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## Essay

# Changing the Student Loan Dischargeability Framework: How the Department of Education Can Ease the Path for Borrowers in Bankruptcy

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## INTRODUCTION

The United States' consumer bankruptcy system supposedly gives "honest but unfortunate" individuals "a new opportunity in life with a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt."<sup>1</sup> Access to bankruptcy's discharge of debt is especially important in the wake of the COVID-19 pandemic, which has resulted in a once-in-a-century economic crisis that is projected to increase bankruptcy filings by people struggling to recover.<sup>2</sup> Those who file bankruptcy will find a system that is already difficult to navigate and has long-recognized racial and gender disparities in access and outcomes.<sup>3</sup>

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1. *Grogan v. Garner*, 498 U.S. 279, 286–87 (1991) (quoting *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934)), *superseded by statute*, Pub. L. No. 107-204, 116 Stat. 801 (2002), *as recognized in* *Osborne v. Kakas*, No. 4:17-CV-00254-JRG, 2018 WL 1354792, at \*4 (Feb. 15, 2018).

2. See Pamela Foohey, Robert M. Lawless, & Deborah Thorne, *Portraits of Bankruptcy Filers*, 56 GA. L. REV. (forthcoming 2022) (manuscript at 1–2), <https://ssrn.com/abstract=3807592> [<https://perma.cc/7FYA-AK4Z>].

3. See *generally id.* (describing who files bankruptcy and barriers to access); Paige Marta Skiba, Dalié Jiménez, Michelle McKinnon Miller, Pamela Foohey, & Sara Sternberg Green, *Bankruptcy Courts Ill-Prepared for Tsunami of People Going Broke from Coronavirus Shutdown*, THE CONVERSATION (May 13, 2020), <https://>

Student loan borrowers will find a system with even more barriers to relief from their education debt. These barriers are two-fold: some are implemented by bankruptcy laws, while others are put up by loan holders—including the United States Department of Education (Department). This Essay focuses on how the Department should update its policies for how it responds to borrowers who seek to discharge their student loans in bankruptcy.

As discussed in Part I, the Department’s current policies for determining whether and how to contest a borrower’s request for discharge of student loans rely on an overly rigid application of case law regarding education loan dischargeability. These policies result in the Department wasting resources to contest discharge requests that likely will yield the Department little recovery.<sup>4</sup> It also unnecessarily leads the Department to hurt individuals and families struggling to get out from under unmanageable debts.<sup>5</sup>

Part II details two options for how the Department can update its approach to bankruptcies to ensure that it calibrates its actions to make the promise of a fresh start more real for student borrowers. Importantly, the Department can implement the framework set forth in this Essay without substantially negatively impacting the net amount of money that it is likely to recover from borrowers who file bankruptcy and seek to discharge their student loans.

#### I. THE DEPARTMENT’S ROLE IN CURRENT BARRIERS TO STUDENT LOAN DISCHARGE

The Bankruptcy Code provides that student loans are presumptively non-dischargeable.<sup>6</sup> To discharge student loans, borrowers must bring a separate lawsuit within their bankruptcy proceeding—termed an adversary proceeding—in which they must show that they and their dependents will suffer an “undue hardship” because of their

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theconversation.com/bankruptcy-courts-ill-prepared-for-tsunami-of-people-going-broke-from-coronavirus-shutdown-137571 [https://perma.cc/C4EN-HAFU].

4. See *infra* Part I.C.

5. *Id.*

6. 11 U.S.C. § 523(a)(8). Two circuit courts have held that some private student loans are not encompassed by the non-dischargeability presumption. See *McDaniel v. Navient Sols., LLC* (*In re* *McDaniel*), 973 F.3d 1083 (10th Cir. 2020); *Crocker v. Navient Sols., LLC* (*In re* *Crocker*), 941 F.3d 206 (5th Cir. 2019). Under this reading of the relevant Code provision, educational loans from the government remain subject to the “undue hardship” standard. See Jason Iuliano, *Student Loan Bankruptcy and the Meaning of Educational Benefit*, 93 AM. BANKR. L.J. 277, 280 (2019) (explaining and supporting this reading).

student loan debt.<sup>7</sup> An aggressive application of the phrase “undue hardship” has raised the bar for most borrowers such that few debtors obtain a discharge of their student loans.<sup>8</sup> As a result, several members of Congress have sponsored legislation to reform the Code to better protect student borrowers.<sup>9</sup>

The Code is not the only barrier to borrowers receiving discharges of student loans. When a student loan borrower brings an adversary proceeding, as in any other litigation, the holder of the loan can contest the discharge request.<sup>10</sup> For federal student loans, such as Direct Loans and many Federal Family Education Loans (FFEL), the Department is the loan holder.<sup>11</sup> Absent legislative action reforming the Bankruptcy Code, the Department can take meaningful steps to help people struggling with student loan debt through its ability to decide whether it will contest borrowers’ requests for undue hardship discharges.

