligations for 3–5 years; and (4) other unsecured creditors in Chapter 13 are not harmed by the preferential treatment for student loan debt because unsecured creditors must receive a return in Chapter 13 that is equivalent to what they would receive in Chapter 7 pursuant to 11 U.S.C. § 1325(a)(4).

In re Mason, 456 B.R. 245, 248 (Bankr. N.D. W. Va. 2011) (citing Seth J. Gerson, Note: *Separate Classification of Student Loans in Chapter 13*, 73 Wash. U.L.Q. 269, 290–92 (1995)). In other words, not only does the favorable treatment of student loans help debtors, but it is also consistent with the Congressional intent to protect the fiscal health of our country’s student loan programs. *Engen*, 561 B.R. at 541–42. The Court finds these reasons persuasive and agrees that student loan debt may be given favorable treatment in a Chapter 13 plan.

Under § 1322(b)(1), a Chapter 13 plan may

designate a class or classes of unsecured claims, as provided in section 1122 of this title, but may not discriminate unfairly against any class so designated; however, such plan may treat claims for a consumer debt of the debtor if an individual is liable on such consumer debt with the debtor differently than other unsecured claims[.]

While a minority of courts have held that a long term nondischargeable student loan claim under § 1322(b)(5) is not subject to the unfair discrimination requirement of § 1322(b)(1), see, e.g., *In re Williams*, 253 B.R. 220, 227 (Bankr. W.D. Tenn. 2000) (inclusion of unsecured creditors in (b)(5) indicates that it is a type of discrimination that is expressly contemplated and sanctioned by the Code), a majority of courts agree that a debtor may use § 1322(b)(5) to maintain long-term student loan payments only as long as the plan complies with the unfair discrimination prohibition set forth in § 1322(b)(1), see, e.g., *In re Brown*, 500 B.R. 255, 265 (Bankr. S.D. Ga. 2013) (separate student loan classification must undergo unfair discrimination analysis). The courts who follow the majority approach, however, do not agree on what the appropriate framework is for analyzing the issue of unfair discrimination.

The Trustee urges this Court to rely on the guidelines set forth in the case of *Bentley v. Boyajian (In re Bentley)*, 266 B.R. 229 (1st Cir. BAP 2001).⁴ In *Bentley*, the Bankruptcy Appellate Panel for the First Circuit looked at “the principles and structure of Chapter 13 itself” “for the baseline against which to evaluate discriminatory provisions for fairness.” *Id.* at 240. The court identified four guiding provisions for doing so. First, there is the general expectation that, absent an express grant of priority, unsecured creditors will share equally in any dividend. As a result, “fairness in Chapter 13 requires equality of distribution among nonpriority unsecured creditors, and the burden of justification is on those who propose plans to the contrary.” *Id.* Second, the Code does not grant student loans priority status. *Id.* Thus, there is nothing in the Code that “warrants or justifies treating the student loans more favorably than the others.” *Id.* at 241. Third, mandatory versus optional contribution expresses the Chapter 13 requirement that a debtor devote all of his or her projected disposable income to a plan if the plan does not pay the full amount of allowed unsecured claims. *Id.* The expectation is that unsecured creditors share pro rata from distributions funded with the *5 debtor’s

mandatory contributions. *Id.* Fourth, a fresh start for honest debtors is one of the Code’s fundamental purposes. *Id.* This is tempered against the notion that “Chapter 13 does not contemplate that a debtor will necessarily emerge from Chapter 13 entirely free of student loan obligations.” *Id.* at 242. Applying this test, the Court held that the plan at issue, which proposed paying the student loan creditor in full while paying other unsecured creditors only a 3.6% dividend, discriminated unfairly. *Id.* at 243.

While this Court has cited to the *Bentley* Court’s analysis favorably in the past, the Court will now consider other approaches that have been undertaken by courts in more recent years. Some courts continue to utilize a number of factor tests other than the test set forth in *Bentley* to determine whether a proposed plan is unfairly discriminatory. One widely applied test considers: “(1) whether the discrimination has a reasonable basis; (2) whether the debtor can carry out a plan without the discrimination; (3) whether the discrimination is proposed in good faith; and (4) whether the degree of discrimination is directly related to the basis or rationale for the discrimination.” *Jordahl v. Burrell (In re Jordahl)*, 539 B.R. 567, 573 (8th Cir. BAP 2015) (quoting *In re Leser*, 939 F.2d 669, 672 (8th Cir. 1991)) (finding that the separate classification of the student loan debt was unfairly discriminatory under the four-part test). After considering this test and others, another court developed its own “streamlined test” which asks: “(1) Is there a good faith, rational basis for the separate classification; (2) Is the separate classification necessary to the debtor’s rehabilitation under Chapter 13; and (3) Is there a meaningful payment to the discriminated class.” *In re Belton*, No. 16-03040-JW, 2016 WL 7011570, 2016 Bankr. LEXIS 4179 (Bankr. D.S.C. October 13, 2016) (finding that the separate classification of the student loan debt was not unfairly discriminatory under the three-part test).

Other courts have rejected the various tests and have instead opted for a more flexible approach. As articulated by one court, “[t]he various tests seem too inflexible to properly reflect the discretion that this Court has with respect to confirmation of a Chapter 13 plan that contains a separately classified creditor.” *Engen*, 561 B.R. at 538. The court noted that the tests can function as a starting point for the court’s analysis, but should not be a barrier to confirmation of a Chapter 13 plan. *Id.* After considering the application of the *Bentley* guidelines to the facts of that case, the court found that the plan proposing to pay the student loan debt in full without post-petition interest prior to payment of other unsecured claims did not discriminate unfairly. *Id.* at 551. Another

court similarly reasoned that “because ‘unfairness’ is ultimately a discretionary determination, subject to individual judgment that is informed by the nature and purpose of the Bankruptcy Code, articulated multifactor tests applicable to all cases are not helpful and are incongruous with the nature of the required judicial process.” *Mason*, 456 B.R. at 251. The court found that while it was permissible to treat the student loan creditors more favorably than the other unsecured creditors, the debtor was required to articulate a reason as to why she proposed making a 72% distribution to her student loan creditors and only an 8% distribution to other unsecured creditors. *Id.* at 252. As another court aptly observed, “[a]lthough courts employ a variety of different tests and approaches in considering what constitutes unfair discrimination, nearly all tests involve considering the totality of the circumstances in each case.” *In re Kindle*, 580 B.R. 443, 451 (Bankr. D.S.C. 2017). Applying a totality of circumstances approach, the court found *6 that the debtor continuing to make her student loan payments while paying the remaining unsecured creditors a 33% dividend was not unfairly discriminatory. *Id.* at 452.

^{12]} ^{13]}The Court agrees that a totality of the circumstances inquiry is appropriate when making the determination of whether the favorable treatment of a student loan debt in a Chapter 13 plan is unfairly discriminatory. Here, the student loan claim is in the amount of \$192,936.15. Under Debtors’ proposed plan, the student loan creditor would receive a minimum of \$850.00, but possibly as much as \$1,112.40, per month. Despite this significant payment, Debtor Lea Quinn would continue to be in default of her student loans because her contractual obligation is \$1,894.00 per month. This is contrary to one of the reasons that supports the favorable treatment of student loan debt, and that is to not force a debtor into default during the term of the plan. Many courts that have confirmed a plan giving student loan debt favorable treatment consider this an important factor. *See, e.g., Webb*, 370 B.R. at 425 (stating that “[i]f debtors are not allowed to continue their direct payments to the Student Loan Creditors, they may face the consequences of default upon completion of their Chapter 13 plan payments, and such a result conflicts with the purpose of a fresh start”). Moreover, here, the remaining unsecured creditors would receive nothing, which is similar to what

they would likely receive in a Chapter 7 bankruptcy. *Cf. id.* at 426 (noting that a payment of a 1% dividend in the proposed plan in that case is more than unsecured creditors would likely receive in a Chapter 7 bankruptcy).

Debtors argue that if their plan is confirmed, they will owe \$215.78 less on their student loan debt at the end of the plan’s sixty month term, but if the Trustee’s objection is sustained, they will owe \$6,006.22 more on their claim. The Court finds that this slight benefit to Debtors does not offset the discrimination against the remaining unsecured creditors. Moreover, the Court questions the efficacy of a Chapter 13 plan where Debtors will be in default of their student loan debt during the term of the plan and, yet, the remaining unsecured creditors will receive nothing. The Court notes that applying the streamlined test set forth by the court in *Belton* further supports its conclusion because under Debtors’ proposed plan, there is no “meaningful payment to the discriminated class.” *See Belton*, 2016 WL 7011570, at *7, 2016 Bankr. LEXIS 4179, at *20. In sum, while the Court finds that student loan debt may be given favorable treatment in a Chapter 13 plan, considering the totality of the circumstances here, the Court finds that the plan proposed by Debtors is unfairly discriminatory under § 1322(b)(1).⁵ The Court therefore sustains the Trustee’s objection to confirmation of the plan.

Conclusion

For the forgoing reasons, the Court sustains the Trustee’s objection to confirmation of Debtors’ Amended Chapter 13 Plan. The Trustee is directed to prepare an order consistent with this Opinion and the entry of order procedures of this Court.

All Citations

586 B.R. 1

Footnotes

- 1 The Trustee estimates that the student loan creditor would be paid \$68,806.00 under the plan.
- 2 The Trustee noted that while the plan set forth that the student loan creditor would receive a minimum payment of \$850.00 per month, due to this language, it may actually receive up to \$1,112.40 per month.

- 3 Some courts draw the distinction between remaining current on student loan payments during the term of the plan and accelerating those payments. *See, e.g., In re Webb*, 370 B.R. 418, 425 (Bankr. N.D. Ga. 2007) (distinguishing cases where the debtors proposed paying substantially greater dividends throughout the course of the plan from that case where debtor proposed making payments in the same amount provided by the original contract).
- 4 Debtors urge this Court to adopt a test set forth in *In re Bird*, No. 94-01012, 1994 WL 738644, 1994 Bankr. LEXIS 2384 (Bankr. D. Idaho Dec. 23, 1994). However, this Court finds that case to be outdated and declines to do so.
- 5 Because the Court sustains the Trustee's objection based on a violation of § 1322(b)(1), there is no need to discuss the Trustee's alternative argument that Debtors' special treatment of their student loan debt also violates § 1322(b)(10), which prohibits payment of post-petition interest on an unsecured, nondischargeable debt unless the debtor pays all other allowed claims in full.

2018 WL 6333588

Only the Westlaw citation is currently available.
United States Bankruptcy Court, S.D. New York.

IN RE: Bruce STERMAN and Luba Pincus,
Debtors.

Robert Geltzer, as Chapter 7 Trustee of Bruce
Serman and Luba Pincus, Plaintiff,

v.

Oberlin College, Oberlin Student Cooperative
Association, Nelnet, Inc., Alexandra Serman, and
Samantha Serman, Defendants.

Case No. 16-10378 (MG)

|
Adv. Pro. Case No. 18-01015 (MG)

|
Signed December 4, 2018

Synopsis

Background: Chapter 7 trustee brought adversary proceeding to avoid, as constructively fraudulent transfers, college tuition and other education-related payments that debtors made on behalf of their daughters. Parties cross-moved for summary judgment.

Holdings: The Bankruptcy Court, Martin Glenn, J., held that:

[1] debtors did not receive either “reasonably equivalent value” or “fair consideration” for prepetition college tuition and other education-related payments made on behalf of their adult daughters;

[2] debtors received both “reasonably equivalent value” and “fair consideration” for prepetition college tuition and other education-related payments that they made to allow their daughter to attend private liberal arts college while she was still a minor; and

[3] debtors did not receive “reasonably equivalent value” for transfers that they made to or for benefit of their daughter after she graduated from college, and after she had attained age of majority.

Motions granted in part and denied in part.

West Headnotes (12)

[1] **Child Support**
Obligation of Parents

Under New York law, parents have obligation to provide for their minor children’s necessities, such as food, clothing, shelter, medical care, and education.

Cases that cite this headnote

[2] **Infants**
Status in General; Commencement and Duration

Age of majority in New York is 21 years old.

Cases that cite this headnote

[3] **Fraudulent Conveyances**
Consideration

Under New York law, party seeking to avoid transfer as constructively fraudulent to creditors generally bears the burden of proving a lack of fair consideration. *N.Y. Debt. and Cred. Law* §§ 272, 273, 275.

Cases that cite this headnote

[4] **Fraudulent Conveyances**
Consideration

Under New York law, while the party seeking to avoid transfer as constructively fraudulent to creditors generally bears burden of proving a lack of fair consideration, if the facts regarding nature of consideration are within transferee’s control, then the burden of proving fairness of consideration shifts to transferee. *N.Y. Debt.*

and Cred. Law §§ 272, 273, 275.

Cases that cite this headnote

^[5] **Bankruptcy**
 ☛ "Reasonably equivalent value" in general

What debtor receives in exchange for alleged constructively fraudulent transfer does not have to be mathematically equal to what he transferred in order to constitute "reasonably equivalent value," as that term is used in fraudulent transfer provision of the Bankruptcy Code. 11 U.S.C.A. § 548(a)(1)(B).

Cases that cite this headnote

^[6] **Bankruptcy**
 ☛ "Reasonably equivalent value" in general

Purely emotional benefits, such as love and affection, will not suffice as "reasonably equivalent value" under constructive fraudulent transfer provision of the Bankruptcy Code. 11 U.S.C.A. § 548(a)(1)(B).

Cases that cite this headnote

^[7] **Bankruptcy**
 ☛ "Reasonably equivalent value" in general

Both direct and indirect benefits flowing to debtor may be considered in deciding whether he received "reasonably equivalent value," of kind sufficient to preclude avoidance of transfer as constructively fraudulent to creditors. 11 U.S.C.A. § 548(a)(1)(B).

Cases that cite this headnote

^[8] **Bankruptcy**
 ☛ "Reasonably equivalent value" in general
Fraudulent Conveyances
 ☛ Sufficiency in general

"Fair consideration" under the constructive fraud provisions of New York fraudulent transfer law and "reasonably equivalent value" under the bankruptcy constructive fraudulent transfer provision have substantially the same meaning. 11 U.S.C.A. § 548(a)(1)(B); N.Y. Debt. and Cred. Law §§ 272, 273, 275.

Cases that cite this headnote

^[9] **Bankruptcy**
 ☛ "Reasonably equivalent value" in general
Fraudulent Conveyances
 ☛ Nature, source, and sufficiency of consideration in general

Chapter 7 debtors did not receive either "reasonably equivalent value" or "fair consideration," under constructive fraud provisions of bankruptcy fraudulent transfer statute or New York fraudulent transfer law, for prepetition college tuition and other education-related payments made on behalf of their adult daughters, though these payments allegedly benefited debtor by increasing likelihood that, with college educations, their daughters would become self-sufficient and also provided psychic assurance to debtors in guaranteeing, in connection with room and board payments, that daughters would have roof over their heads and food to eat while attending college. 11 U.S.C.A. §§ 544, 548(a)(1)(B); N.Y. Debt. and Cred. Law §§ 272, 273, 275.

