I. EFFECTUATING THE FRESH START

A. Discharge and Dischargeability

§ 1.01 Student Loans

(a) Bankruptcy Code Amendments.

(1) Section 523(a)(8) should except from discharge only student loans that

(A) were made, insured, or guaranteed by a governmental unit,

(B) were incurred for the debtor's own education, and

(C) absent a showing of undue hardship, first became payable less than seven years before the bankruptcy case was filed, regardless of any suspension of payments.

(2) Section 507(a) should have a new, eleventh priority for claims excepted from discharge under § 523(a)(8).

(3) Section 1322(a) should allow the plan to provide for less than full payment of all amounts owed for a claim entitled to the student loan priority only if the plan provides that all of the debtor's projected disposable income for a five-year period beginning on the date that the first payment is due under the plan will be applied to make payments under the plan.

(4) Section 1322(b)(10) should provide that it does not apply to priority unsecured debts.

(b) Promulgation and Interpretation of Regulations. Through regulations or interpretive guidance, the Department of Education should provide the following with respect to governmental student loans:

(1) 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:

(A) 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.

(B) Poverty-based guidelines.

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

(ii) 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.

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

(3) 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.

(c) Best Interpretation of Current Law.

(1) Standard for Dischargeability.

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

(i) 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,

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

(iii) 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 whether to appeal by the Department of Education, any guaranty agency, eligible lender, or holder of a federal student loan, and any agent of these parties.

(2) Treatment of Nondischargeable Student Loans in Chapter 13.

(A) Section 1322(b)(1) should be interpreted to allow separate classification and payment of nondischargeable student loans at a higher dividend than other general unsecured claims as long as the other unsecured claims are paid at least as much as is required under the best interest test of § 1325(a)(4), including cases where the best interest test would not require any payment.

(B) If precedent requires rejection of the recommendation in subparagraph (A) and a higher payment of nondischargeable student loans is held not to be generally available under § 1322(b)(1), courts should use the following best interpretations:

(i) If another person is liable for payment of a nondischargeable student loan, § 1322(b)(1) should be interpreted to allow a plan to provide for its payment at a higher rate than other general unsecured claims, as long as the other unsecured claims are paid at least as much as is required under the best interest test of § 1325(a)(4), including cases where the best interest test would not require any payment;

(ii) Section 1322(b)(5), providing for the cure and maintenance of long-term unsecured claims, should be interpreted to apply to student loans; and

(iii) Section 1322(b)(10), disallowing payment of interest on nondischargeable debts, should be interpreted as not applying to claims being treated under § 1322(b)(5).

Scope of the Problem. 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 today.[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 both.[2] Among all types of household debt, student loans have the highest delinquency rate.[3] The most recent data show 10.9% of student loans as 90+ days delinquent,[4] and various reports suggest that the true default rate is higher because government figures look only at defaults in the first three years after graduation.[5]

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) lower earnings of college graduates,[6] (2) lower levels of homeownership,[7] (3) lower automobile purchases,[8] (4) higher household financial distress,[9] (5) lower probability of students choosing public-service careers,[10] (6) poorer psychological functioning,[11] (7) delayed marriage,[12] and (8) lower probability of continuing education through graduate school.[13] Student loan debt thus affects not only those who owe the loans but also has consequences that ripple through our communities and our nation.

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1 These figures are from calculations based on 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 (2018:Q2), at 3 (Aug. 2018) https://www.newyorkfed.org/medialibrary/interactives/householdcredit/data/pdf/HHDC_2018Q2.pdf.

3 *See id.* at 12-14.

4 *Id*. at 1.

5 *See* Kristen Blagg, "Underwater on Student Debt," (Aug. 2018) (https://www.urban.org/research/publication/underwater-student-debt/view/full_report); Ben Miller, "Getting Repayment Rates Right," Center for American Progress (July 10, 2018) https://www.americanprogress.org/issues/education-postsecondary/reports/2018/07/10/453199/getting-repayment-rates-right/; Judith Scott-Clayton, "The Looming Student Debt Crisis Is Worse Than We Thought," Economic Studies at Brookings (Jan. 10, 2018), https://www.brookings.edu/wp-content/uploads/2018/01/scott-clayton-report.pdf.