#### A. THE DEPARTMENT’S ANALYSIS OF “UNDUE HARDSHIP” IS TOO STRICT

At present, the Department’s position on discharges largely relies on an overly rigid application of case law interpreting the phrase “undue hardship.” This case law dates back to the Second Circuit’s decision in *Brunner v. N.Y. State Higher Education Services Corporation*, which requires a three-prong inquiry to determine undue hardship.<sup>12</sup> Debtors must show that (1) they “cannot maintain, based on current income and expenses, a ‘minimal’ standard of living” for themselves and their dependents if required to repay their 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

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7. See Matthew A. Bruckner, Brook Gotberg, Dalié Jiménez, & Chrystin D. Ondersma, *A No-Contest Discharge for Uncollectible Student Loans*, 91 U. COLO. L. REV. 183, 193–96 (2020) (detailing how debtors can seek discharges of student loans).

8. See *id.* at 187–88 (discussing barriers to dischargeability of student loans).

9. See, e.g., *Baldwin, Colleagues Introduce Medical Bankruptcy Bill Amid Raging Pandemic*, U.S. SENATOR TAMMY BALDWIN OF WISC. (Feb. 3, 2021), <https://www.baldwin.senate.gov/press-releases/medical-bankruptcy-fairness-act-2021> [<https://perma.cc/7AD6-CL3Z>]; *Warren and Nadler Introduce the Consumer Bankruptcy Reform Act of 2020*, U.S. SENATOR ELIZABETH WARREN OF MASS. (Dec. 9, 2020), <https://www.warren.senate.gov/newsroom/press-releases/warren-and-nadler-introduce-the-consumer-bankruptcy-reform-act-of-2020> [<https://perma.cc/HGF6-MJS8>].

10. Bruckner et al., *supra* note 7, at 187 (noting how a debtor had to defend a discharge request against the lender’s “repeated attacks”); see also 11 U.S.C. § 523(a)(8); FED. R. BANKR. P. 7001(6).

11. *Federal Student Loan Portfolio*, FED. STUDENT AID, <https://studentaid.gov/data-center/student/portfolio> [<https://perma.cc/U23Q-AHCU>] (last visited July 14, 2021).

12. 831 F.2d 395, 396 (2d Cir. 1987).

loans,” and (3) they have made “good faith efforts to repay the loans.”<sup>13</sup>

To meet their burden of proof under these criteria, borrowers must undergo often burdensome discovery and disclose earnings and spending data to demonstrate that they cannot pay their student loan debt, now or in the future, and maintain a minimal standard of living. This calculus is especially common for borrowers on income-driven repayment (IDR) plans, which may allow for nominal payments over a very long term.<sup>14</sup> The result is that extremely few student borrowers, especially those on IDRs, can surpass the hurdles currently required to show that their education debt is an undue hardship.<sup>15</sup>

At least as recently as April 2021, the Department continues to assert that *Brunner* requires a debtor to establish a “certainty of hopelessness” to show undue hardship.<sup>16</sup> Circuit and district courts likewise have cited this language, often in dicta, to set the bar for student loan discharge.<sup>17</sup> But in a recent decision from the Bankruptcy Court for the Southern District of New York, Chief Judge Cecilia Morris refused to accept that *Brunner* was so demanding and rejected “perpetuating the[] myth[]” that the “certainty of hopelessness” is required by *Brunner*.<sup>18</sup> As the court noted, faulty language interpreting *Brunner* has been “applied and reapplied so frequently . . . that they have subsumed the actual language of the *Brunner* test.”<sup>19</sup> But the Department has not adopted Judge Morris’s careful analysis, and continues to

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13. U.S. Dep’t of Educ. v. Gerhardt (*In re Gerhardt*), 348 F.3d 89, 91 (5th Cir. 2003) (quoting *Brunner*, 831 F.2d at 396).