Cases that cite this headnote

^[10] **Bankruptcy**
 ☛ "Reasonably equivalent value" in general
Fraudulent Conveyances
 ☛ Nature, source, and sufficiency of consideration in general

Chapter 7 debtors received both “reasonably equivalent value” and “fair consideration,” under constructive fraud provisions of bankruptcy fraudulent transfer statute and New York fraudulent transfer law, for prepetition college tuition and other education-related payments that they made to allow their daughter to attend private liberal arts college while she was still a minor under New York law, in form of satisfaction of their obligation to provide for their minor child’s necessities, though daughter could have attended public university at much lesser cost. 11 U.S.C.A. §§ 544, 548(a)(1)(B); N.Y. Debt. and Cred. Law §§ 272, 273, 275.

Trustee [Robert L. Geltzer](#), 630 Third Avenue, New York, NY 10017, By: Allen G, Kadish, Esq.

PAUL MILBAUER, ESQ., Counsel to Debtors Bruce Serman and Luba Pincus and Defendants Alexandra Serman and Samantha Serman, 90 John Street – Suite 313, New York, NY 10038

[Cases that cite this headnote](#)

[11] Bankruptcy
 🟡 Powers, Duties and Fiduciary Capacity

Trustee’s is not granted veto power over debtor’s personal decisions, at least not with respect to prepetition expenditures.

[Cases that cite this headnote](#)

[12] Bankruptcy
 🟡 “Reasonably equivalent value” in general

Chapter 7 debtors did not receive “reasonably equivalent value” for transfers that they made to or for benefit of their daughter after she graduated from college, and after she had attained age of majority, and such transfers could be avoid as constructively fraudulent to creditors under bankruptcy fraudulent transfer statute. 11 U.S.C.A. § 548(a)(1)(B).

[Cases that cite this headnote](#)

Attorneys and Law Firms

ARCHER & GREINER, P.C., Counsel to the Chapter 7

MEMORANDUM OPINION AND ORDER
GRANTING IN PART AND DENYING IN PART
CROSS-MOTIONS FOR SUMMARY JUDGMENT

MARTIN GLENN UNITED STATES BANKRUPTCY JUDGE

*1 The Chapter 7 Trustee, Robert L. Geltzer (the “Trustee”), seeks to recover as constructive fraudulent transfers amounts paid by the Chapter 7 co-debtors, Luba Pincus and Bruce Serman (the “Debtors”), to or for the benefit of their two daughters, defendants Alexandra Serman and Samantha Serman (the “Defendants”), allegedly for college tuition, books and supplies, and room and board while they were students at Oberlin College. The Trustee and the Defendants filed cross-motions for summary judgment (the “Trustee’s Motion,” ECF Doc. # 24; the “Defendants’ Motion,” ECF Doc. # 22 at 11). The Defendants’ Motion is supported by the affidavits of debtor Luba Pincus (the “Pincus Affidavit,” ECF Doc. # 22 at 1) and debtor Bruce Serman (the “Serman Affidavit,” ECF Doc. # 22 at 5).

The parties also entered a stipulation of undisputed facts (the “Stipulated Facts,” ECF Doc. # 21). The Stipulated Facts indicate that some of the transfers to or for the benefit of Samantha were made while she was a college student *before* she was 21 years old and some were made while she was a college student *after* she was 21 years old. The Stipulated Facts indicate that the transfers to or for the benefit of Alexandra were made *after* she was 21 years old and *had already graduated from college*. According to the Stipulated Facts, since Alexandra graduated college in 2009, she has been “financially independent.” (Stipulated Facts ¶ 15.)

The parties limit their cross motions to a request that the Court rule whether the Debtors received “reasonably equivalent value” for the transfers for college tuition and expenses; if the Debtors received reasonably equivalent

value, the transfers would not be avoidable as constructive fraudulent transfers even if the Debtors were insolvent at the time of the transfers. There are two questions presented: first, did the Debtors receive reasonably equivalent value for their daughters' college educations and related expenses because their daughters' education will enhance their self-sufficiency; and second, does it matter whether the daughters were younger or older than 21 when the transfers were made?

For the reasons explained below, the Court grants the Trustee's Motion in part and denies it in part with respect to the transfers to or for the benefit of Samantha. The Trustee's Motion is granted with respect to the transfers to or for the benefit of Alexandra, as she was older than 21 and no longer a student when the transfers were made.

I. BACKGROUND

The Debtors, Luba Pincus and Bruce Sterman, filed a joint chapter 7 petition on February 19, 2016 (the "Petition Date"). (The Stipulated Facts ¶ 2.) The Trustee filed an adversary proceeding to recover allegedly constructively fraudulent transfers made by the Debtors to or for the benefit of their daughters. (*Id.* ¶ 11-12.)¹

*2 Alexandra attended Oberlin College from 2005-2009; Samantha attended Oberlin College from 2009-2013. (*Id.* ¶ 15-19.) In the six years prior to the Petition Date, the Debtors made several transfers to or for the benefit of their daughters. The parties stipulate that the transfers were made in connection with the Defendants' "college educations at Oberlin College and related expenses, including school books and supplies, meals, campus housing/rent/utilities, transportation and birthday presents." (*Id.* ¶ 12.)

The Stipulated Facts state that Alexandra Sterman reached age 21 on January 12, 2008 and graduated from Oberlin College in 2009. (Stipulated Facts ¶¶ 13 & 14.) Exhibit A to the Complaint (ECF Doc. # 1) indicates that transfers to or for the benefit of

Alexandra, totaling \$15,675.00, were made between August 13, 2010 and October 13, 2015. Paragraph 12 of the Stipulated Facts states that "[t]he schedules of transfers that are attached to the Complaint as Exhibits A and B accurately describe the transfers to and/or for the benefit of the Defendants that are the subject of the Complaint." Those two exhibits list transfers between

2010-2015. Both the Stipulated Facts and the Pincus Affidavit state that Alexandra attended college between 2005 and 2009, and graduated in 2009, so it is clear under the Stipulated Facts that the transfers to or for the benefit of Alexandra all were made after she was 21 years old and after she graduated from Oberlin. The Pincus Affidavit also makes clear that "[s]ince graduation [Alexandra] has been fully employed, self sufficient and tax paying adult." (Pincus Affidavit ¶ 9.)

^[1] ^[2]The Trustee claims that the transfers are constructively fraudulent. The Trustee seeks to recover \$15,675.00 from Alexandra for transfers "while she was of majority age." (Stipulated Facts ¶ 16.) The Trustee seeks to recover \$9,952.00 from Samantha; \$2,276.00 of those transfers were made "in respect of college tuition and living expenses ... while she was a minor, and \$7,676.00 were made while she was of majority age."² (*Id.* ¶ 18.)

For purposes of the summary judgment motions, "the parties have agreed not to put solvency at issue." (Trustee's Motion ¶ 12, ECF Doc. # 11.) Therefore, the sole question is whether the Debtors received reasonably equivalent value for the transfers to or for the benefit of their daughters.³

II. LEGAL STANDARD

A. Summary Judgment

Rule 56(a) of the Federal Rules of Civil Procedure, made applicable by Bankruptcy Rule 7056, states that "[t]he court shall grant summary judgment if the movant shows that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." FED. R. CIV. P. 56(a). To successfully assert that a fact is not in dispute or cannot be disputed, a movant must:

*3 cit[e] to particular parts of materials in the record, including depositions, documents, electronically stored information, affidavits or declarations, stipulations (including those made

for purposes of the motion only), admissions, interrogatory answers, or other materials; or show[] that the material cited do not establish the absence or presence of a genuine dispute, or that an adverse party cannot produce admissible evidence to support the fact.

FED. R. CIV. P. § 56(c)(1).

“The party seeking summary judgment bears the burden of establishing that no genuine issue of material fact exists and that the undisputed facts establish [the movant’s] right to judgment as a matter of law.” *In re Soliman*, 515 B.R. 179, 185 (Bankr. S.D.N.Y. 2014), (citing *Rodriguez v. City of New York*, 72 F.3d 1051, 1060–61 (2d Cir. 1995)).

B. Fraudulent Transfers

The Trustee claims that the transfers were constructively fraudulent pursuant to Bankruptcy Code § 544. Section 544 provides that the trustee may avoid a transfer of a debtor’s property interest that is voidable under state law by a creditor holding an allowed unsecured claim. See 11 U.S.C. § 544(b)(1); see also *Banner v. Lindsay (In re Lindsay)*, Adv. 2010 WL 1780065, at *5 (Bankr. S.D.N.Y. 2010). The Trustee alleges that the transfers in question were fraudulent under the New York Debtor and Creditor Law (“NYDCL”). Under the NYDCL, a conveyance is fraudulent if it is incurred without “fair consideration.” NYDCL §§ 273 and 275. “Fair consideration” is defined by the NYDCL as follows:

fair consideration is given for property, or obligation,

- a. When in exchange for such property, or obligation, as a fair equivalent therefor, and in good faith, property is conveyed or an antecedent debt is satisfied, or
- b. When such property, or obligation is received in good faith to secure a present advance or antecedent debt in amount not disproportionately small as compared with the value of the property, or obligation obtained.

NYDCL § 272.

^[3] ^[4] Ordinarily, the plaintiff bears the burden of proving a lack of fair consideration but where, as here, “the facts

regarding the nature of the consideration are within the transferee’s control, the burden of proving the fairness of consideration shifts to the transferee.” *Ackerman v. Ventimiglia (In re Ventimiglia)*, 362 B.R. 71 (Bankr. E.D.N.Y. 2007).

^[5] ^[6] ^[7] ^[8] The Trustee also argues that the conveyances were constructively fraudulent under Bankruptcy Code § 548. Under that provision, a trustee may avoid a transfer made by the debtor within two years of the filing of the petition if the debtor did not receive “reasonably equivalent value” in the exchange. 11 U.S.C. § 548(a)(1)(b). The Bankruptcy Code defines the term “value” as “property, or satisfaction or securing of a present or antecedent debt of the debtor, but does not include an unperformed promise to furnish support to the debtor or to a relative of the debtor.” 11 U.S.C.A. § 548(d)(2)(A). The Bankruptcy Code does not define the term “reasonably equivalent value.” *In re Gonzalez*, 342 B.R. 165, 169 (Bankr. S.D.N.Y. 2006). Courts have found that the term does not require the exchange to be “mathematically equal” but “[p]urely emotional benefits, such as love and affection” will not suffice. *Id.* at 169, 173. Both direct and indirect benefits flowing to the debtor may be considered. *In re Akanmu*, 502 B.R. 124, 130–31 (Bankr. E.D.N.Y. 2013) (quoting *Liquidation Trust v. Daimler AG (In re Old CarCo LLC)*, No. 11 Civ. 5039(DLC), 2011 WL 5865193, at *7 (S.D.N.Y. Nov. 22, 2011)). “Fair consideration” under the NYDCL and “reasonably equivalent value” under section 548(a)(1)(B)(i) have substantially the same meaning. *Id.* (citing *Picard v. Madoff (In re Bernard L. Madoff Inv. Sec. LLC)*, 458 B.R. 87, 110 (Bankr.S.D.N.Y.2011)).⁴

III. DISCUSSION

*4 The conveyances in this case must be broken down into three categories: (A) transfers made for education-related expenses to or for the benefit of both daughters after they reached the age of majority so that they could attend Oberlin College,⁵ (B) transfers made for education-related expenses to or for the benefit of Samantha when she was a minor, and (C) transfers to Alexandra after she graduated from college. Summary judgment should be granted to the Trustee with respect to categories (A) and (C) and denied with respect to category (B). Summary judgment should be denied to Alexandra and Samantha with respect to category (A) and (C) and granted to Samantha with respect to category (B).⁶

A. The Education Related Transfers Made after the Defendants Reached the Age of Majority

⁹There is a developing body of law regarding whether college tuition payments made by parents for the education of their children after they reach the age of majority are constructively fraudulent. The Trustee points to several decisions where courts held that pre-petition college tuition payments are avoidable because the debtor parents did not receive reasonably equivalent value in exchange for the tuition payments. See *Boscarino v. Bd. of Trs. of Conn. State Univ. Sys. (In re Knight)*, 2017 WL 4410455 (Bankr. D. Conn. 2017); *Roach v. Skidmore Coll. (Matter of Dunston)*, 566 B.R. 624, 636-37 (Bankr. S.D. Ga. 2017); *Gold v. Marquette Univ. (In re Leonard)*, 454 B.R. 444 (Bankr. E.D. Mich. 2011); *Lindsay*, 2010 WL 1780065. The Defendants counter by pointing to case law holding that parents did receive reasonably equivalent value in exchange for college tuition payments. See *Lewis v. Penn. St. Univ. (In re Lewis)*, 574 B.R. 536, 541 (Bankr. E.D. Pa. 2017); *DeGiacomo v. Sacred Heart Univ., Inc. (In re Palladino)*, 556 B.R. 10, 16 (Bankr. D. Mass. 2016); *Trizechahn Gateway, LLC v. Oberdick (In re Oberdick)*, 490 B.R. 687, 712 (Bankr. W. D. Pa. 2013); *Sikirica v. Cohen (In re Cohen)*, 2012 WL 5360956, at *10 (Bankr. W. D. Pa. 2012).⁷

Whether insolvent parents receive reasonably equivalent value for college tuition payments made for the benefit of their adult children is a culturally and socially charged issue. With the greatest respect for the courts that have found reasonably equivalent value for such tuition payments, the Court is constrained by the language of the Bankruptcy Code and the NYDCL—those statutes define the terms “value” and “fair consideration” to require either the transfer of property or the satisfaction of an antecedent debt in return for an insolvent debtor’s payments. 11 U.S.C.A. § 548(d)(2)(A); NYDCL § 272. The Debtors received neither in this case with respect to transfers made to or for the benefit of Alexandra and Samantha after they reached the age of majority—21 years old in New York State.⁸

*5 Alexandra and Samantha argue that their parents received reasonably equivalent value because the transfers made after they were adults increased the likelihood that they would be self-sufficient. (Pincus Affidavit ¶ 23.) The Massachusetts bankruptcy court reached that conclusion in *In re Palladino*, 556 B.R. at 16. In that case, the debtors made pre-petition tuition payments so that their daughter could attend college. *Id.* at 12. The Trustee

attempted to set aside the tuition payments on a theory of constructive fraud. *Id.* at 13. The court ruled against the trustee because it found that the parents received an economic benefit from the tuition payments. The court stated:

I find that the [debtors] paid [the college] because they believed that a financially self-sufficient daughter offered them an economic benefit and that a college degree would directly contribute to financial self-sufficiency ... A parent can reasonably assume that paying for a child to obtain an undergraduate degree will enhance the financial well-being of the child which in turn will confer an economic benefit on the parent. This, it seems to me, constitutes a *quid pro quo* that is reasonable and reasonable equivalence is all that is required.

Id. at 16.

The court’s conclusion is supported by studies on the value of a college education to a family. See Brief *Amici Curiae* of American Council on Education, and 19 Other Education Associations in Support of Sacred Heart University, Inc. and Affirmance, at 4-7, *DeGiacomo v. Sacred Heart University*, No. 17-1334 (1st Cir. Jul. 27, 2017) (citing studies showing that a college degree improves an individual’s chances of gaining employment, increases their average income, and decreases the chances that they will live with their parents).