6 *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.

7 *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.

8 *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.

9 *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).

10 *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).

11 *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).

12 *See* Dora Gicheva, *Student Loans or Marriage? A Look at the Highly Educated*, 53 Econ. Educ. Rev. 207 (2016).

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

History. Congress first excepted student loans from the bankruptcy discharge in the Education Amendments of 1976.[14] A debtor in bankruptcy could discharge a student loan after five years had passed since the beginning of the repayment period, not counting any period during which repayment had been suspended. Before the end of the five-year period, a debtor could discharge a student loan only upon a showing of undue hardship to the debtor or the debtor's dependents. To be excepted from the discharge, the student loan had to be (1) from certain financial institutions like a bank, a state agency, an institution of higher education, or a vocational school, and (2) insured by the federal government, a state government, or a nonprofit private institution. This amendment went into effect on September 30, 1977.[15]

When Congress enacted the Bankruptcy Code in 1978, section 523(a)(8) retained the basic rule that a student loan was freely dischargeable after five years and dischargeable before that time upon a showing of undue hardship.[16] There were a few changes. The nondischargeability provision applied to any debt to a "governmental unit, or a nonprofit institution of higher education, for an educational loan." Gone was the requirement that the loan be insured, although because at the time most every student loan was insured, the change made little practical difference. The Bankruptcy Code framed the undue-hardship standard as whether there was an undue hardship on the debtor *and* the debtor's dependents, arguably a change from the previous rule that required a showing of undue hardship either as to the debtor *or* the debtor's dependents. The Bankruptcy Code now measured the running of the five-year period as beginning when the student loan "first became due" and did not toll the running of the period during any time payment was suspended. Finally, and most importantly, student loans were dischargeable in chapter 13 through its "superdischarge" (presuming the loan was "provided for by the plan").[17]

The next major legal development happened not through a legislative enactment but through decisional law. Marie Brunner graduated in 1982 with a master's degree in social work and $9,000 in student loans. Less than a year later, she filed bankruptcy. The bankruptcy court allowed a discharge, finding undue hardship in Ms. Brunner's "shaky finances and her unsuccessful efforts to find work following her graduation."[18] The Second Circuit rejected Ms. Brunner's attempt to get an early discharge of her student debt. In doing so, the Second Circuit announced what has become the widely accepted *Brunner* test to define undue hardship:

> (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

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14 Pub. L. No. 94-482, § 127, 90 Stat. 2081, 2141 (adding section 439A to the Higher Education Act of 1965).

15 *See* Alan M. Ahart, *Discharging Student Loans in Bankruptcy*, 52 Am. Bankr. L.J. 201, 202-03 (1978).

16 Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, § 109(e), 92 Stat. 2549, 2591.

17 *See id.* § 1328(a)(2) (discharging all debts provided for by a chapter 13 plan except for debts specified in § 523(a)(5)).

18 Brunner v. New York State Higher Educ. Serv. Corp. *(In re* Brunner*)*, 46 B.R. 752 (S.D.N.Y. 1985), *aff'd*, 831 F.2d 395 (2d Cir. 1987).

(3) the debtor has made good faith efforts to repay the loans.[19]

The Second Circuit noted that there was no evidence that Ms. Brunner's "current inability to find any work will extend for a significant portion of the loan repayment period. She is not disabled, nor elderly. . . . No evidence was presented indicating a total foreclosure of job prospects in her area of training."[20] With the congressional judgment at the time of *Brunner* that a debtor could freely get a discharge for student loans after five years, a strict "undue hardship" standard was understandable.