14. See Bruckner et al., *supra* note 7, at 203–04 (noting that some courts assess the debtor’s ability to repay as measured against the IDR plan).

15. See *id.* at 203–05 (discussing IDR plans and student loan discharge).

16. Brief Filed by Department of Education at 13, *Bradley v. Dep’t of Educ.*, No. 1:20-ap-01012 (Bankr. N.D. Ohio Feb. 7, 2020), ECF No. 61 (citing *In re Oyler*, 397 F.3d 382, 386 (6th Cir. 2005)).

17. See, e.g., *Tetzlaff v. Educ. Credit Mgmt. Corp.*, 794 F.3d 756, 759–60 (7th Cir. 2015) (discussing “certainty of hopelessness”); *Educ. Credit Mgmt. Corp. v. Mosley* (*In re Mosley*), 494 F.3d 1320, 1326 (11th Cir. 2007) (noting that there must be “certainty of hopelessness”); *Graddy v. Educ. Credit Mgmt. Corp.*, 615 B.R. 336, 343 (N.D. Ga. 2020) (noting that “courts have often described the necessary showing as ‘certainty of hopelessness’”); *Devos v. Price*, 583 B.R. 850, 856 n.6 (E.D. Pa. 2018) (explaining that Third Circuit precedent requires “certainty of hopelessness”).

18. *Rosenberg v. N.Y. State Higher Educ. Servs. Corp.* (*In re Rosenberg*), 610 B.R. 454, 459 (Bankr. S.D.N.Y. 2020), *leave to appeal granted sub nom.* *Rosenberg v. Educ. Credit Mgmt. Corp.*, 2020 WL 1048599 (S.D.N.Y. Mar. 4, 2020).

19. *Id.*

suggest that courts should apply the “certainty of hopelessness” standard.<sup>20</sup>

This framework for proving undue hardship has allowed the Department to nitpick borrowers’ spending and to argue that they could make payments, at least when they get back on their feet. For instance, in 2020 the Department contested a discharge based on a lack of undue hardship in the bankruptcy case of Ronishia Monique Bradley, a thirty-eight-year-old single mother of three children with approximately \$50,000 in student loans.<sup>21</sup> Bradley qualified for subsidized rent and had held a series of low-wage jobs for multiple years, through which she earned no more than \$27,000 per year.<sup>22</sup> Although Bradley submitted evidence that she followed a tight budget, the Department took issue with small expenses, such as streaming services and occasional expenditures at fast food restaurants.<sup>23</sup>

Similarly, in 2019 the Department contested a discharge of approximately \$73,000 across twenty-six student loans owed by Jamie Mudd.<sup>24</sup> The fifty-year-old grandmother worked over fifty hours a week at two jobs to maintain a minimal standard of living to support herself and her autistic grandson.<sup>25</sup> Mudd also had applied for and received an IDR of \$0.00 per month from the Department.<sup>26</sup> In granting the debtor’s request for an undue hardship discharge, the bankruptcy judge took note of several aspects of the Department’s litigation strategy: it contended that the debtor exaggerated her monthly food expenses because she testified that she accepts donated food;<sup>27</sup> it “insinuated that Mudd must maintain two jobs to meet her burden of showing undue hardship”;<sup>28</sup> it argued against the borrowers’ claimed

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20. See *supra* note 16. The precedent cited by the Department traces to *Briscoe v. Bank of N.Y.* (*In re Briscoe*), 16 B.R. 128, 131 (Bankr. S.D.N.Y. 1981). Chief Judge Morris detailed how *Briscoe* misapplies *Brunner. In re Rosenberg*, 610 B.R. at 458–59.

21. Brief Filed by Department of Education, *supra* note 16, at 1–7.

22. Complaint by Ronishia Monique Bradley against Great Lakes Educational Loan Service, Inc., Department of Education at 3–5, *Bradley v. Dep’t of Educ.*, No. 1:20-ap-01012 (Bankr. N.D. Ohio Feb. 7, 2020), ECF No. 1; Brief Filed by Department of Education, *supra* note 16, at 1–7.

23. Brief Filed by Department of Education, *supra* note 16, at 10–11. At the time of this Essay’s publication, this adversary proceeding remains pending.

24. Complaint to Determine the Dischargeability of Student Loan Under 11 U.S.C. § 523(a)(8) at 2, *Mudd v. United States of America*, No. 4:19-ap-04048 (Bankr. D. Neb. Oct. 3, 2019), ECF No. 1.