The Court does not question whether the Debtors’ decision to send money to or for the benefit of their adult daughters for their college education was economically prudent. But, unfortunately, the economic “benefit” identified by the Defendants does not constitute “value” under the NYDCL or the Bankruptcy Code.

In *In re Lindsay*, 2010 WL 1780065, Judge Morris ordered avoidance, as constructively fraudulent transfers, of college tuition payments made for the benefit of the debtors’ son. It is unclear whether the tuition payments were made before or after the son turned 21. The opinion only refers to the “adult son” living with his parents. *Id.* at

*1. The court rejected the defendants' argument that a legal obligation to pay the tuition existed.⁹ The defendants argued that they had a legal and moral obligation to pay for their child's education. *Id.* at *9. But the defendants did not point to any authority supporting these arguments. *Id.* ("The Court is not aware of any law requiring a parent to pay for a child's college education. Defendants do not offer any authority in support of their argument that a judgment debtor's 'moral obligation' to pay for a child's college education is a defense to [the NYDCL]."). To the extent that *Lindsay* is read to require avoidance for tuition and education-related expenses for adult children, this Court agrees with the decision. *See also Knight*, 2017 WL 4410455, at *5 ("While such support is unquestionably admirable ... it is undisputed that the Debtor had no legal obligation [to] pay for her adult son's college education.")¹⁰

*6 The Defendants here also argue that the Debtors received "psychic and other intangible benefits" from the conveyances. (Defendants' Opposition Brief, at 12.) The Defendants explain:

The debtors benefited when they paid rent by knowing their daughters had a roof over their heads on campus. The debtors benefited when they paid utilities by knowing their daughters has [sic] heat and light to read their books on campus. The debtors benefited when they paid health insurance by knowing their daughters could receive medical care. The debtors benefitted when they paid for transportation to and from Oberlin by knowing their daughters were travelling safely to and from campus.

(*Id.* at 11.) The Defendants support this argument by citing to *In re Gonzalez*, 342 B.R. 165. In that case, the debtor had a son out of wedlock with a woman named Karen. *Id.* at 167. Although he had no legal obligation to do so, the debtor made regular monthly payments on a mortgage for the home where his son and Karen lived. *Id.* The debtor claimed "that he made the payments to support his son ... and because Karen was unable to keep current on the note and could not otherwise provide a proper home for [their son]." *Id.* The debtor spent "all of

his weekends" at the home with Karen and his son. *Id.* at 167. The trustee argued that the mortgage payments made by the debtor were avoidable because they were constructively fraudulent. *Id.* at 168. The court ruled against the trustee. The Defendants correctly point out that the *Gonzalez* court's ruling was based in part because the debtor received "psychic" and "other intangible benefits" from the mortgage payments. *Id.* at 172. The Defendants ignore, however, that the court found that these benefits were "in addition to" the debtors' use of the property on a weekly basis. *Id.* Thus, *Gonzalez* does not stand for the proposition that "psychic" benefits alone constitute reasonably equivalent value, as the Defendants portend.

Accordingly, the Trustee's summary judgment motion with respect to the transfers made after Alexandra and Samantha reached the age of 21 is granted.

B. Education Related Conveyances before Samantha Reached the Age of Majority

^[10] ^[11]The Stipulated Facts indicate that \$2,276.00 of the transfers to or for the benefit of Samantha were made while she was a minor. (Stipulated Facts ¶ 18.) The Stipulated Facts also state that the transfers were made for her "college education[] at Oberlin College and related expenses, including school books and supplies, meals, campus housing/rent/utilities, transportation and birthday presents." (*Id.* ¶ 12.) While the case law does not *require* that parents pay for college tuition for a minor child at a private college to satisfy the parents' obligation to provide a minor child with education, the issue rather is whether the parents receive reasonably equivalent value when they do pay for such an education. On this issue, the Court agrees with Chief Judge Craig, writing in *In re Akkanmu*:

The Trustee argues that New York law does not require the Debtors to provide parochial or private school education, and that the Debtors could have satisfied their obligation at no cost by sending the children to public school. This argument misses the point. The fact that the Debtors chose to educate their children in parochial school rather than public school, arguably exceeding the "minimum standard of care," does not change the fact that, by doing so, they satisfied their legal obligation to educate their children, thereby receiving reasonably equivalent value and fair consideration. It is irrelevant to this determination whether the Debtors could have spent less on the children's education, or, for that matter, on their clothing, food, or shelter. To hold otherwise would

permit a trustee to scrutinize debtors' expenditures for their children's benefit, and seek to recover from the vendor if, in the trustee's judgment, the expenditure was not reasonably necessary, or if the good or service could have been obtained at a lower price, or at no cost, elsewhere. For example, a trustee could seek to avoid a debtor's payments to a restaurant for a meal purchased for the debtor's child, or payments to a department store for clothing purchased for the child, on a theory that adequate food or clothing could have been obtained at lower cost. A trustee could sue the vendor to recover the cost of a computer or other electronic device purchased pre-petition by a debtor for his child, on the theory that the item was not reasonably necessary..... The absurdity of this scenario is obvious.

*7 A trustee is not granted veto power over a debtor's personal decisions, at least with respect to pre-petition expenditures. "[A] trustee's powers are not limitless." *In re Thompson*, 253 B.R. 823, 825 (Bankr. N.D. Ohio 2000). "[T]he 'Bankruptcy Code confers absolutely no power upon the trustee to make decisions concerning how a debtor manages his everyday affairs such as where the debtor will live or work.'" *French v. Miller (In re Miller)*, 247 B.R. 704, 709 (Bankr. N.D. Ohio 2000) (determining whether a chapter 7 trustee may waive the attorney-client privilege of a debtor). This is equally applicable to a debtor's decisions concerning where and how to educate his children.

In re Akanmu, 502 B.R. at 132–33; *Graves v. Graves*, 177 Misc.2d 358, 675 N.Y.S.2d 843, 846-47 (Sup. Ct. 1998) (requiring father to pay for child's college education).

Therefore, barring facts showing egregious conduct by debtors (which has not been shown here with respect to these Debtors),¹ the Court concludes that Samantha is entitled to summary judgment dismissing the portion of the Trustee's claim seeking to recover \$2,276.00 of the transfers to or for the benefit of Samantha made while she was a minor; the Trustee's cross motion to recover this portion of the transfers is denied.

Footnotes

¹ The Complaint also seeks to recover conveyances made to Oberlin College, Oberlin Student Cooperative Association, Navient Corporation, and Nelnet, Inc. The Trustee entered into a stipulation dismissing the Complaint against Nelnet, Inc. on September 24, 2018 (ECF Doc. # 30), and has since reached settlement agreements with Oberlin College, Oberlin Student Cooperative Association, and Navient Corporation. (ECF Doc. # 31-33.) Accordingly, the only remaining defendants are Alexandra and Samantha Serman.

² Settled New York law recognizes parents' obligation to provide minor children with housing, food, education and healthcare. "[I]t

C. Transfers to Alexandra After She Graduated from College

¹²The Court has already concluded in Section A above that the Debtors did not receive reasonably equivalent value in return for the transfers made to or for the benefit of Alexandra and Samantha after they were 21. The Stipulated Facts show that all the transfers to or for the benefit of Alexandra were *after* she graduated college, *after* she reached the age of 21, and *after* she was financially independent. Even if any argument could support paying college tuition and related expenses for an adult child while still in school, if the student started college while still a minor, no argument has been made that would immunize from avoidance transfers made after graduation once the adult child has become financially independent.

IV. CONCLUSION

For the reasons explained above, the Court concludes that transfers to or for the benefit of Alexandra and Samantha after they reached the age of 21 for college tuition and related expenses are avoidable as constructive fraudulent transfers if the Debtors were insolvent at the times the transfers were made. On the other hand, on the record before the Court, transfers to or for the benefit of Samantha while she was a minor for college tuition and related expenses were supported by reasonably equivalent value and, therefore, are not avoidable.

IT IS SO ORDERED.

All Citations

--- B.R. ----, 2018 WL 6333588

is axiomatic that parents are obligated to provide for their children's necessities, such as food, clothing, shelter, medical care, and education." *In re Michel*, 572 B.R. 463, 475 (Bankr. E.D.N.Y. 2017) (quoting *In re Akanmu*, 502 B.R. 124, 132 (Bankr. E.D.N.Y. 2013). The age of majority in New York is 21 years old. *Columbia Cty. Dep't of Soc. Servs. ex rel. William O v. Richard O*, 262 A.D.2d 913, 914, 692 N.Y.S.2d 496, 498 (1999) ("As a general rule, parents are required to support a child until the child attains the age of 21 (see, *Family Ct. Act § 413 [1][a]*).").

- 3 The Complaint also includes a claim for unjust enrichment. (Complaint ¶¶ 45-49.) The parties' summary judgment papers are silent on the unjust enrichment claim and only consider whether the conveyances were constructively fraudulent. Accordingly, the unjust enrichment claim is not presently before the Court.
- 4 Both [section 548 of the Bankruptcy Code](#) and the NYDCL require that the trustee establish that the Debtors were insolvent when the transfers were made. Whether the Debtors were insolvent at the times of the transfers remains unresolved.
- 5 All the challenged transfers to or for the benefit of Alexandra were made *after* reached the age of majority (21) and *after* she graduated from college in 2009, and while she was working and "financially independent." It is unclear how these transfers after Alexandra graduated were made so that Alexandra could attend Oberlin College from which she had already graduated. In any event, as explained below, the Court concludes that the Debtors did not receive reasonably equivalent value for transfers made to or for the benefit of Alexandra or Samantha after they reached the age of 21.
- 6 The Complaint also seeks to recover \$700 in cash gifts to Alexandra and Samantha. The Stipulated Facts do not provide any details about those gifts. Nothing in this Opinion addresses the issues concerning the cash gifts.
- 7 The recent decision by the district court in [Pergament v. Brooklyn Law School](#), 18-CV-2204 (ARR), 2018 WL 6182502 (E.D.N.Y. November 27, 2018), is inapposite. The court reversed the bankruptcy court's grant of summary judgment on constructive fraudulent transfer claims in favor of three universities that received tuition payments from a chapter 7 debtor for two of his children. The issue addressed by the district court was whether the colleges were initial transferees, or subsequent transferees that took the tuition payments in good faith. The issue whether the debtor received reasonably equivalent value for the tuition payments is not addressed.
- 8 State law determines the age of majority. It defines the age below which parents are required to provide financial support for their children. The State law requirement to provide financial support establishes the antecedent debt that is satisfied by the payment for tuition and related expenses. As already indicated, New York law sets the age of majority at 21. *See supra* n.3. *In re Knight*, 2017 WL 4410455, one of the best reasoned decisions concluding that tuition payments for adult children does not provide reasonably equivalent value arose from transfers for college tuition for a child over 18 years of age in Connecticut. Unlike New York which defines the age of majority as 21, Connecticut defines the age of majority as 18. *See Spencer v. Spencer*, 10 N.Y.3d 60, 63, 853 N.Y.S.2d 274, 882 N.E.2d 886 (2008).
- 9 *In re Lindsay*, No. 06-36352 (CGM), 2010 WL 1780065, at *9 (Bankr. S.D.N.Y. May 4, 2010) ("Defendants admit that they transferred proceeds of certain assets sales to a university for their son's education. The Court notes at the outset that Defendants produce no evidence of their alleged legal obligation to pay their son's tuition, such as a promissory note in favor of the university or a lender. The Court is not aware of any law requiring a parent to pay for a child's college education.").
- 10 To the extent that *Lindsay* is read to require avoidance for tuition and education-related expenses for adult children, I agree with the decision. As explained in the next section of this Opinion, however, I reach a different result for transfers for tuition and education-related expenses for minor children, which I conclude may be supported by reasonably equivalent value.
- 11 One could postulate egregious facts—such as a distressed debtor making a lump sum transfer of several years of tuition payments and expected related expenses before filing a bankruptcy case—that could lead a court to conclude that the transfer is avoidable as an actual or constructive fraudulent transfer.



Jeffrey J. Graham
Jeffrey J. Graham
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

IN RE:)	
)	
MATTHEW RICHARD ROTH,)	Case No. 17-04109-JJG-7
)	
Debtor.)	
_____)	
MATTHEW RICHARD ROTH,)	
)	
Plaintiff,)	
)	
v.)	Adversary No. 18-50097
)	
BUTLER UNIVERSITY,)	
DISCOVER FINANCIAL SERVICES,)	
INC., and)	
SALLIE MAE BANK,)	
)	
Defendants.)	

**ORDER DENYING MOTION TO COMPEL ARBITRATION
AND DISMISS OR STAY PENDING ARBITRATION**

The motion before the Court asks if an arbitration clause in a student loan contract is enforceable in the context of a dischargeability action. For the reasons stated below, the Court answers that question in the negative.

JURISDICTION

Venue is proper pursuant to 28 U.S.C. §§ 1408 and 1409. The issue of whether a debt is dischargeable is a core matter pursuant to 28 U.S.C. § 157(b)(2)(I). Both parties consent to this Court’s entry of final orders or judgments. *See Wellness Int’l Network, Ltd. V. Sharif*, -- U.S. --, 125 S.Ct. 1932, 191 L.Ed.2d 911 (2015). The Court, at least initially, has jurisdiction over this adversary proceeding pursuant to 28 U.S.C. § 1334, subject to the determination of whether the arbitration agreement removes this matter from the Court’s bailiwick.

BACKGROUND

Plaintiff/Debtor Matthew Richard Roth (“Roth”) attended Butler University in Indianapolis, Indiana. While attending Butler, Roth obtained a student loan in the amount of \$32,800 from Defendant Sallie Mae Bank (“Sallie Mae”). Roth’s promissory note with Sallie Mae contained an arbitration provision that allowed either party to elect to arbitrate any claim arising under the note, including “the imposition or collection of principal, interest, attorneys’ fees, collection costs or other fees or charges relating to this Note[.]”

Roth filed a chapter 7 bankruptcy and scheduled a debt to Sallie Mae in the amount of \$36,927.88. Roth received a discharge and his case was closed. Roth later moved to reopen his case and filed *Plaintiff Matthew Roth’s Amended Complaint Regarding Dischargeability of “Private” Student Loans* (the “Amended Complaint”), seeking to discharge his student loan debt to Sallie Mae (among other lenders) pursuant to 11 U.S.C § 523(a)(8). Specifically, Roth alleges that his loan

with Sallie Mae is not a “qualified educational loan” and, alternatively, that the loan debt should be discharged as its repayment constitutes an undue hardship.

In lieu of an answer Sallie Mae filed its *Motion to Compel Arbitration and Dismiss or Stay Pending Arbitration* (the “Motion to Compel”). In the Motion to Compel, Sallie Mae argues that the Court should compel arbitration of the Amended Complaint in compliance with the Federal Arbitration Act (the “FAA”), 9 U.S.C. §§ 2-3, and dismiss the claims against Sallie Mae for lack of subject matter jurisdiction pursuant to Federal Rule of Civil Procedure 12(b)(1), made applicable to this proceeding pursuant to Federal Rule of Bankruptcy Procedure 7012. Alternatively, Sallie Mae asks the Court to stay Roth’s claims as to Sallie Mae to allow an arbitrator to decide the issues.