Congress next acted in 1990, lengthening the period before a student loan became freely dischargeable from five years to seven years after it first became due.[21] In a separate statute, Congress also removed student loans from chapter 13's "superdischarge," meaning debtors now could not freely obtain an early discharge of a student loan in either chapter 7 or chapter 13.[22]

The most significant development for the treatment of student loans in bankruptcy occurred in 1998 when Congress eliminated the time period after which student loans became freely dischargeable.[23] The rule now became that student loans were nondischargeable at any time unless the debtor made a showing of undue hardship. By this time, however, a substantial body of case law had developed, primarily using the *Brunner* test, that defined what a debtor must show to establish undue hardship. The courts had developed this case law under the prior statutory structure but now began applying it in the different context of nondischargeability without a time limit.

In 2005, Congress again added to the definition of student debt that could not be discharged in bankruptcy. For the first time, even private educational loans became nondischargeable in bankruptcy.[24]

Underlying the legal developments has been a belief that student loans have different characteristics from other types of debts that merit exception from the bankruptcy discharge. First, educational lending often enables increased earning power and supposes graduates will use that earning power to repay the loan. Having a procedure that allows graduates to walk away from that debt, especially soon after graduation, particularly increases the moral hazard risk from nonpayment in ways that are not present for other types of debt. Second and relatedly, it offends a sense of fairness to allow nonpayment of a debt

19 Brunner v. New York State Higher Educ. Serv. Corp. *(In re* Brunner*)*, 831 F.2d 395 (2d Cir. 1987).

20 *Id.* at 396-97.

21 *See* Crime Control Act of 1990, Pub L. No. 101-647, § 3621, 104 Stat. 4789, 4965. Congress also added "an educational benefit overpayment" and "an obligation to repay funds received as an educational benefit, scholarship or stipend" to the types of student loan debts excepted from the bankruptcy discharge. *Id.* 4964-65.

22 *See* Omnibus Budget Reconciliation Act of 1990, Pub. L. No. 101-508, § 3007(b)(1), 104 Stat. 1388, 1388-28. This provision was originally set to expire in 1996, *id.* § 3008, 104 Stat. at 1388-29, but was made permanent in 1994, *see* Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 501(d)(38)(A), 108 Stat. 4106, 4147.

23 *See* Higher Education Amendments of 1998, Pub. L. No. 105-244, § 971(a), 112 Stat. 1581, 1837.

24 *See* Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 220, 119 Stat. 23, 59. The definition, codified at § 523(a)(8)(B), refers to any educational loan that is a "qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986," a category that includes educational loans made by private entities regardless of whether they have a governmental or nonprofit insurance guaranty.

that enabled a higher income.[25] Third, nondischargeability of student loans may be important to protect the solvency of the governmental student loan program.[26]

Retention of Nondischargeability. The Commission weighed the reasons for student loan nondischargeability against the problems that massive amounts of student loan debt are creating for American households today. The Commission considered but rejected the notion of making student loans freely dischargeable like any other debt, concluding that the rationales supporting nondischargeability remain valid. Funding of sources for educational lending is essential to the system of higher education, and increased earnings resulting from higher education will often allow a student to repay loans that are initially quite large. If reasonably applied,[27] *Brunner*'s three-factor undue-hardship standard can allow appropriate bankruptcy relief during a period when discharge of student loans is not otherwise available. The Commission's recommendations are intended as a package and represent a practical, middle-ground approach that will provide meaningful changes while respecting the traditional protections for student loans.

Statutory Amendments — Return to the Seven-year Rule. The centerpiece of the Commission's recommendation is to return to the pre-1998 rule that allowed student loans to be discharged after seven years from the time they first became payable. Before seven years, student loans would be dischargeable only upon a finding of undue hardship. The rationales for nondischargeability lose their force after a student loan has been outstanding for a significant time. If a debtor cannot obtain sufficiently lucrative employment to repay a student loan that has long been outstanding, it is unlikely the debtor's circumstances will change to allow significant repayment of the student loan. For loans that have been long outstanding and have become delinquent, it is more likely that the overhang of substantial student loan debt will prevent the debtor from engaging in productive economic activity, diminishing the debtor's contribution to the community, such as by establishing a household and supporting the tax base.