25. *Id.*; Memorandum and Order at 2–11, *Mudd v. United States of America*, 4:19-ap-04048 (Bankr. D. Neb. Oct. 3, 2019), ECF No. 100.

26. Memorandum and Order, *supra* note 25, at 10–11.

27. *Id.* at 7–8 & n.14.

28. *Id.* at 17.

medical expenses because she failed to produce receipts for prescriptions and medical visits;<sup>29</sup> and it took issues with small expenses, such as streaming services, which, even if eliminated from her budget, would not have left her with enough money after necessary expenses to be able pay her student loans.<sup>30</sup>

B. BANKRUPTCY LAW AND STUDENT LOAN BORROWING HAVE EVOLVED

Since *Brunner* was decided, numerous courts have recognized that both bankruptcy law and the extent of student loan borrowing have changed significantly.<sup>31</sup> When added to the Code by Congress in 1976, the phrase “undue hardship” was part of a non-dischargeability standard that only applied to certain student loans within the first five years of the loans coming due.<sup>32</sup> Post-1976, Congress made the discharge of student loans increasingly difficult by amending the Code to expand the types of student loans presumptively not dischargeable and to increase the time during which student loans were not dischargeable after first coming due.<sup>33</sup>

This history means that *Brunner* was decided when the Code allowed for the discharge of student loans provided that the debt first came due more than seven years before the bankruptcy filing.<sup>34</sup> The undue hardship standard only applied to debtors who asked to discharge student loans that were in repayment for less than seven years.<sup>35</sup> In other words, the undue hardship standard was meant to accompany a narrow window of non-dischargeability.

While Congress repeatedly amended the Code to expand the non-dischargeability of educational loans, outstanding federal student loan debt skyrocketed. It nearly tripled in the span of fifteen years, growing from about \$340 billion in 2001 to \$1.3 billion in 2016.<sup>36</sup> Student loan default rates likewise have risen. The Federal Reserve Bank

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29. *Id.* at 20.

30. *Id.* at 20–22.

31. See Bruckner et al., *supra* note 7, at 194–201 (discussing how courts apply “undue hardship”); NAT’L CONSUMER L. CTR, STUDENT LOAN LAW § 11.4.1.2 (5th ed. 2015).

32. See Abbye Atkinson, *Race, Education Loans & Bankruptcy*, 16 MICH. J. RACE & L. 1, 17 (2010) (detailing the legislative history of student loan non-dischargeability).

33. *Id.* at 17–19.

34. *Id.*

35. *Id.* at 36.

36. Laura Feiveson, Alvaro Mezza, & Kamila Sommer, *Student Loan Debt and Aggregate Consumption Growth*, BD. OF GOVERNORS OF THE FED. RESRV. SYS.: FEDS NOTES (Feb. 21, 2018), <https://www.federalreserve.gov/econres/notes/feds-notes/student-loan-debt-and-aggregate-consumption-growth-20180221.htm> [https://perma.cc/Y2CR-X57Z].

of New York estimates that roughly twenty percent of the outstanding dollars of student loans are delinquent, which is a higher proportion than any other type of consumer credit.<sup>37</sup> As applied to the 2004 entry cohort, an estimated forty percent of borrowers will default by 2023.<sup>38</sup> Only sixty percent of student loans are in active repayment.<sup>39</sup>

C. THE DEPARTMENT STANDS TO GAIN LITTLE FROM CHALLENGING DISCHARGE REQUESTS, WHILE BORROWERS MAY LOSE GREATLY

The increase in student loan debt outstanding and in default has led to an increase in the number of people who file bankruptcy with student loan debt. In recent years, an estimated 222,000 people filed bankruptcy with student loans.<sup>40</sup> Among student loan borrowers who file bankruptcy, it is estimated most owe amounts less than fifty percent of their annual income.<sup>41</sup> The people who file bankruptcy, at median, earn \$42,444 per year.<sup>42</sup> Given these figures, most people who file bankruptcy likely owe \$20,000 or less in student loan debt. This figure aligns with data about the amount of student loan debt that people who default owe: the median defaulter owes slightly over \$9,600.<sup>43</sup>

Given these facts, the Department's aggressive litigation positions opposing discharges of student loan debt in bankruptcy can often be short-sighted. A strongly litigated undue hardship adversary proceeding can cost the debtor as much as \$10,000, and most undue