Roth counters by arguing that the promissory note’s arbitration provisions are critically vague and unenforceable. Roth further argues that the Court should deny arbitration because the proceeding involves a core matter and that a debtor’s discharge is a matter of paramount concern for the bankruptcy court. For the purposes of this opinion, the Court will assume that the promissory note’s arbitration provision is clear and enforceable, focusing instead on the question of whether the Roth’s claims against Sallie Mae should be subject to arbitration.

DISCUSSION

Roth and Sallie Mae contractually agreed to arbitrate issues regarding claims relating to the promissory note. The FAA, 9 U.S.C. §§ 1 *et seq.*, places arbitration agreements on equal ground with other contractual provisions and makes them

valid, irrevocable and enforceable absent some contrary legal or equitable ground for revocation. *Epic Sys. Corp. v. Lewis*, -- U.S. --, 138 S.Ct. 1612, 1622 (2018). The Supreme Court has read the FAA as establishing “a liberal federal policy favoring arbitration agreements.” *Id.* (citations omitted). Furthermore, courts are to “rigorously enforce agreements to arbitrate.” *Shearson/American Exp., Inc. v. McMahon*, 482 U.S. 220, 226 (1987). This is true even when the claims at issue are statutory rights. *Id.*

The Supreme Court’s decision in *Epic* is the most recent case to explore the alleged conflict between the FAA and another federal statute. There, the Supreme Court was asked to determine if the Fair Labor Standards Act and the National Labor Relations Act overrode an arbitration agreement. When reviewing an alleged conflict between the FAA on the one hand and the FLSA and NLRA on the other, the Supreme Court noted that the party asserting a conflict “bears a heaving burden of showing “a clearly expressed congressional intention’ that such a result should follow” and that there is a “‘stron[g] presum[ption]’ that repeals by implication are ‘disfavored’ and that ‘Congress will specifically address’ preexisting law when it wishes to suspend its normal operations in a later statute.” *Id.* at 1624 (citations omitted). Moreover, the language must be “clear and manifest” for the FAA’s mandate to arbitrate to be overridden. *Id.*

Sallie Mae points to the language in *Epic* and notes that nothing in § 523 of the Bankruptcy Code contains a clear and manifest Congressional intent to override an agreement to arbitrate. Were *Epic* the only Supreme Court to case to address

the interplay of federal statutes and the FAA, Sallie Mae might prevail. But *Epic* does not stand alone on this issue.

In 1987 the Supreme Court tackled the issue of whether the Securities Exchange Act and the Racketeer Influenced and Corrupt Organizations Act rendered a matter non-arbitrable in *Shearson/American Exp., Inc. v. McMahon*, 482 U.S. 220 (1987). Acknowledging that the FAA mandated the enforcement of arbitration agreements, the Supreme Court held that “[l]ike any statutory directive, the Arbitration Act’s mandate may be overridden by a contrary congressional command.” *Id.* at 226. The Supreme Court then set forth a test for determining whether a contrary congressional command existed: (1) the statute’s text; (2) the statute’s legislative history; or (3) an inherent conflict between arbitration and the statute’s underlying purpose. *Id.* at 227.

This approach makes sense. The FAA was intended to put arbitration agreements “upon the same footing as other contracts.” *McMahon*, 482 U.S. at 225-26 (citations omitted); *see also Volt Info. Sci., Inc. v. Bd. of Tr. of Leland Stanford Jr. Univ.*, 489 U.S. 468, 478 (1989) (FAA “simply requires courts to enforce privately negotiated settlements to arbitrate, like other contracts, in accordance with their terms.”). But the FAA did not make arbitration agreements more enforceable than other contracts. *See Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404 n.12 (1967) and *In re Brown*, 354 B.R. 591, 600 (D.R.I. 2006). Similarly, arbitration agreements have been held akin to contractual forum selection clauses,

privately negotiated provisions meant to be enforced according to their terms. *Id.* (collecting cases).

Federal bankruptcy law also is a fundamental public policy, one that is grounded in the Constitution. *Moses v. CashCall, Inc.*, 781 F.3d 63, 72 (4th Cir. 2015). The very purpose of the Bankruptcy Code is to modify the rights – contractual and otherwise – of debtors and creditors. *See In re D&B Swine Farms, Inc.*, 430 B.R. 737, 744 (Bankr. E.D.N.C. 2010). So it should come as no surprise that a bankruptcy court could, in certain circumstances, override a contractual agreement such as an arbitration provision or a forum selection clause. *See In re Anderson*, 884 F.3d 382 (2d Cir. 2018) (upholding decision not to enforce arbitration provision) and *In re Dozier Fin., Inc.*, Adv. Pro. No. 17-80113-HB, 2018 WL 2386812 (Bankr. D.S.C. May 24, 2018) (declining to enforce a forum selection clause in adversary proceeding). The *McMahon* framework provides a way for courts to balance the competing public policies of enforcing arbitration agreements and bankruptcy court’s ability to alter the contractual rights of debtors and creditors. To take away this framework and rely solely on an explicit textual override would elevate arbitration agreements over other contractual provisions and unfairly diminish the Bankruptcy Code.

The High Court’s decision in *McMahon* has never been overruled, and in fact the case was cited in the *Epic* decision. Supreme Court precedent is only overruled after “appropriate consideration and clarity[.]” *In re Williams*, 564 B.R. 770, 777 (Bankr. S.D. Fla. 2017) (collecting cases). Because *Epic* is silent as to any attempt

to overrule *McMahon*, the Court will treat *McMahon* as good law and will apply it to the matter at hand. See *In re Golden*, 587 B.R. 414, 424 (Bankr. E.D.N.Y. 2018) (applying *McMahon* after *Epic* was decided).

No appellate court has found that either the text of the Bankruptcy Code or its legislative history suggests that Congress intended to have the Bankruptcy Code override the FAA. *In re Eber*, 687 F.3d 1123, 1129 (9th Cir. 2012) (collecting cases). The analysis therefore hinges on a single question: whether arbitration would create an inherent conflict with the purposes of the Bankruptcy Code. *Id.*

Although the Seventh Circuit has yet to opine on this issue, several Courts of Appeals have tackled *McMahon*'s inherent conflict inquiry. Most courts have held that bankruptcy courts have discretion to decline arbitration if the matter is a core proceeding and arbitration would frustrate or conflict with the purposes of the Bankruptcy Code. See *Anderson*, 884 F.3d at 387; *In re EPD Inv. Co., LLC*, 821 F.3d 1146, 1150 (9th Cir. 2016); *Whiting-Turner Contracting Corp. v. Elec. Mach. Enters. Inc.*, 479 F.3d 791, 796 (11th Cir. 2007); *In re White Mountain Mining Co., L.L.C.*, 403 F.3d 164, 169 (4th Cir. 2005); but see *In re Mintze*, 434 F.3d 222, 229 (3rd Cir. 2006) (focusing not on core vs. non-core but instead whether the matter was a statutory right under the Bankruptcy Code).

The issues subject to arbitration here are: (1) whether Roth's loan with Sallie Mae is a qualified educational loan under § 523(a)(8) of the Bankruptcy Code; and (2) if so, whether such loan may be discharged as an undue hardship under § 523(a)(8). Both issues are included in the text of the Bankruptcy Code, satisfying

Mintze. The issue of dischargeability is a core proceeding under 28 U.S.C. § 157(b)(2)(I), thereby satisfying *Anderson* and related cases. The Court therefore has the discretion to not enforce the promissory note’s arbitration provision if it finds arbitration would conflict with the purposes and policies of the Bankruptcy Code under any test utilized by the various Courts of Appeals.¹

Sallie Mae argues that there is no inherent conflict present here, pointing to *Williams* as support. There, the debtor sought to avoid arbitration of claims under §§ 523(a)(8) and 524(a)(2) of the Bankruptcy Code. The court enforced the arbitration provision at issue, reasoning that there was no inherent conflict with the Bankruptcy Code as: (1) the debtor had already received a discharge; (2) arbitration would not interfere or affect distribution of the estate or an ongoing reorganization; (3) there was no interference with the preservation of estate assets or the determination of the priority of claims; and (4) the debtor was asserting claims on behalf of a class action. *Williams*, 565 B.R. at 783. Sallie Mae points out that Roth has received his discharge, that this is a chapter 7 liquidation with no reorganization, and that resolution of the claim will not affect estate assets. This, Sallie Mae posits, shows there is no conflict with the Bankruptcy Code and that the arbitration provision should be enforced.

Roth counters by arguing that the Court should follow the reasoning employed in *Golden* and find an inherent conflict exists. Similar to *Williams*, the court in *Golden* had to determine whether claims brought under §§ 523(a)(8) and

¹ The Court specifically reserves any decision as to whether a different result would occur if the matter at issue were a non-core proceeding.

524 of the Bankruptcy Code should be subject to arbitration. Unlike *Williams*, the court in *Golden* found that arbitrating claims under those sections did create an inherent conflict with the Bankruptcy Code because: (1) the fundamental purpose of bankruptcy law was to give debtors a fresh start and that purpose was impeded by arbitrating potential violations of discharge; and (2) Congress specifically allowed bankruptcy courts the power to enforce their own orders and arbitrating violations of the discharge injunction impeded that goal. *Golden*, 587 B.R. at 427-28.

The Court, having considered the issue, believes that *Golden* contains the sounder reasoning of the two cases put forth by the parties. The Supreme Court has recently reiterated that “[o]ne of the main purposes of the federal bankruptcy system is to aid the unfortunate debtor by giving him a fresh start[.]” *Lamar, Archer & Cofrin, LLP v. Appling*, --U.S.--, 138 S.Ct. 1752, 1758 (2018) (citations omitted). The primary tool for effectuating a debtor’s fresh start is the discharge. *Anderson*, 884 F.3d at 390. Allowing an arbitrator to determine dischargeability creates an inherent conflict with the Bankruptcy Code because it would remove an essential function of bankruptcy law from bankruptcy courts. *See Eber*, 687 F.3d at 1131 (allowing arbitrator to decide issues of dischargeability conflicts with the underlying purposes of the Bankruptcy Code) and *In re Koper*, 516 B.R. 707, 719 (Bankr. E.D.N.Y. 2014) (dischargeability of debt is an essential function of bankruptcy courts). Really it is more than inherent conflict. Allowing arbitration of dischargeability – the central purpose of the Bankruptcy Code according to *Anderson*

– would effectively allow parties to contractually overrule the application of federal bankruptcy law. Bankruptcy without the discharge is like a car without an engine; a useful tool rendered ineffective. The Court is unwilling to do that, and finds that the arbitration of dischargeability issues creates an inherent conflict with the Bankruptcy Code.

Another pillar of federal bankruptcy law is Congress’ intention to centralize disputes about a debtor’s legal obligations for prompt and efficient resolution in bankruptcy courts. *See Moses*, 781 F.3d at 72 and *White Mountain*, 403 F.3d at 169-170. Were Sallie Mae to prevail, Roth’s claims against it would be decided by an arbitrator. However, Roth’s claims against the other two defendants would be decided in this proceeding. Roth would have to argue undue hardship on the same set of facts in two forums, incur the cost of two separate proceedings, and face potentially different outcomes were the arbitrator and the Court to rule differently. This dual forum litigation would be inefficient, costly, and time consuming.

The Court finds that enforcing the arbitration of the claims presented by Roth would be inconsistent with the Bankruptcy Code’s purpose of centralizing litigation before a bankruptcy court for efficient resolution.² *See Brown*, 453 B.R. at 603; *see also Moses*, 781 F.3d at 73 (holding arbitration of a core claim is an inherent conflict with the purposes of the Bankruptcy Code).

² It is interesting that the *Williams* opinion – the decision on which Sallie Mae relies – notes that “[i]t seems doubtful that arbitration will present a more efficient resolution of the matter than continued litigation in this adversary proceeding.” *Williams*, 564 B.R. at 784 n.3.

CONCLUSION

Based on the foregoing, the Court finds it has jurisdiction over Roth's claims against Sallie Mae. Furthermore, the Court declines to enforce the arbitration agreement between Sallie Mae and Roth or stay this proceeding to allow such arbitration to go forward. The Court does so because enforcement in this case would create an inherent conflict with the Bankruptcy Code's fundamental policies of affording debtors a fresh start and centralizing disputes about a debtor's obligations for efficient resolution. The Court therefore SUSTAINS Roth's objection and DENIES the Motion to Compel in its entirety.

Having ruled on the Motion to Compel, the Court hereby dissolves the stay on all pending discovery imposed by the Court's Order dated September 7, 2018. The Court will reschedule the pretrial conference on this adversary via separate order.

###

ORDERED.

Dated: June 28, 2018



Roberta A. Colton
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF FLORIDA
TAMPA DIVISION
www.flmb.uscourts.gov

In re:)	
)	
Cheryl Ann Reid,)	Case No. 8:17-bk-09503-RCT
)	Chapter 13
Debtor.)	
_____)	

**MEMORANDUM DECISION AND ORDER
GRANTING, IN PART, DEBTOR’S MOTION TO DETERMINE SECURED
STATUS OF HYUNDAI CAPITAL AMERICA DBA HYUNDAI MOTOR FINANCE**

As a matter of first impression, this court must determine whether a vehicle purchased by a debtor to earn a living driving for a ridesharing service, here Uber, is considered a vehicle purchased for “personal use.”

This issue is considered, following trial, on Debtor Cheryl Ann Reid’s Amended Motion to Determine Secured Status of Hyundai Capital America DBA Hyundai Motor Finance (the “Motion”).¹ Ms. Reid seeks to bifurcate Hyundai Capital America DBA Hyundai Motor Finance’s (“Hyundai”) claim, which is secured by Ms. Reid’s 2016 Hyundai Elantra (the “Vehicle”), under section 506 of the Bankruptcy Code.² Hyundai objects, asserting the hanging paragraph in section

¹ Doc. 17.

² Unless otherwise stated, all statutory references are to 11 U.S.C. §§ 101 *et seq.* (“Code” or “Bankruptcy Code”).

1325(a) of the Code prevents the use of section 506 to reduce the amount of a secured claim owed on a vehicle purchased less than 910 days before a bankruptcy filing when that vehicle was purchased “for the personal use of the debtor.”

BACKGROUND

Ms. Reid purchased the Vehicle new on June 20, 2016. Hyundai provided the financing for the purchase. Some 506 days later, on November 8, 2017, Ms. Reid filed her chapter 13 petition. She valued the Vehicle at \$9,225.00 in her bankruptcy schedules. Hyundai timely filed a fully secured claim in the amount of \$22,756.71.³

In her chapter 13 plan, Hyundai’s debt is designated as a claim to be valued under section 506.⁴ As required by this court’s model plan, Ms. Reid promptly filed her Motion to value the Vehicle and bifurcate Hyundai’s claim into a \$9,225.00 secured claim and a \$13,531.71 unsecured claim. Hyundai objected, citing the hanging paragraph.