The Commission considered different time periods after which a student loan could be freely discharged. Some commissioners thought five years or less might be appropriate, while others believed much longer time periods were appropriate. Drawing on the experience from the pre-1998 law, the Commission decided a seven-year period best balanced the need for payment and the need to encourage economic activity by the debtor. A seven-year period is 70% of the initial ten-year repayment period for a student loan.

Statutory Amendments — No Protection for Nongovernmental Loans. The Commission recommends that only student loans made, insured, or guaranteed by a governmental unit receive any protection from discharge. Governmental student loan programs advance the public policy of making higher education widely available and generally must make their loans available to anyone who qualifies, without regard to underwriting criteria. When making student loans, the government cannot choose only the most creditworthy borrowers. Failure to repay these loans can threaten the viability of government student loan programs.

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25 *See, e.g.*, T.I. Federal Credit Union v. DelBonis, 72 F.3d 921, 936 (1st Cir. 1995) ("It is undisputed that Section 523(a)(8) was enacted to prevent abuses in student loan programs."); *In re* Pelkowski, 990 F.2d 737, 742-43 (3d Cir. 1993) (citing House floor statements).

26 *See, e.g., Pelkowski*, 990 F.2d at 743 (citing House floor statements).

27 *See infra* notes 43-53 and accompanying text.

In contrast, private student loans are underwritten in a similar fashion to other unsecured debt, and the interest rates charged on the loans can reflect the risk of loss associated with these obligations. As with any participant in a consumer lending market, private student lenders may require co-signers and security to protect their loans. BAPCPA added private student lenders to those protected from discharge. Academic research, however, suggests that this change did not lead to lower interest rates for student borrowers[28] and was not necessary given the lack of strategic default in the private student loan market before BAPCPA.[29] The Commission therefore recommends that Congress should return section 523 to its pre-2005 state where private student loans did not receive any dischargeability exception.

Statutory Amendments — Protecting Nonstudent Debtors. The Commission also recommends that section 523(a)(8) should limit nondischargeability to student loans owed by the student who benefitted from the loan, rather than by third parties. Third parties — guarantors or suppliers of collateral — would not have benefitted from the loans, and if they are otherwise in need of bankruptcy relief, they should not have their discharge impaired by their support of the student who did benefit.

Statutory Amendments — Priority for Student Loan Debt and Treatment in Chapter 13. Loans that are excepted from discharge should be a priority claim under section 507, specifically a new eleventh priority, which would be the lowest bankruptcy priority. Thus, student loans excepted from discharge would be paid after all other priority claims but before general unsecured creditors.

The Commission recommends this priority for two reasons. The first is to further the goal of obtaining payment of governmental student loans, allowing for distribution of a greater share of the estate in a chapter 7 case where there are distributions to creditors.

Second, and more importantly, giving nondischargeable student loans a priority will improve their treatment in a chapter 13 plan. Student loans are general unsecured debts. Although a chapter 13 plan may designate separate classes of unsecured claims, the plan may not "discriminate unfairly" against any class.[30] Some chapter 13 debtors have separately classified their student loan debt to provide for greater payments on the student loan debt as compared to other unsecured debts. Although as discussed below the Commission believes the better interpretation of existing law is that such separate treatment is not "unfair," some courts have found otherwise.[31]

But regardless of whether student loans can be classified separately as nonpriority claims, a plan can separately classify a priority claim. As *Collier* explains, "there can be no doubt that a plan may separately classify priority claims."[32] A priority reflects a congressional judgment that the type of claim merits

28 Alexei Alexandrov & Dalié Jiménez, *Lessons from Bankruptcy Reform in the Private Student Loan Market*, 11 Harv. L. & Pol'y Rev. 175 (2017).