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37. QUARTERLY REPORT ON HOUSEHOLD DEBT & CREDIT, FED. RSRV. BANK OF N.Y. 2 (May 2019) [https://www.newyorkfed.org/medialibrary/interactives/householdcredit/data/pdf/hhdc\\_2019q1.pdf](https://www.newyorkfed.org/medialibrary/interactives/householdcredit/data/pdf/hhdc_2019q1.pdf) [<https://perma.cc/DB9K-KCRB>]. The rate reported is 10.9% for the first quarter of 2019. *Id.* The report notes: "delinquency rates for student loans are likely to understate effective delinquency rates because about half of these loans are currently in deferment, in grace periods or in forbearance and therefore temporarily not in the repayment cycle. This implies that among loans in the repayment cycle delinquency rates are roughly twice as high." *Id.* at 2 n.2.

38. Judith Scott-Clayton, *The Looming Student Loan Default Crisis Is Worse Than We Thought*, BROOKINGS: EVIDENCE SPEAKS (Jan. 10, 2018), <https://www.brookings.edu/research/the-looming-student-loan-default-crisis-is-worse-than-we-thought> [<https://perma.cc/7YD6-ZANG>].

39. See Iuliano, *supra* note 6, at 278.

40. Jason Iuliano, *The Student Loan Bankruptcy Gap*, 70 DUKE L.J. 497, 525 tbl.2 (2020) (estimating bankruptcy filers with student loan debt).

41. Bruckner et al., *supra* note 7, at 189.

42. Foohey et al., *supra* note 2, at 32 tbl.4.

43. Ben Miller, *Who Are Student Loan Defaulters?*, CTR. FOR AM. PROGRESS (Dec. 14, 2017, 12:01 AM), <https://www.americanprogress.org/issues/education-postsecondary/reports/2017/12/14/444011/student-loan-defaulters> [<https://perma.cc/MX4Z-WPLB>].

hardship proceedings are estimated to cost the debtor at least \$4,000.<sup>44</sup>

The Department likewise must expend potentially thousands of dollars in arguing that the debtor does not face undue hardship. Although the Department may succeed at keeping loans on the books, the costs of doing so may exceed the outstanding value of the loan. The Department also must weigh the cost of arguing over undue hardship against the real value of the debt—that is, what the Department could reasonably expect to recover over a long term. This figure must include administrative costs of servicing that debt, which may outweigh the expected return over the long term without even counting the cost of defending an undue hardship discharge proceeding.

In calculating the value of its student loan debt, the Department additionally should consider the demographics of the people who carry student loan debt and file bankruptcy. Communities of color and women bear the brunt of the increase in student loan debt and default. Women make up half of the United States' population but owe two-thirds of outstanding student loan debt.<sup>45</sup> Black students are more likely to fund their education with loans, take out more money than other borrowers, are less likely to pay down the balances on their loans over time, and are more likely to be in default on their loans.<sup>46</sup> Latinx borrowers likewise pay down less of their loan balances over time as compared to white borrowers.<sup>47</sup>

Black households file bankruptcy at more than twice the rate they appear in the general population.<sup>48</sup> Single women also are more likely to file bankruptcy than single men.<sup>49</sup> These disparities intersect with larger economic and social issues, including who is more likely to take out student loans and who is more likely to default on those loans. In short, student loan borrowers who file bankruptcy should be less likely to repay their loans in the future, meaning that the Department

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44. See Rafael I. Pardo, *The Undue Hardship Thicket: On Access to Justice, Procedural Noncompliance, and Pollutive Litigation in Bankruptcy*, 66 FLA. L. REV. 2101, 2137–39, 2141 (2014).

45. DEEPER IN DEBT: WOMEN AND STUDENT LOANS, AM. ASS'N OF UNIV. WOMEN 1 (2017), <https://www.aauw.org/app/uploads/2020/03/DeeperinDebt-nsa.pdf> [<https://perma.cc/Z6QM-ZXMS>].

46. See Dalié Jiménez & Jonathan D. Glater, *Student Debt Is a Civil Rights Issue: The Case for Debt Relief and Higher Education Reform*, 55 HARV. C.R.–C.L. L. REV. 131, 132–35 (2020).

47. See *id.*

48. See Foohey et al., *supra* note 2, at 41.

49. See *id.* at 32 tbl.4.

should discount its likelihood of recovering a larger portion of the debt people seek to discharge.