After a preliminary hearing, the Motion was set for trial.⁵ The parties later agreed to bifurcate the trial and limit the court’s consideration to the issue of whether the Vehicle was purchased for Ms. Reid’s “personal use.”⁶

At trial,⁷ Ms. Reid testified that in January 2016, after working at Applebee’s and IHOP for over four years, the restaurants cut her hours dramatically from her then forty hours per week. Ms. Reid testified that she started driving for Uber in March 2016 to make up some of the income she lost from her two other jobs. Shortly thereafter, Ms. Reid discovered that she needed a new car to continue driving for Uber. Her old car did not meet Uber’s standards because it had both

³ Claim No. 1.

⁴ Doc. 2, p.4

⁵ Doc. 22.

⁶ Doc. 32.

⁷ The evidence adduced at trial consisted of Ms. Reid’s testimony, Hyundai’s credit file for the Vehicle (Cr. Ex. 1), and Ms. Reid’s 2016 federal tax return (D. Ex. 1).

aesthetic and mechanical issues. So she bought the Vehicle that June, and immediately started driving for Uber full time as her principal employment.

When she bought the Vehicle, Ms. Reid told the sales associate that she was going to be an Uber driver. She also told the sales associate that she did not have a commercial insurance policy because Uber does not require one.

The Retail Installment Sale Contract under the heading “Primary Use For Which Purchased” indicates the use to be “Personal, family, or household unless otherwise indicated below.” The contract then provides the option to check a box next to “business,” “agricultural,” or a blank which could be filled in. On the contract, the blank line is filled in with “N/A.” None of the boxes are checked.⁸

On the Florida Department of Highway Safety and Motor Vehicles Application for Certificate of Title under line 3 labeled “Brands, Usage and Type,” the box next to “private use” is checked. However, as Ms. Reid testified, there is no box available for commercial or business use. The only other option that might apply is “Taxi Cab.”⁹ And as Ms. Reid explained, to her mind the car was not a “Taxi Cab” and Uber is not a taxi service.

Ms. Reid’s Schedule C of her 2016 federal tax return lists her “[p]rincipal business or profession” as “Uber Driver.” Ms. Reid claimed “Car and truck expenses” of \$3,780.00 based on 7,000 “[b]usiness” miles driven for Uber.¹⁰ Her Schedule C indicates she drove 8,000 miles for “[o]ther” purposes. Ms. Reid stated these latter miles included a one-time trip to visit her daughter in Boston for the birth of her grandchild.

⁸ Cr. Ex. 1, p.5.

⁹ The options available on the Florida application include the following: Short Term Lease, Assembled From Parts, Long Term Lease, Bonded Title, Rebuilt, Kit Car, Police Vehicle, Glider Kit, Private Use, Manuf. Buy Back, Taxi Cab, Replica, Flood, Autonomous, Ilev, Electric, Custom, and Street Rod. No option is provided for “other” or “not applicable.” Cr. Ex. 1, p.14.

¹⁰ D. Ex. 1, p.5 (calculated at \$0.54 per mile).

Ms. Reid also claimed related business expenses, specifically a phone.¹¹ The Schedule C notes the Vehicle was available for personal use when off-duty and that Ms. Reid had no other vehicle available for her personal use.¹²

DISCUSSION

If a chapter 13 debtor wants to retain personal property over the objection of a secured creditor, section 1325(a)(5)(B) requires that the debtor’s plan provide that the secured creditor retains its lien and for full payment of the allowed secured claim. Section 506 of the Code typically authorizes a debtor to limit the amount of a secured claim to the value of the collateral. However, section 1325(a) contains an unnumbered paragraph, commonly referred to as the “hanging paragraph,” which makes section 506 unavailable to limit the secured claims of certain motor vehicle lenders. The hanging paragraph¹³ states, in relevant part:

For purposes of paragraph (5), section 506 shall not apply to a claim described in that paragraph if the creditor has a purchase money security interest securing the debt that is the subject of the claim, the debt was incurred within the 910-day period preceding the date of the filing of the petition, and the collateral for that debt consists of a motor vehicle . . . acquired for the personal use of the debtor

The parties concede that the Vehicle was purchased within the 910-day period preceding the bankruptcy filing and that Ms. Reid is the only person who drives the car. The parties also agree that the relevant inquiry involves the determination of Ms. Reid’s intended use on the day she purchased the Vehicle. So the sole issue remaining is whether, when purchased, Ms. Reid intended the Vehicle for her “personal use.”

Hyundai argues that the Retail Installment Sale Contract states on its face that the Vehicle

¹¹ The court takes judicial notice that Uber drivers require the use of a smart phone in order to connect with Uber and its patrons, as well as obtain route information and transmit GPS data.

¹² D. Ex. 1, p.5.

¹³ The hanging paragraph is not enumerated. Because it follows section 1325(a)(8), the hanging paragraph is often referred to as “§ 1325(a)(9)” or “§ 1325(a)(*).”

was acquired for personal use. Ms. Reid responds that she bought the Vehicle with the intention that driving for Uber would become her sole source of income.¹⁴ She admits that she uses the car for personal errands and used the Vehicle for a trip to visit her daughter, but stresses that her personal use was not the reason for her purchase of the Vehicle.

The Bankruptcy Code does not define the term “personal use.”¹⁵ Courts typically look at the “totality of the circumstances” to determine the debtor’s intended use of a vehicle subject to the hanging paragraph, focusing on when the vehicle was acquired.¹⁶

Some courts use the “significant contribution” test. This test examines whether the debtor’s use of the vehicle allows the debtor to make a significant contribution to the income of the family unit.¹⁷ If so, the test is met and the hanging paragraph presents no obstacle to the application of section 506. This test is quite liberal, as it allows any amount of personal use so long as the debtor also uses the vehicle to drive to and from work, thereby generating income.¹⁸

At the opposite end of the spectrum is the “significant and material” test. This test looks to whether the debtor’s personal use of the vehicle is significant and material regardless of the vehicle’s other uses.¹⁹ Under this conservative test, anything more than nominal personal use may negate a finding that the vehicle was purchased for business purposes even if that vehicle is instrumental in a debtor’s business or the performance of the debtor’s job.²⁰

Somewhere in the middle is the “predominant use” test. Under this test, a court determines

¹⁴ Ms. Reid’s Schedule I indicates that, at the time when she filed her bankruptcy petition in November 2017, she had been employed as an Uber driver for 1.6 years. Doc. 1, Attachment to Sch. I.

¹⁵ *In re McGuiness*, No. 17-bk-14746, 2018 WL 1162876, at *2 (Bankr. E.D. Tenn. March 2, 2018).

¹⁶ *See id.*; *In re Strange*, 424 B.R. 584, 588, 592 (Bankr. M.D. Ga. 2010) (“It is well-established that the relevant time period for analyzing the personal use question is the time of acquisition of the vehicle at issue.”).

¹⁷ *See, e.g., In re Hill*, 352 B.R. 69 (Bankr. W.D. La. 2006).

¹⁸ *See In re McGuiness*, 2018 WL 1162876, at *3 (citing *In re Counts*, No. 07-bk-60542, 2007 WL 2669204, at *9 (Bankr. D. Mont. Sept. 6, 2007)).

¹⁹ *See, e.g., In re Solis*, 356 B.R. 398 (Bankr. S.D. Tex. 2006).

²⁰ *See id.*

whether the vehicle is used predominantly for business or personal use.²¹ Recognizing that vehicles are often used for both purposes, one court explained the difference between a vehicle used to travel to and from work and a vehicle used to perform the actual functions of a job:

Transportation to and from work is a personal use in the sense that it satisfies the debtor's personal needs and obligations—namely, the need for a reliable means for the debtor to commute to his or her place of employment. The court recognizes that work transportation has a monetary value in the sense that it allows the debtor to maintain a job (especially where there is no reliable public transportation), and that the income from the debtor's job may provide monetary benefits to the debtor and the debtor's family. However, these benefits are still personal to the debtor and the debtor's family. Any other reading would essentially eradicate the distinction between personal and business use.

In order to establish that a vehicle is used for a “business” or “profit-making” purpose, a debtor must show that the vehicle is used to perform the functions of a business or a trade. In other words, does the debtor use the vehicle to carry out his or her job duties once the debtor arrives at work?²²

The issue presented—whether Ms. Reid, who acquired the Vehicle with the intent of driving for Uber, acquired it for personal use—is rather nuanced since Uber drivers are not required to have a dedicated work vehicle and are afforded the opportunity to drive as much or as little as they wish in order to earn income. This factual scenario does not lend itself to either the “significant contribution” or the “significant and material” test. Reminded of Goldilocks's experience with the three bears, the court finds the “predominate use” test to be just right.

When applying the “predominate use” test, a court considers several factors. These are:

the nature of the debtor's work, how the debtor's vehicle is used to perform the debtor's job duties, whether or not the debtor's employer requires the debtor to use his or her vehicle to perform the debtor's job-related duties, whether the debtor's employer reimburses the debtor for mileage, and whether or not the debtor claims any vehicle-related expenses as business expenses on the debtor's tax returns.²³

Although a court must also consider the retail installment contract signed by the debtor at the time

²¹ See, e.g., *In re Joseph*, No. 06-bk-50655, 2007 WL 950267 (Bankr. W.D. La. March 20, 2007).

²² *In re Joseph*, 2007 WL 950267, at *3 (footnote omitted).

²³ *Id.*

of the vehicle's acquisition, the contract is not dispositive.²⁴

Here, Ms. Reid drives for Uber, a ridesharing company. She picks up passengers at one location and drops them off at another location. To drive for Uber, drivers are required to use an eligible 4-door vehicle.²⁵ Although Uber allows drivers to rent a vehicle, access to an eligible vehicle is necessary. Ms. Reid credibly testified that her previous car was unreliable and did not meet the standards set forth by Uber. It makes sense that she would need a reliable car if she wanted to earn a living as an Uber driver. Moreover, immediately after she purchased the Vehicle, Ms. Reid began to drive for Uber full time.

Although the Retail Installment Sale Contract states that the Vehicle was acquired for personal use, it is unclear whether it was Ms. Reid or the sales associate who filled in the contract blanks. Ms. Reid credibly testified that she clearly informed the sales associate that she was buying the Vehicle to drive for Uber. Because Ms. Reid expressed her intent to use the Vehicle as an Uber driver and the contract does not reflect that intent, the court finds the contract to be ambiguous and inconclusive of Ms. Reid's intent.²⁶ For similar reasons, the statement in the Application for Certificate of Title is not dispositive.

It is true, as Hyundai notes, that Ms. Reid's 2016 federal tax return indicates that she used the Vehicle for non-business purposes more than for business purposes as it states she drove 7,000 miles for business purposes and 8,000 miles for other purposes.²⁷ However, Ms. Reid explained that she did not start driving full time for Uber until June, halfway through the year. She also testified that she had to use the Vehicle for a trip to visit her daughter in Boston for the birth of her

²⁴ *Id.*

²⁵ DRIVER REQUIREMENTS – HOW TO DRIVE WITH UBER, <https://www.uber.com/drive/requirements/> (last visited June 25, 2018) (“In addition to [Uber’s] minimum requirements . . . , each city has its own regulations for vehicles.”).

²⁶ *See In re McGuiness*, 2018 WL 1162876, at *5 (finding the retail installment contract to be both ambiguous and inconclusive of the debtor’s intent).

²⁷ D. Ex. 1, p.5.

grandchild. Depending on the route, Boston is approximately 1,300-1,600 miles away from Ms. Reid's home in Palm Harbor, Florida. Therefore, from that one trip alone, she put about 2,600 – 3,200 miles on the Vehicle. Had she not made this trip, the number of miles for business purposes would have exceeded those for other purposes. And furthermore, the court is mindful that “[t]he words ‘solely’, ‘exclusively’, ‘mostly’, ‘primarily’, ‘partially’ or any other type of quantitative requirement do not appear in the hanging paragraph”²⁸

CONCLUSION

Considering all of the evidence and the circumstances, the court concludes that Ms. Reid bought the Vehicle to earn a living as a full time Uber driver and not for personal use. Thus, the hanging paragraph does not apply and Ms. Reid may value the Vehicle under section 506 of the Bankruptcy Code.

It is therefore **ORDERED**:

1. The Motion (Doc. 17) is GRANTED, in part.
2. A further hearing on the Motion is hereby set for July 10, 2018, at 10:00 a.m., at which time the court will set the matter for trial on the issue of the Vehicle's value. The parties may appear by telephone via Court Solutions.

Attorney Jay M. Weller is directed to serve a copy of this Decision and Order on interested parties who are not registered CM/ECF users and file proof of service with 3 days of its entry.

²⁸ *In re Solis*, 356 B.R. at 409.

ORDERED.

Dated: October 23, 2018



Roberta A. Colton
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF FLORIDA
TAMPA DIVISION
www.flmb.uscourts.gov

In re:

Vickie Joann Roseman,
Debtor.

Case No. 8:16-bk-07215-RCT
Chapter 13

**ORDER SUSTAINING DEBTOR'S OBJECTION TO
CLAIM NO. 7-1 OF GRAND OAKS MASTER ASSOCIATION, INC.**

In this “chapter 20” case,¹ the court must decide what becomes of a secured creditor’s claim in the chapter 13 case when the lien is successfully stripped pursuant to 11 U.S.C. §§ 506(a) and 1322(b)(2)² and when, in the prior chapter 7 case, the debtor discharged her personal liability for the underlying debt. Does the once-secured creditor have an allowed, unsecured claim payable through the chapter 13 plan? Courts are divided on this question. After reviewing the applicable law, this court joins those who find that the creditor does not hold an allowed, unsecured claim.

¹ A “chapter 20” case is where a debtor, after having obtained a chapter 7 discharge, files a chapter 13 case to address non-dischargeable priority or secured debts through a plan of adjustment, notwithstanding that the debtor is not eligible for a second discharge. *E.g. In re Akram*, 259 B.R. 371, 371 and n.1 (Bankr. C.D. Cal. 2001).

² Statutory references are to 11 U.S.C. §§ 101–1532 (“Code” or “Bankruptcy Code”), unless otherwise stated.

Introduction

The facts are undisputed. Debtor Vickie Joann Roseman filed this chapter 13 case on August 22, 2016.³ Approximately 18 months earlier, on February 3, 2015, Ms. Roseman filed a chapter 7 case and received a discharge.⁴ Under § 1328(f)(1), Ms. Roseman is therefore not eligible to receive a discharge in her chapter 13 case.⁵

Ms. Roseman owns her home at 25081 Bloomsbury Court in Land O' Lakes, Florida (the "Property"), which is located within a community managed by Grand Oaks Master Association, Inc. ("Grand Oaks").⁶ Grand Oaks obtained a final judgment against Ms. Roseman and her Property on December 23, 2014.⁷ Ms. Roseman duly scheduled Grand Oaks and the debt in her chapter 7 case, which she filed shortly after entry of the judgment. The debt was not reaffirmed.⁸

In this chapter 13 case, Ms. Roseman again duly scheduled Grand Oaks. Ms. Roseman's schedule D splits the debt owed to Grand Oaks into "Pre Chapter 7" and "Post Chapter 7" amounts.⁹ Consistent with schedule D, Ms. Roseman's proposed chapter 13 plan provides for Grand Oaks as follows: (a) direct payment of ongoing assessments, (b) curing of the "Post Chapter 7" arrears paid at 18%, and (c) stripping of Grand Oaks's lien.¹⁰

Grand Oaks filed a fully secured claim in this case in the amount of \$25,344.43, payable at 18% interest. (Claim No. 7-1). In its claim summary, Grand Oaks acknowledges the prior

³ Doc. 1.