29 *See* Rajeev Darolia & Dubravka Ritter, *Strategic Default Among Private Student Loan Debtors: Evidence from Bankruptcy Reform* (2017), https://ssrn.com/abstract=3064662.

30 11 U.S.C. § 1322(b)(1).

31 *See infra* notes 54-58 and accompanying text.

32 8 Collier on Bankruptcy ¶ 1322.05 (16th ed. Richard Levin & Henry Sommer eds.).

payment before other general unsecured claims. Carrying through that priority into the chapter 13 plan not only furthers the policy goal of repayment of federally backed student loans but also helps further the debtor's fresh start by reducing the amount of nondischargeable debt that will remain after the chapter 13 case ends.

Section 1322(a)(2) requires that any priority debt be paid in full through the chapter 13 plan. Section 1322(a)(4) excepts domestic support obligations owed to a governmental unit from the payment-in-full requirement because many debtors might owe a large enough amount of domestic support debt to a government unit that it would be impossible to pay the debt in full during the three- to five-year life of a chapter 13 plan.[33] Nondischargeable student debt similarly can be large, and in conjunction with giving student loan debt a priority, the Commission recommends a coordinating amendment to section 1322(a)(4) to except priority student loan debt from the payment-in-full requirement.

Finally, section 1322(b)(10) prohibits payment of interest on nondischargeable unsecured claims unless all claims are paid in full. This rule conflicts with section 1322(b)(5), which allows for curing and maintaining current payments on loans for which the last payment is due after the end of the plan. To maintain the current payment requires payment of the interest on it, meaning a debtor cannot comply with both section 1322(b)(5) and (b)(10) in regard to interest payments on long-term nondischargeable debts where the last payment is scheduled for after the plan completion date (like student loans). Congress should make conforming amendments to section 1322(b)(10), which would mean eliminating the exception clause (i.e., all the language that currently appears in 1322(b)(10) after the phrase "except that").

Regulatory Changes — Bright-Line Rules.[34] 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.

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 has both caused the federal government to incur substantial costs in the bankruptcy collection process with little recovery and has left bankrupt borrowers without effective relief. It is in the interest of the federal government and borrowers that the government use 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.

33 *Id.* ¶ 1322.05[5].

34 The Commission released its recommendations on regulatory changes for student loan debt in a letter that responded to Department of Education, Request for Information on Evaluating Undue Hardship Claims in Adversary Actions Seeking Student Loan Discharge in Bankruptcy Proceedings, 83 Fed. Reg. 7460 (Feb. 21, 2018). The Commission's letter can be found at https://www.regulations.gov/document?D=ED-2017-OPE-0085-0378.

Our recommendations suggest two sets of bright-line rules,[35] 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. The Commission recommends that the Department of Education through regulations or interpretive guidance provide that student loan creditors should not oppose the dischargeability of student loans of persons (i) who are eligible for Social Security or veterans disability benefits or (ii) who fall below certain poverty-level thresholds.

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.”[36] 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 guidelines.[37]

Our second set of guidelines are built around the federal poverty guidelines. The most recently revised federal poverty guidelines are:[38]

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 in two situations: retirees on fixed incomes, and persons providing support for an elderly, chronically ill, or disabled household or family member.

35 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.

36 42 U.S.C. § 423(d)(1).

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

38 *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.

Determinations of disability by the Department of Veterans Affairs or the Social Security Administration can serve as grounds for an administrative forgiveness of student loan debt,[39] but that does not eliminate the need for judicial alternatives 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. The administrative and judicial remedies can be equally effective. Just as there is no reason for the Department of Education'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 Department of Education should respect the choice the borrower makes in addressing debt problems.

Regulatory Changes — 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."[40] If so, the discharge petition should not be opposed. Despite the regulation's directive, it is the sense of the Commission that student loan collectors have often vigorously litigated student loan discharge proceedings regardless of the costs and benefits 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 resort, not the first. 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 a discharge of the student loan debt.