⁴ Case No. 8:15-bk-01075-MGW, Docs. 1 and 13.

⁵ Doc. 9.

⁶ Doc. 1.

⁷ Claim No. 7-1 Ex. B.

⁸ See Case No. 8:15-bk-01075-MGW.

⁹ Doc. 1 Sch. D.

¹⁰ Doc. 30. Although not mentioned in the papers, the court notes that Ms. Roseman's amended chapter 13 plan proposes to pay allowed unsecured claims "\$5,000 – 100%". Although subject to a slight adjustment based on the claims filed, the proposal to pay unsecureds in full could be possible only if the "Pre Chapter 7" amounts due Grand Oaks are not considered.

chapter 7 case and, like Ms. Roseman, splits its claim into pre- and post-chapter 7 amounts. Grand Oaks asserts that although it holds an *in-rem* claim in the full amount of \$25,344.43, it recognizes that Ms. Roseman is personally liable only for the post-chapter 7 amounts, which Grand Oaks calculates at \$6,711.15. Debtor does not dispute her post-chapter 7 liability.

As contemplated by her chapter 13 plan, on March 19, 2018, Ms. Roseman filed a motion to determine the secured status of Grand Oaks and to strip its lien.¹¹ The motion was served in accord with the negative notice provisions of Local Rule 2002-4. After Grand Oaks failed to respond timely, the court entered an order granting Ms. Roseman’s motion on May 1 (the “Lien Strip Order”).¹² The order provides, in relevant part:

If Creditor timely filed a proof of claim, the claim shall be treated as an unsecured claim in the chapter 13 case. If Creditor has not timely filed a proof of claim, the Motion is not deemed an informal proof of claim except for the purpose of initiating the Debtor’s ability to request relief pursuant to 11 U.S.C. § 506(a).

About a week after entry of the Lien Strip Order, Ms. Roseman filed her objection to Grand Oaks’s proof of claim (the “Claim Objection”) (Doc. 68), which is presently before the court. She objects to Grand Oaks’s claim to the extent it seeks to recover the “Pre Chapter 7” amounts, noting that the recent lien strip and her chapter 7 discharge, taken together, render those amounts no longer owed by her or, by extension, the chapter 13 estate.

Grand Oaks makes two points in opposition to the Claim Objection. (Doc. 69). First, it asserts that paragraph 2 of the Lien Strip Order (quoted above) “explicitly establish[es]” that its claim is an allowed unsecured claim in the case. Second, because Grand Oaks held an *in rem* claim against the Property as of the petition date, the claim “is entitled to be treated in full as an unsecured claim against the estate.” *Id.* at ¶¶ 6–7.

¹¹ Doc. 59.

¹² Doc. 65.

Following a preliminary hearing on the Claim Objection, the parties filed supplemental briefs.¹³

Arguments of the Parties

Ms. Roseman argues that to allow Grand Oaks an unsecured claim for the “Pre Chapter 7” amounts impermissibly resurrects her personally liability for the debt and converts that debt, which is nonrecourse by virtue of her chapter 7 discharge, back into recourse debt. She notes that Congress expressly provided for such a result in chapter 11 cases, *see* § 1111(b), but elected not to extend this result into chapter 13. Ms. Roseman asserts that § 502(b)(1) is clear that a claim that is unenforceable against the debtor and her property, like Grand Oaks’s, may not be an allowed claim. Accordingly, she asks the court to reduce Grand Oaks’s claim to \$6,711.15, *i.e.* the undisputed “Post Chapter 7” amounts.

Grand Oaks argues that its claim was valid as of the filing of the chapter 13 petition and therefore is an allowed claim irrespective of Ms. Roseman’s chapter 7 discharge. Grand Oaks adds that the Lien Strip Order “explicitly provides” that its claim is allowed and must be treated as an unsecured claim, payable in full. And it notes that Ms. Roseman “agrees” with this result based upon the *ad damnum* clause in her motion that resulted in entry of the Lien Strip Order.

Discussion

Courts do not agree on how to treat the claim of creditor holding an *in rem* claim when the lien supporting that claim is stripped and the debtor’s personal liability for the underlying debt was discharged. *Compare In re Rosa*, 521 B.R. 337 (Bankr. N.D. Cal. 2014) (concluding the creditor did not hold an allowed, unsecured claim), and *In re Sweitzer*, 476 B.R. 468 (Bankr. D. Md. 2012) (same), with *In re Jennings*, 454 B.R. 252 (Bankr. N.D. Ga. 2011) (stating the creditor’s claim

¹³ Docs. 75 and 76.

must be treated as an allowed, unsecured claim under the chapter 13 plan), and *In re Akram*, 259 B.R. 371 (Bankr. C.D. Cal. 2001) (refusing to value the creditors' "stripped" claims at zero for purposes of the chapter 13 plan). The court finds the analyses in *In re Rosa* and *In re Sweitzer* well-reasoned and persuasive.

As an initial matter, the court can quickly dispense with Grand Oaks's contention that the Lien Strip Order is dispositive of the issue. First, the order does not expressly provide that Grand Oaks has an "allowed" unsecured claim. The order states simply that if Grand Oaks timely filed a claim, its claim "shall be treated as an unsecured claim". The word "allowed" is not used, which is consistent with the purpose of § 506(a). See *In re Rosa*, 521 B.R. at 339–40 (noting § 506(a) does not address the merits or the allowance of the resultant unsecured claim).¹⁴

Second, Grand Oaks's claim was not timely filed. This point is not mentioned by the parties. The claims bar date set in this case was December 27, 2016.¹⁵ Grand Oaks's filed its claim March 2, 2017, 65 days later. Accordingly, even if the language in the Lien Strip Order upon which its argument rests were dispositive, Grand Oaks could not benefit as it failed to satisfy the express condition precedent.

Turning to the merits of the Claim Objection, the court agrees with Ms. Roseman that, to adopt Grand Oaks's position, would revive her personal liability for the discharged debt and convert the debt from nonrecourse into recourse. Grand Oaks is correct that as of the date of the chapter 13 petition, it held a valid *in rem* claim. But that is not the end of the analysis. Ms. Roseman's motion under § 506 and the resulting Lien Strip Order have terminated Grand Oaks's lien rights, albeit provisionally. And "nothing in the Bankruptcy Code mandates that [the creditor]

¹⁴ See also *In re Sweitzer*, 476 B.R. at 470–71 (noting the order avoiding the mortgagee's lien did not contain the language "shall be allowed as a general unsecured claim", which although the standard language provided in the court's local form had been omitted, seemingly intentionally, by debtor's counsel).

¹⁵ Doc. 6.

has an *allowed*, unsecured claim as a result.” *In re Rosa*, 521 B.R. at 339 (emphasis in original).

The definition of a claim under § 101(5) is very broad, but merely having a “claim” is not the same as having an “allowed claim”. The allowance of claims is governed by § 502.¹⁶ Here, Grand Oaks’s “claim,” once stripped of its lien rights, is not enforceable against either Ms. Roseman or the Property. Thus, it must be disallowed under § 502(b)(1). *See In re Rosa*, 521 B.R. at 340–42; *In re Sweitzer*, 476 B.R. at 471–73.

Further, as Ms. Roseman points out, Congress expressly provided for the conversion of a nonrecourse obligation into a recourse obligation in chapter 11 cases via § 1111(b), but declined to so provide in chapter 13. Knowing how to do so, Congress’ silence in chapter 13 cannot simply be ignored. *See In re Rosa*, 521 B.R. at 342; *In re Sweitzer*, 476 B.R. at 472.

In support of its position, Grand Oaks directs the court to *In re Dang*, *In re Jennings*, and *In re Akram*.¹⁷ Although *In re Dang* and *In re Jennings* discuss the issue, they do so without detailed analysis.¹⁸ This is understandable as both courts were confronted not with an objection to claim but objections to confirmation of plan, and further were focused on the preliminary question of whether a junior lien could even be stripped off in a so-called “chapter 20.” *See In re Dang*, 467 B.R. 227; *In re Jennings*, 454 B.R. 252.

At the time *Dang* and *Jennings* were decided, the question of whether a wholly unsecured junior lien could be stripped off in a “chapter 20” case was a hot topic, dividing the bankruptcy courts within this circuit and, for that matter, across the nation. *See Wells Fargo Bank, N.A. v.*

¹⁶ Grand Oaks’s argument as to the import of the phrase “as of the date of the filing of the petition” in the introduction of § 502(b) is of no moment. The phrase references merely to the time at which the court is to value “in lawful currency” any claim to which an objection is made. And contrary to suggestion, the analysis under § 502 does not come before applying § 506(a). *See In re Dang*, 467 B.R. 227, 234 (Bankr. M.D. Fla. 2012) (citing *In re Jennings*, 454 B.R. at 255).

¹⁷ *In re Dang*, 467 B.R. 227; *In re Jennings*, 454 B.R. 252; and *In re Akram*, 259 B.R. 371.

¹⁸ *See In re Dang*, 467 B.R. at 237–38; *In re Jennings*, 454 B.R. at 258–59.

Scantling (In re Scantling), 754 F.3d 1323, 1328–29 (11th Cir. 2014) (gathering cases).¹⁹ But in the summer of 2014, the Eleventh Circuit held in *Scantling* that the stripping off a wholly unsecured junior lien in a “chapter 20” was permissible. The *Scantling* court, reaffirming its earlier holding in *Tanner*,²⁰ stated that the stripping of a “worthless lien” was accomplished by a two-part procedure: a valuation under § 506(a) which determines whether a creditor holds a secured claim followed by a modification of the creditor’s “rights” under § 1322(b)(2). Under this analysis, the court concluded that the debtor’s ineligibility for a discharge in the chapter 13 case was “irrelevant to a strip off in a Chapter 20 case.” *Id.* at 1329–30. The ability of a “chapter 20” debtor to strip off a wholly unsecured lien is now the rule in this circuit and is steadily becoming the majority rule nationwide.²¹ But then, the question remains—what becomes of the creditor’s claim once its lien is rendered valueless and its rights are modified by stripping the lien from its collateral?

In re Akram supports Grand Oaks’s position. There, in 2001, the court declined to “reach a result more damaging to creditors” than that already permitted by lien stripping in the first instance. The court refused to permit the debtors to value the creditors’ claims at zero, thereby “depriving” them of a general unsecured claim in the case. *In re Akram*, 259 B.R. at 374.

But in *In re Akram* too, the procedural posture and the analysis are distinguishable. The court did not consider § 502. Instead, the court was concerned with a possible result that it perceived undermined the Supreme Court’s holding in *Dewsnup v. Timm*,²² which barred lien stripping in chapter 7.

For the same reasons articulated in *In re Rosa*, this court also respectfully disagrees with

¹⁹ See also *HSBC Bank USA, N.A. v. Blendheim (In re Blendheim)*, 803 F.3d 477, 491–92 (9th Cir. 2015) (noting courts within the Ninth Circuit were split on whether “chapter 20” debtors may strip off lien obligations).

²⁰ *Tanner v. FirstPlus Fin. (In re Tanner)*, 217 F.3d 1357 (11th Cir. 2000).

²¹ See, e.g., *In re Blendheim*, 803 F.3d at 497 (joining the Eleventh and Fourth Circuits); *Curwen v. Whiton (In re Curwen)*, 557 B.R. 39, 43–46 (D. Conn. 2016).

²² 502 U.S. 410 (1992).

the *Akram* court's analysis. *In re Rosa*, 521 B.R. at 340–42. The *Akram* court does not articulate a clear basis for providing that the creditors, once stripped of their liens, held allowed unsecured claims. And as also echoed by other courts, concerns over upholding *Dewsnup* are “better suited for a bad faith objection [to confirmation of plan].” *Id.* at 342 (citing cases); *cf. In re Dang*, 467 B.R. at 236–37 (“[A]n issue may arise as to whether the debtor is attempting to avoid the ruling . . . in [*Dewsnup*]. . . . The debtor's intent in filing the later case and seeking to strip the lien may impact on the good faith analysis under § 1325(a)(3) and § 1325(a)(7).”).

For these reasons, it is **ORDERED**:

1. The Claim Objection (Doc. 68) is SUSTAINED, as provided below.
2. Claim No. 7-1 of Grand Oaks Master Association, Inc. is DISALLOWED, in part, as to any “Pre Chapter 7” amounts. Grand Oaks shall receive no distribution as to these amounts.
3. Grand Oaks's claim shall be reduced in amount to \$6,711.15, *i.e.* the undisputed “Post Chapter 7” amounts, and shall be deemed an allowed unsecured claim²³ payable through Debtor's chapter 13 plan.
4. Consistent with the Lien Strip Order, this Order does not prohibit Grand Oaks from asserting, at any time prior to Debtor's successful completion of the chapter 13 plan, any rights it may have as a defendant in any foreclosure proceeding brought by a senior mortgagee, including the right to claim excess proceeds from any foreclosure sale.

Attorney Robert DeLeon is directed to serve a copy of this Order on interested parties that are not served by CM/ECF and to file proof of service within 3 days of it entry.

²³ 11 U.S.C. § 502(a).

**43rd Annual Alexander L. Paskay Memorial Bankruptcy Seminar
Consumer Bankruptcy Legal Update
February 7, 2019**

Recent cases

In re Brown, 742 F.3d 1309 (11th Cir. 2014) - bankruptcy court's finding that Chapter 13 plan filed to pay debtor's attorney's fees only was "not clearly erroneous," but the court "offered no opinion as to other fee-centric Chapter 13 plans," which must be reviewed on a case by case basis.

In re Woide, 720 F. App'x 731 (11th Cir. 2018) - bankruptcy court did not abuse discretion in reopening case to compel surrender.

In re Echeverry, 720 F. App'x 598 (11th Cir. 2018) - debtor's failure to provide transcripts of hearings precluded full and meaningful review.

In re Doolittle, 2018 WL 1627152 (Bankr. S. D. Ga. March 30, 2018) - mortgage lender send escrow overpayment to trustee; court rules it should be turned over to debtor.

In re Adams, 583 B.R. 541 (Bankr. N.D. Ga 2018) - corrective deed outside the chain of title did not provide trustee with constructive notice.

Federal Rule of Bankruptcy Procedure 3002.1(b), December 1, 2018 amendment - regarding notices of payment changes from mortgage lenders.

CONSUMER BANKRUPTCY LEGAL UPDATE

43RD ANNUAL ALEXANDER L. PASKAY MEMORIAL BANKRUPTCY SEMINAR

PRESENTERS:

- **Hon. Caryl E. Delano, Moderator:** *U.S. Bankruptcy Court (M.D. Fla.); Tampa, FL*
- **Alane A. Becket:** *Becket & Lee, LLP; Malvern, Pa.*
- **Robert B. Branson:** *BransonLaw, PLLC; Orlando, FL*
- **Gregory A. Champeau:** *Champeau Law, P.A.; Naples, FL*
- **Kelley M. Petry:** *Kelley M. Petry, P.A.; Tampa, FL*

WORKING WITH STUDENT LOANS IN BANKRUPTCY

\$1.5 TRILLION
PROBLEM

QUALIFIED EDUCATION LOANS & EDUCATIONAL BENEFIT

11 USC § 523(a)(8)(B) QUALIFIED EDUCATION LOAN

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

...