Regulatory Changes — 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 from borrowers under "exceptional circumstances."[41] The safeguards built into the confirmation of a chapter 13 plan set out statutory requirements more stringent than the Department of Education's income-driven repayment plans, including a liquidation analysis that is not otherwise considered by the Department of Education. 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.[42] Section 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

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39 *See* 34 C.F.R. §§ 685.212(b), 685.213.

40 *Id.* § 682.402(i)(1)(iii).

41 *Id.* § 685.208(l)(1).

42 *Id.* §§ 685.211(f), 685.220.

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 toward 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). Finally, the Department of Education 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 forgo administrative costs under 34 C.F.R. § 30.60 and penalties assessed under 34 C.F.R. § 30.61.

Best Interpretation — Section 523(a)(8). As discussed above,[43] many courts have interpreted the undue-hardship standard using a three-factor test known as the *Brunner* test.[44] 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.[45]

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43 *See supra* notes 18-20 and accompanying text.

44 The Eighth Circuit uses a "totality of the circumstances" test. *See* Long v. Educational Credit Mgmt. Corp., 322 F.3d 549 (8th Cir. 2003). The Commission's recommendations apply to whichever judicial test is used.

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

For example, the second of these *Brunner* 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.[46]

Because of the *Brunner* test's strictness, seemingly dire financial circumstances sometimes are not enough to constitute "undue hardship." For example, in *In re Oyler,* a pastor who was married with three dependent children claimed that repayment of his $40,000 in student loans would be an undue hardship. The pastor suffered from a medical condition that had caused four retinal detachments, but the family had no health insurance.[47] Although his annual income was less than $10,000 and well below the poverty line for a family of five, the court of appeals ruled the student loan could not be discharged because the debtor had not sought the highest paid possible work for which he was qualified.[48] With such strict judicial case law, few debtors have sought to discharge student loans in bankruptcy.[49]

The Commission recommends that courts properly understand the *Brunner* test by hewing closely to the statute, as appropriate judicial interpretive techniques require. Section 523(a)(8) directs the court to consider "the debt" and not some different contract the debtor and creditor might have made under different circumstances. Thus, the court should consider whether the debtor can repay within the contractual term of the loan, which is typically ten years. The statutory language suggests other interpretive guideposts for what constitutes "undue hardship" under section 523(a)(8):

> (a) Courts 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.[50]
>
> (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.[51]
>
> (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.[52]

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

47 *Oyler*, 397 F.3d at 384.

48 *Id.* at 386.

49 *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.").

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

51 *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).

52 *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).

> (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.[53]

Because the open-ended nature of the *Brunner* inquiry cannot account for all situations that might arise, the Commission recommends a best interpretation of the third *Brunner* factor that incorporates the concept of bad faith. The court should deny discharge to a student loan only where the debtor has acted in bad faith in failing to make loan payments before filing bankruptcy.

Best Interpretation — Section 1322 and Chapter 13 Plans. As discussed above, the Commission has recommended a statutory amendment to give nondischargeable student loans a priority in bankruptcy. With a priority, nondischargeable student loans clearly could be classified separately from other unsecured debt and treated differently under the chapter 13 plan.[54] Although such treatment might discriminate among classes, it would not run afoul of section 1322(b)(1)'s prohibition against *unfair* discrimination, as the priority would itself be a reason for the separate classification.

If Congress does not amend the Bankruptcy Code to give nondischargeable student loans a priority, the Commission believes the best interpretation of section 1322(b)(1) still allows separate classification of student loans. Unsecured creditors always are protected by section 1325(a)(4)'s best-interest test, which ensures they receive at least as much under the chapter 13 plan as they would have received had the debtor filed under chapter 7.

Like priorities, nondischargeability represents a congressional judgment that a debt merits special treatment. In the context of student loans, the nondischargeability provision also furthers the protection of the public fisc and the solvency of student loan programs. Allowing separate classification promotes repayment of student loans and indeed directly furthers the congressional reasons behind nondischargeability. It is not unreasonable to prefer a student loan in the chapter 13 plan. Allowing separate classification also lets the debtor pay down a nondischargeable debt and promotes the debtor's fresh start.