(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; ...

QUALIFIED EDUCATION LOAN

- Any indebtedness **incurred solely to pay qualified higher education expenses of the debtor**, his or her spouse, or any other who was a dependent of the debtor when the indebtedness was incurred. 26 U.S.C. § 221(d)(1)(A).
- The **expenses must be paid or incurred within a reasonable time** before or after the incurring of the indebtedness. 26 U.S.C. § 221(d)(1)(B).
- The loan must be attributable to education provided while the recipient was an **eligible student**. 26 U.S.C. § 221(d)(1)(C). An eligible student is one who carries at least one-half of the normal full-time academic load for his particular course of study. 26 U.S.C. § 25A(b)(3)(B).
- A QEL can not be owed to a debtor's relative, employer, or under certain employment related contracts (see 26 U.S.C. § 72(p)(5)). 26 U.S.C. § 221(d)(1).

QUALIFIED EDUCATION EXPENSES

- The **costs of attendance** at an **eligible educational** institution, less the amounts of certain items including scholarships and allowances. 26 U.S.C. § 221(d)(2).
 - Required hours of instruction.
 - Institution must be eligible to participate in "Title IV" programs.
- **Qualifying costs of attendance** are itemized in 20 U.S.C. § 1087II and include the expected costs such as tuition, fees, books, supplies, room and board, and others. The lists of qualifying costs vary according to the student's status, e.g., full-time, half-time, program of study by correspondence or telecommunications, and others.

EDUCATIONAL BENEFIT

- **(8)** unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor's dependents, for—
- **(A) (i)** an **educational benefit** overpayment or loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution; or
- **(ii)** an obligation to repay funds received as an **educational benefit**, scholarship, or stipend;

IN RE CARDONA, No. 15-16365-BKC-LMI, 2015 WL 9459883 (Bankr. S.D. Fla. Dec. 23, 2015).

- Thus, while educational benefit is not defined in the Bankruptcy Code, it is clear that, as Congress has amended section 523(a)(8) over time, the meaning of educational benefit has become broader. At *2.
- Where, such as in this case, the delineated purpose of the loan is for education, whether that purpose is indicated by the title of the loan, or in the application for the loan or extension of credit, and the use of the funds is consistent with the delineated purpose, I hold that those funds do constitute "funds received for an educational benefit" and, in the absence of a showing of undue hardship, the debt is not dischargeable. At *3.

EDUCATIONAL BENEFIT

- Notably, an interpretation of section 523(a)(8)(A)(ii) that focuses on “funds received as an educational benefit, scholarship, or stipend” not only gives meaning to the other subsections of the statute, but it also comports with the well-established principle of construing exceptions to discharge narrowly. As the Fourth Circuit has explained, “[w]hen considering the applicability of an exception to discharge, we construe the exception narrowly ‘to protect the purpose of providing debtors a fresh start.’” *Nunnery v. Rountree (In re Rountree)*, 478 F.3d 215, 219 (4th Cir. 2007).

BRUNER TEST HARD TO SATISFY

Hemar Ins. Corp. of America v. Cox (In re Cox), 338 F.3d 1238 (11th Cir. 2003).

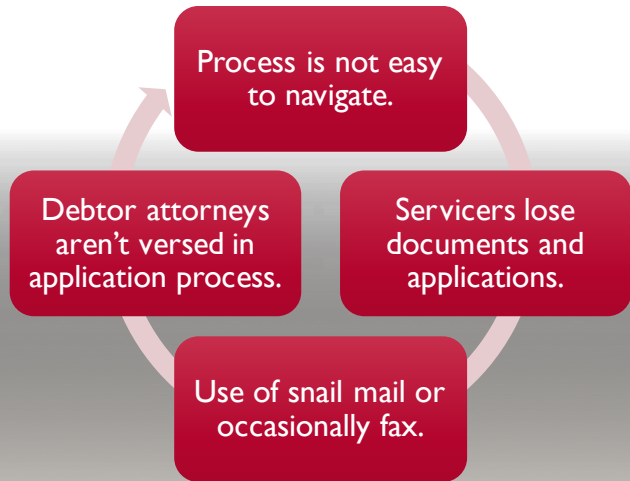
STUDENT LOAN PROGRAMS ARE AVAILABLE

- Need to rethink how we treat student loans in bankruptcy.
- Old way was abatement, interest accrued.

STUDENT LOAN REPAYMENT ALTERNATIVES

- Many income based options
 - Income Based Repayment “IBR”
 - Revised Pay as you Earn “REPAYE”
 - Income-Contingent Repayment “ICR”
 - Pay as you Earn “PAYE”

DEALING WITH STUDENT LOAN SERVICERS



STUDENT LOANIFY



DMM developed Student Loanify, the same company used for the MMM process throughout bankruptcy courts across the United States.



Provides program options including payment amounts.



Applications mail merge, similar to Turbo Tax.

FIRST STEP

- Borrower signs into NSLDS (National Student Loan Data for Students).
 - Pull transcript of all federally guaranteed loans.
 - Upload to Student Loanify.

COMPLETE QUESTIONS

Name, address, Social Security number, driver's license number.

Is debtor disabled? Was debtor defrauded?

Is debtor working in public service such as a teacher or public entity?

Provide income of debtor, marital status, household size.

PROVIDES CURRENT STATUS OF ALL LOANS.

(CONTINUED ON NEXT PAGE)

Current Status of Borrower's Loans:

Right now LDA has 18 Federal Student Loans totaling \$ 134,209.00.

Loan Type/Loan Holder/Loanholder	Principal Balance	Interest	Interest Rate	Status
FFEL Stafford (UNLADROCCS (DEPT OF EDGREAT LAKES))	\$ 1,388.38	\$ 1,888.00	4.8%	BANKRUPTCY CLAIM ACTIVE
FFEL Stafford (UNLADROCCS (DEPT OF EDGREAT LAKES))	\$ 4,887.38	\$ 987.00	4.8%	BANKRUPTCY CLAIM ACTIVE
FFEL Stafford (UNLADROCCS (DEPT OF EDGREAT LAKES))	\$ 4,887.38	\$ 987.00	4.8%	BANKRUPTCY CLAIM ACTIVE
FFEL Stafford (UNLADROCCS (DEPT OF EDGREAT LAKES))	\$ 1,588.38	\$ 1,888.00	4.8%	BANKRUPTCY CLAIM ACTIVE
FFEL Stafford (UNLADROCCS (DEPT OF EDGREAT LAKES))	\$ 1,718.38	\$ 1,887.00	4.8%	BANKRUPTCY CLAIM ACTIVE
FFEL Stafford (UNLADROCCS (DEPT OF EDGREAT LAKES))	\$ 4,887.38	\$ 987.00	4.8%	BANKRUPTCY CLAIM ACTIVE
FFEL Stafford (TRANSITIONAL GUARANTY AGENCY)	\$ 4,288.38	\$ 888.00	9%	BANKRUPTCY CLAIM ACTIVE
FFEL Stafford (TRANSITIONAL GUARANTY AGENCY)	\$ 1,188.38	\$ 1,281.00	4.8%	BANKRUPTCY CLAIM ACTIVE
FFEL Stafford (TRANSITIONAL GUARANTY AGENCY)	\$ 1,188.38	\$ 1,281.00	4.8%	BANKRUPTCY CLAIM ACTIVE
FFEL Stafford (TRANSITIONAL GUARANTY AGENCY)	\$ 4,888.38	\$ 988.00	9%	BANKRUPTCY CLAIM ACTIVE
FFEL Stafford (TRANSITIONAL GUARANTY AGENCY)	\$ 4,888.38	\$ 988.00	9%	BANKRUPTCY CLAIM ACTIVE
FFEL Stafford (TRANSITIONAL GUARANTY AGENCY)	\$ 4,288.38	\$ 1,078.00	4.8%	BANKRUPTCY CLAIM ACTIVE

STUDENT LOANS CONTINUED

AGENCY)	Principal Balance	Interest	Interest Rate	ACTIVE CHAPTER 13
FFEL CONSOLIDATED (TRANSITIONAL GUARANTY AGENCY)	\$ 13,279.00	\$ 558.00	3.5%	DEFAULTED, THEN BANKRUPT, ACTIVE, CHAPTER 13
DIRECT PLUS PARENT (DEPT OF EDGREAT LAKES)	\$ 4,848.00	\$ 22.00	7%	DEFERRED
DIRECT PLUS PARENT (DEPT OF EDGREAT LAKES)	\$ 2,999.00	\$ 33.00	7%	DEFERRED

AMERICAN BANKRUPTCY INSTITUTE

<p>Graduated</p> <p>\$ 885.00 /mo</p> <p>*First 2 years only 120 months</p> <p>Not Eligible</p>	<p>Pay off full balance of loan – not eligible for loan forgiveness</p> <p>Payment increases every 2 years</p> <p>Payment must cover accrued interest but will never be more than three times greater than any other payment</p>
<p>Extended Fixed</p> <p>\$ 898.00 /mo</p> <p>300 months</p> <p>Not Eligible</p>	<p>Pay off full balance of loan – not eligible for loan forgiveness</p> <p>Fixed monthly payments</p> <p>Balance must be at least \$30,000</p>
<p>Extended Graduated</p> <p>\$ 697.00 /mo</p> <p>*First 2 years only 300 months</p> <p>Not Eligible</p>	<p>Pay off full balance of loan – not eligible for loan forgiveness</p> <p>Payment increases every 2 years</p> <p>Balance must be at least \$30,000</p> <p>Payment must cover accrued interest but will never be more than three times greater than any other payment</p>
<p>Revised Pay As You Earn (REPAYE)</p> <p>\$ 13.00 /mo</p> <p>*Based on current income 300 months</p>	<p>Repayment based on income and family size (must recertify each year)</p> <p>Monthly payment set at 10% of discretionary income (may be as low as \$0.00)</p> <p>Eligible for loan forgiveness (20 years for undergrads, 25 Years if ANY)</p>

<p>Pay As You Earn (PAYE)</p> <p>\$ 13.00 /mo</p> <p>*Based on current income 360 months</p> <p>Not Eligible</p>	<p>Repayment based on income and family size (must recertify each year)</p> <p>Monthly payment set at 10% of discretionary income (may be as low as \$0.00)</p> <p>Eligible for loan forgiveness (20 years)</p> <p>Must be a new borrower as of 10/1/2007</p>
<p>Income-Based Repayment (IBR)</p> <p>\$ 19.00 /mo</p> <p>*Based on current income 300 months</p> <p>Not Eligible</p>	<p>Repayment based on income and family size (must recertify each year)</p> <p>Monthly payment set at 15% of discretionary income (may be as low as \$0.00)</p> <p>Eligible for loan forgiveness (25 years)</p>
<p>IBR for New Borrowers</p> <p>\$ 13.00 /mo</p> <p>*Based on current income 360 months</p> <p>Not Eligible</p>	<p>Repayment based on income and family size (must recertify each year)</p> <p>Monthly payment set at 10% of discretionary income (may be as low as \$0.00)</p> <p>Eligible for loan forgiveness (20 years)</p> <p>Must be a new borrower as of 7/1/2014</p>
<p>Income-Contingent Repayment (ICR)</p> <p>\$ 234.00 /mo</p> <p>*Based on current income 300 months</p> <p>Consolidation Required</p>	<p>Repayment based on income and family size (must recertify each year)</p> <p>Monthly payment set at 20% of discretionary income (may be as low as \$0.00)</p> <p>Eligible for loan forgiveness (25 years)</p>


HELPFUL TIPS

- Public Service Loan Forgiveness (PSLF) is more flexible than Teacher Loan Forgiveness and unlike Teacher Loan Forgiveness, there is no cap on the amount forgiven. Full-time teachers at any elementary or secondary school, public or non-profit private, may meet the employment requirements. Under PSLF, the entire remaining balance on LISA's Direct Loans will be forgiven after 120 monthly payments have been made under a qualifying repayment plan. Only Direct Loans are eligible for PSLF.

AFTER DEBTOR CHOOSES A PROGRAM

- Push “apply” button, pay \$40.00, and Student Loanify will mail-merge applications based on the questions answered.
 - Consolidation application, choosing servicer
 - Income Based Repayment application
- Authorization to represent
 - Tip: mail separately.

AMERICAN BANKRUPTCY INSTITUTE

 **Federal Direct Consolidation Loan Application and Promissory Note**
William D. Ford Federal Direct Loan Program

OMB No. 1545-0053
Form Approved
Exp. Date 06/30/2018

WARNING: Any person who knowingly makes a false statement or misrepresentation on this form or any accompanying documentation is subject to penalties that may include fines, imprisonment, or both, under the U.S. Criminal Code and 20 U.S.C. 1097.

BEFORE YOU BEGIN

Read the Instructions for Completing the Federal Direct Consolidation Loan Application and Promissory Note ("Instructions").
NOTE: PAGES 1 THROUGH 5 MUST BE SUBMITTED FOR YOUR LOAN REQUEST TO BE PROCESSED.

BORROWER INFORMATION

1. Last Name: [REDACTED] First Name: Lisa Middle Initial: _____

2. Former Name(s): Lisa [REDACTED]

3. Social Security Number: [REDACTED] [REDACTED] [REDACTED]

4. Date of Birth: [REDACTED]

5. Permanent Address (Street, City, State, Zip Code) (if P.O. box or general delivery, see Instructions):
1848 [REDACTED], Clermont, Florida, 34711

6. Area Code/Telephone Number: (407) 894-6834

7. E-Mail Address (Optional): [REDACTED]

8. Driver's License State and Number: [REDACTED]

9. Employer's Name and Address (Street, City, State, Zip Code):
Orange County Public Schools, 445 West Amelia Street, Orlando, Florida, 32801

STUDENT LOANIFY PORTAL*

*PENDING APPROVAL IN THE MIDDLE DISTRICT OF FLORIDA AND NUMEROUS BANKRUPTCY COURTS

- Portal will assist with exchange of documents and direct communication.
- Cost to debtor \$40.00.
- Upload signed applications.
- Provide proof of income.
 - Tip: if only using borrower's income and not spouse, DO NOT provide joint return, use W2, paystub or profit and loss for self employed borrower.
- Authorization that firm represents borrower.

STUDENT LOANIFY AND PORTAL

- We hope these new tools will help make the student loan process easier!



SEPARATE CLASSIFICATION IN CHAPTER 11'S & 13'S

...somewhere between total whim and an Act of God lies the answer to what justification is needed to hew out a particular class of unsecured creditors and distinguish it from other unsecured creditors

- *In re Orawsky*, 387 B.R. 128, 141 (Bankr. E.D. Pa. 2008).