Only the most wooden interpretive methods ignore the context of their times. The Commission found persuasive Judge Berger's explanation in *In re Engen*[55] of why the context of student loans is different today than it was when the nondischargeability rules first came into effect:

> Student loans are different because unlike other nondischargeable debts, it is not the debtor's misconduct in acquiring the loans that supports nondischargeability. . . . [T]he idea that student loans are nondischargeable to avoid fraud and a free ride is inaccurate.

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53 *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.").

54 *See supra* note 32 and accompanying text. Section 1322(a)(3) requires the same treatment of claims within a class. Therefore, if a debtor wishes to provide a different payment for student loans, a separate classification would be necessary.

55 561 B.R. 523 (Bankr. D. Kan. 2016).

> The Code already contains ample provisions to address fraud and debtors are allowed to keep other services or property acquired on unsecured credit. Further . . . student loans are unlike other types of § 523(a) debt where the dischargeability rationale is based on society's interest in preventing mischievous debtors from usurping prior bad acts.
>
> Student loans are also different because Congress has an interest in protecting the fiscal health of the federal student loan program. In furtherance of this goal, the government has enormous collection powers on federal student loans.
>
> Further, "[u]nlike any other type of debt, there is no statute of limitations. The government can pursue borrowers to the grave." . . . Conversely, the Internal Revenue Service generally may only pursue collection on assessed taxes "within 10 years after the assessment of the tax."
>
> Originally, the federal student loans were "intended as a program of last resort for college students seeking to finance their educations." . . . Now, "[n]o longer can the average student from the lower middle classes hope to enter and exit a postsecondary institution with a valuable degree without, to some extent, participating in the guaranteed student loan program." . . .
>
> As of June 30, 2016, outstanding student loan debt reached $1.259 trillion and comprised ten percent of household debt—ahead of credit card debt at six percent and automobile debt at nine percent. To place this aggregate student loan balance in perspective, it exceeds the annual gross domestic product of all but the 11 largest economies in the world, including the economies of Russia, Spain and Mexico. . . . The massive shift of the skyrocketing costs of college education to the middle class over the last three decades has replaced the decreased government subsidization of public colleges and universities. It is accurate to classify student loan debt as singular in identity since borrowers are in effect compensating for the reduced tax revenue allocated to post-secondary education.[56]

The Commission recognizes that precedent may bind some lower courts to hold that separate classification and a higher payment to student loans are not generally available. The Commission believes the appropriate court should reconsider any such precedent. But even where separate classification is not generally available, current law should be interpreted to permit higher payments in two situations:

> 1. Where a party other than the debtor is liable on the student loan, such as by co-signing or guaranteeing the debt, section 1322(b)(1) expressly allows treatment different from other unsecured claims. This provision is applicable on its face to co-signed or guaranteed student loans.[57]

56 *Id.* at 545-48 (citations omitted).

57 *See In re* Russell, 503 B.R. 788, 798 (Bankr. S.D. Ohio 2013) (allowing greater payment of co-signed student loans, observing that "a disparity—even a large one—between the dividend paid on such claims and the dividend paid on other unsecured claims does not itself constitute unfair discrimination").

> 2. Where the last payment on an unsecured claim is due after the date on which the final payment under the plan is due, section 1322(b)(5) allows a chapter 13 plan to cure any default in payments of the claim and maintain current payments. This provision should be interpreted as fully applicable to student loans.[58]

Because section 1322(b)(10), by prohibiting payment of interest on nondischargeable unsecured claims in the absence of full payment of all claims, conflicts with § 1322(b)(5), it should be held inapplicable to student loan claims being treated through cure and maintenance.[59]

58 *See In re* Truss, 404 B.R. 329, 332 (Bankr. E.D. Wis. 2009).

59 *See In re* Brown, 500 B.R. 255, 269 (Bankr. S.D. Ga. 2013).