11 U.S.C. § 1322(b)(5)

(5) notwithstanding paragraph (2) of this subsection, provide for the curing of any default within a reasonable time and maintenance of payments while the case is pending on any unsecured claim or secured claim on which the last payment is due after the date on which the final payment under the plan is due;

11 U.S.C. § 1322 (b)(1)

(b) Subject to subsections (a) and (c) of this section, the plan may-

(1) designate a class or classes of unsecured claims, as provided in section 1122 of this title, but may not discriminate unfairly against any class so designated; however, such plan may treat claims for a consumer debt of the debtor if an individual is liable on such consumer debt with the debtor differently than other unsecured claims;

11 U.S.C. § 1122 provides:

(a) Except as provided in subsection (b) of this section, a plan may place a claim or an interest in a particular class only if such claim or interest is substantially similar to the other claims or interests of such class.

(b) A plan may designate a separate class of claims consisting only of every unsecured claim that is less than or reduced to an amount that the court approves as reasonable and necessary for administrative convenience.

11 U.S.C. § 1129(b)(1) provides:

Notwithstanding section 510(a) of this title, if all of the applicable requirements of subsection (a) of this section other than paragraph (8) are met with respect to a plan, the court, on request of the proponent of the plan, shall confirm the plan notwithstanding the requirements of such paragraph if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan.

Separate Classification/ 2 Views

Minority View:

A long-term nondischargeable student loan claim under § 1322(b)(5) is not subject to the unfair discrimination requirement of § 1322(b)(1).

In re Williams, 253 B.R. 220, 227 (Bankr. W.D. Tenn. 2000) (inclusion of unsecured creditors in (b)(5) indicates that it is a type of discrimination that is expressly contemplated and sanctioned by the Code).

Majority View:

A debtor may use § 1322(b)(5) to maintain long-term student loan payments only as long as the plan complies with the unfair discrimination prohibition set forth in § 1322(b)(1).

In re Brown, 500 B.R. 255, 265 (Bankr. S.D. Ga. 2013).

Policy Reasons for Separate Classification of Student Loan Debt

- (1) a debtor will not be afforded a fresh start in bankruptcy if the debtor is defaulting on student loan payments over the term of a 3-5 year plan, considering that on-going monthly plan payments are likely to be less than the amount owed on the student loan debt, interest is accruing, and the debts survive the debtor's discharge;
- (2) strong public policy supports the repayment of education loans;
- (3) Congress prefers Chapter 13 over Chapter 7, and debtors in Chapter 7 fare better with making post-bankruptcy payment on student loans debts because a Chapter 7 debtor will not have been in forced default of student loan debt obligations for 3-5 years; and
- (4) other unsecured creditors in Chapter 13 are not harmed by the preferential treatment for student loan debt because unsecured creditors must receive a return in Chapter 13 that is equivalent to what they would receive in Chapter 7 pursuant to 11 U.S.C. § 1325(a)(4).

In re Quinn, 586 B.R. 1 (Bankr. E.D. Mich. 2018).

What is “Unfair Discrimination?”

Historical View

The discrimination has a reasonable basis;
The debtor can carry out a plan without the discrimination;
The discrimination is proposed in good faith; and
The degree of discrimination is directly related to the basis or rationale for the discrimination.

In re Leser, 939 F.2d 669, 672 (8th Cir. 1991); *In re Wolff*, 22 B.R. 510, 512 (B.A.P. 9th Cir. 1982).

Emerging View

Totality Approach:
“because ‘unfairness’ is ultimately a discretionary determination, articulated multifactor tests applicable to all cases are not helpful and are incongruous with the nature of the required judicial process.”

In re Mason, 456 B.R. 245, 251 (Bankr. N.D.W.V. 2011).

Recent Authority

Successful Separate Classification

In re Kindle, 580 B.R. 443 (Bankr. D.S.C. 2017).

Student loan – 45%

Unsecured – 33% Dividend

In re Belton, No. 16-03040-JW, 2016 WL 7011570 (Bankr. D.S.C. Oct. 13, 2016).

Student Loan – Cure & Maintain

Unsecured – 11%

Unsuccessful Separate Classification

In re Quinn, 596 B.R. 1 (Bankr. E.D. Mich. 2018).

Student Loan – \$850.00 per month

Unsecured – 0%

SPECIAL CIRCUMSTANCES

- *In re Patterson*, 392 B.R. 497 (Bankr. S.D. Fla. 2008): student loan payments for adult daughter NOT a special circumstance.
- *In re Thompson*, 457 B.R. 872 (Bankr. M.D. Fla. 2011):
 - Debtors have not established this monthly payment is a necessary and reasonable expense for which there is no reasonable alternative.
 - They did not establish payment of the student loans cannot be deferred or placed in forbearance; the loans cannot be consolidated to yield a lower monthly payment; or they cannot lower their monthly payments through participation in the William D. Ford Federal Direct Loan Program for direct consolidation and income-contingent repayment.

PARTIAL LOAN STUDENT LOAN FORGIVENESS

***In re Metz*, 589 B.R. 750 2018
(Bankr. D. Kan. 2018).**

Court allowed the discharge of the interest portion of student loan debt in Chapter 13.

***In re Coplin*, No. 13-46108, 2017 WL 6061580 (Bankr.W.D. Wash. Dec. 6, 2017).**

Court allowed the discharge of student loan liability above \$222,000. Total student loan indebtedness was in excess of \$415,000.

WHEN TO BRING A DISCHARGEABILITY ACTION?

- *In re Brantley*, No. 15-81516-WRS, 2016 WL 3003429 (Bankr. M.D. Ala. May 17, 2016).
- Chapter 13 debtor's adversary proceeding to discharge her student loans pursuant to 11 U.S.C. § 523(a)(8) was not ripe because the issue of undue hardship should be considered at or near discharge.

ABI CONSUMER COMMISSION COMMENTS DOE'S RFI FOR EVALUATING UNDUE HARDSHIP

I. Promulgation and Interpretation of Regulations

(a) *Bright-line Rules*. Creditors should not oppose discharge proceedings where the borrower meets any of a set of the criteria below. These criteria should be set out in federal guidelines that indicate household financial distress and therefore undue hardship:

- (1) Disability-based guidelines
 - (2) Poverty-based guidelines
- (b) *Alternative Payment Plans*.

ABI COMMISSION RECOMMENDATIONS

II. Best Interpretation of 11 U.S.C. § 523(a)(8): *Brunner* should be understood to require the debtor to establish only that:

- (1) the debtor cannot pay the student loan sought to be discharged according to its standard ten-year contractual schedule while maintaining a reasonable standard of living,
- (2) the debtor will not be able to pay the loan in full within its initial contractual payment period (10 years is the standard repayment period) during the balance of the contractual term, while maintaining a reasonable standard of living, and
- (3) the debtor has not acted in bad faith in failing to pay the loan prior to the bankruptcy filing.

(b) *Standard of Proof*.

(c) *Appellate Review*.

BORROWER DEFENSE TO REPAYMENT

- Giving borrowers access to consistent, clear, fair, and transparent processes to file claims;
- Empowering the Secretary to provide debt relief to borrowers without requiring individual applications in instances of widespread misrepresentations;
- Protecting taxpayers by ensuring that financially troubled institutions provide the government with protection against the risks they create and that institutions whose actions lead to discharges of Federal student loans are held responsible;
- Helping students make more informed decisions by requiring proprietary schools with poor loan repayment outcomes to include a plain-language warning in their advertising and promotional materials;
- Ensuring affected borrowers have information about loan discharge when schools close and access to an automated process; and
- Banning schools from inducing students to sign pre-dispute arbitration agreements that waive their rights to go to court and bring class action lawsuits based on borrower defense claims.

BORROWER DEFENSE TO REPAYMENT

- The final regulations strengthen several provisions in response to public comment on the proposed regulations, including:
 - **Early Implementation of Automatic Closed School Discharge:**
 - The final regulations provide for the automatic discharge of the loans of borrowers whose school closed on or after Nov. 1, 2013 and have not re-enrolled in another Title IV participating institution within three years. The Department intends to designate this provision for early implementation as soon as operationally possible before July 1, 2017, which will allow eligible Corinthian borrowers to benefit from this streamlined process sooner.
 - **Banning All Pre-dispute Arbitration Agreements:**
 - The final regulations strengthen the limitations on pre-dispute arbitration agreements that prevent students from taking institutions to court by permanently banning any pre-dispute arbitration agreements for all Direct Loan borrowers for disputes related to the educational services provided or the making of Direct Loans, regardless of whether such clauses are a condition of enrollment. These provisions not only allow students to choose where to pursue claims against an institution after claims arise, but also prohibit institutions from banning class action lawsuits by students.
 - **Determining Borrower Defense Loan Relief:**
 - The final regulations make clear that the Department will determine in a reasonable and practicable way the appropriate relief for a borrower defense claim, taking into account any educational benefit received.

VALUATION ISSUES

VALUATION OF VEHICLE

- *In re Reid*, 8:17-bk-09503-RCT, June 28, 2018.
- Issue: what is meaning of “personal use” as used in the hanging paragraph of § 1325(a) in allowing cramdown of a 910 vehicle?
- Debtor stated reason for purchase of the vehicle was to become an Uber driver. With the exception of one long distance road trip, a larger percentage of the mileage was accrued while driving for Uber.
- Judge Colton identified 3 approaches: (1) significant contribution = any amount of personal use is allowed as long as the vehicle is used to drive to and from work that generates income (liberal); (2) significant and material = anything more than nominal personal use negates business use, no matter how important or necessary the vehicle is for performance of debtor’s business or job (conservative); (3) predominate use = vehicle used to travel to and from work, or is it used to perform the actual functions of the job (Goldilocks position).
- Documents such as purchase agreement and registration were not dispositive. Debtor actually used the vehicle to perform her work as ride share driver.
- Court noted that terms *solely*, *exclusively*, *mostly*, *primarily*, *partially*, or any other quantitative words were included in the hanging paragraph.
- Debtor was allowed to cramdown the vehicle.

VALUATION OF HOA

- *In re Roseman*, 8:16-bk-07215-RCT, October 23, 2018.
- Issue: Does an HOA discharged in a prior Chapter 7 have an allowed unsecured claim payable through a subsequent Chapter 13?
- In the Chapter 13, the debtor filed an unopposed motion to strip lien of HOA. Order entered contained standard language regarding treatment as an unsecured claim.
- The debtor objected to HOA POC as it included the amount discharged in the Chapter 7. The creditor defends that its *in rem* rights entitled it to be treated as unsecured for the full amount, including the discharged amount.
- Court rules for the debtor. The creditor's position would effectively revive her *in personam* liability on the discharged amount, effectively converting the debt from nonrecourse to recourse. Court elaborates that having a claim is not the same as having an allowed claim. Once the order was entered stripping the creditor of its lien rights, the claim is not enforceable and is disallowed. Further, the Court points out that Congress provided for the conversion of nonrecourse debt into recourse in Chapter 11, but specifically omitted that provision in Chapter 13.

RECENT CASES

MORTGAGE PAID OUTSIDE THE PLAN

- *Dukes vs Suncoast Credit Union (In re Dukes)*, 909 F.3d 1306 (11th Cir. 2018).
- When the debtor filed Chapter 13, she had a first and second mortgage on her homestead with Suncoast. The plan stated that debtor would pay Suncoast directly rather than through the Chapter 13 Trustee. The plan was completed and discharged “all debts provided for under the plan.” During the course of the plan, the debtor defaulted on the two mortgages. Suncoast reopened the case to file an adversary to declare that the debtor’s personal liability on the first mortgage had not been discharged.
- Bankruptcy Court and District Court found that debt was not discharged as it was not “provided for under the plan.” Debtor appealed, 11th Circuit affirmed.
- Court pointed to § 1328(a), finding the plan must make a provision for or stipulate to the debt in the plan. Because the debtor’s plan did nothing more than state that it would be paid outside the plan, it was not “provided for” and not discharged. The plan’s terms must in some way affect or govern the debt’s repayment. Mere reference was only clarification of what was included and excluded from the plan. Further, even if it was “provided for,” discharge would violate § 1322(b) by modifying Suncoast’s rights under the loan documents to obtain a deficiency judgment.

CMI AND 100% PAYMENT OF CREDITORS

- *In re McKinney*, No. 18-70417-BHL-13, 2018 WL 4378655 (Bankr. S.D. Ind. Sept. 13, 2018) {via Michael Barnett’s blog}.
- Issue: If the debtor’s CMI exceed amount necessary to pay 100% to allowed unsecured claims, must the debtor pay interest if he chooses to pay less than CMI monthly?
- Chapter 13 Trustee asserts that § 1325(b)(1) requires debtor to pay all projected disposable income into the plan, or to pay the present value of unsecured claims which would require the payment of interest.
- Court looks to meaning of “as of the effective date of the plan.” A distinction is made of the use of the phrase “the value, as of the effective date of the plan, of property to be distributed” as in § 1129(a)(7), § 1225(a)(4), § 1325(a)(4), etc. This phrase is interpreted to require a present value analysis of the proposed payments.

CMI AND 100% PAYMENT OF CREDITORS - Continued

- HOWEVER, when the phrase “as of the effective date of the plan” is moved, it arguably reflects an intentional legislative distinction, reflecting the different justifications for paying interest. Unlike secured creditors or unsecured creditors in a solvent Chapter 7, unsecured creditors in Chapter 13 have no right to immediate payment in full at the front end of the case. Given the lack of a forced deferral of a pre-existing payment right, there is no entitlement to interest. Placement of the phrase “as of the effective date of the plan” outside of § 1325(b)(1)(A) may have been to prevent courts misconstruing such section as requiring a present value requirement. The only interpretation of such placement as applied to both subsections (A) and (B) is that the date as of which the court is to determine whether (A) or (B) is applicable and satisfies the Trustee’s objection. The contrary interpretation would lead to the anomalous result of paying interest to general unsecured claims even though § 1322(a)(2) allows for deferred payment of priority claims without interest.
- Court allows payment without interest.

PAYMENT OF EDUCATION EXPENSES AS FRAUDULENT TRANSFERS

- *In re Serman*, No. 16-10378(MG), 2018 WL 6333588 (Bankr. S.D.N.Y. Dec. 4, 2018).
- Issue: Is the debtors’ payment of daughters’ college tuition, books and supplies, and room and board while students in college constructive fraudulent transfers made to or for the benefit of the daughters?
- Under New York law, a conveyance is fraudulent if it is incurred without “fair consideration.” The standard under Florida Law and the Bankruptcy Code is “reasonably equivalent value.” Fla. Stat. § 726.105; 11 U.S.C. § 548(a)(1)(B). Courts have found that the term does not require the exchange to be “mathematically equal,” but “purely emotional benefits, such as love and affection” will not suffice.
- Trustee asserts that payments made for their children after the age of majority are constructively fraudulent. Daughters defend that parents received an economic benefit because a college degree would increase the likelihood they would be self-sufficient.
- The court lands on the age of majority as determining whether a parent has a legal obligation to support their child, including education expenses. In New York, the age of majority is stated to be 21. [Florida is 18. Fla. Stat. § 743.07]. Any costs paid within the lookback period and prior to the daughter turning 21 were found to not to be constructive fraudulent transfers, as reasonable equivalent value was given.

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