D. THE DEPARTMENT MUST RECONSIDER ITS POLICIES REGARDING STUDENT LOAN DISCHARGES

The only formal guidance from the Department on how it will proceed in bankruptcy cases are regulations requiring it, as the loan holder, to evaluate claims and concede an undue hardship in very limited circumstances.<sup>50</sup> Otherwise, the regulations direct the Department to apply the undue hardship criteria and determine whether “the costs reasonably expected to be incurred to oppose discharge will exceed one-third of the total amount owed on the loan, including principal, interest, late charges and collection costs.”<sup>51</sup> These regulations, and the fact that no single individual bankruptcy case is typically of a level that rises to senior Department leadership,<sup>52</sup> have fostered the need for structure, guidance, and oversight about which discharge cases to contest.

Indeed, in 2018, the Department issued a request for information regarding what factors the Department should use going forward to assess undue hardship discharge requests, including what “considerations should weigh into whether an undue hardship claim should be conceded by the loan holder.”<sup>53</sup> The Attorney General of the United States recently cited this request as a reason that the Supreme Court should reject a *writ of certiorari* in a case dealing with the undue hardship discharge standard, arguing that review was not warranted “[b]ecause the Department [] continues to study this issue, and may revise its regulations and related policies in the future.”<sup>54</sup>

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50. 34 C.F.R. §§ 674.49, 682.402(i)(1), 685.212(c). This includes some instances in which schools have closed, in the circumstances of death or total disability, and in cases filed before 1998.

51. *Id.* § 674.49(c)(4).

52. This observation is based on two of this Essay’s authors’ tenures as employees of the Department.

53. Request for Information on Evaluating Undue Hardship Claims, 83 Fed. Reg. 7460, 7461 (Feb. 21, 2018); *see also* Letter from Martha Upton Fulford, Sr. Counsel, National Student Legal Defense Network, to Jean-Didier Gainer, Docket No. ED-2017-OPE-0085 (May 22, 2018) (responding to this request for information); Dalié Jiménez, Matthew Bruckner, Pamela Foohey, Brook E. Gotberg, & Chrystin D. Ondersma, *Comments of Academics to Department of Education’s RFI Regarding Evaluating Undue Hardship Claims in Adversary Actions Seeking Student Loan Discharge in Bankruptcy Proceedings*, Docket No. ED-2017-OPE-0085 (May 22, 2018), <https://ssrn.com/abstract=3183893> [<https://perma.cc/K8M4-BQTM>] (same).

54. Brief of Respondent United States in Opposition at 20, *McCoy v. United States*, No. 20-886 (U.S. Jan. 4, 2021), ECF No. 21. The Supreme Court denied the writ of

Now is the time for the Department to evaluate its policies for when it will contest the discharge of student loans in bankruptcy proceedings. Many of the student loans that debtors may attempt to discharge likely are not actually worth their face value, particularly as compared to the cost of contesting undue hardship requests. The Department can adopt a new approach to litigating undue hardship requests that is far friendlier to borrowers and will not bring nearly as significant of a financial loss to the Department's books as previously anticipated.

## II. UPDATING THE DEPARTMENT'S POLICIES REGARDING STUDENT LOAN DISCHARGE

This Part offers two proposals for how the Department should respond to future adversary proceedings in bankruptcy cases seeking to discharge student loans based on "undue hardship." Both proposals offer a form of "rough justice" whereby the Department resolves cases by relying on easy-to-implement criteria.<sup>55</sup> These proposals can be implemented through a directive to the Department of Justice, which represents the Department of Education in bankruptcy proceedings, and an internal staff directive regarding student loan discharge in bankruptcy proceedings.<sup>56</sup>

To effectuate these proposals, based on the criteria detailed, the Department should respond to a debtor's request for an undue hardship discharge in one of two ways. If the Department determines that contesting is not warranted, it can simply not respond, or it can settle with the debtor and file a short response stipulating that it agrees that the debtor's circumstances amount to an undue hardship. Alternatively, the Department can contest the discharge by arguing that the debtor's circumstances do not amount to an undue hardship. Regardless of whether the Department does not contest the discharge,

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certiorari. *McCoy v. United States*, No. 20-886, 2021 WL 2519103 (June 21, 2021). A recent announcement by the Department regarding upcoming topics for rulemaking does not suggest changes to the Department's regulations in this regard. Negotiated Rulemakings Committee; Public Hearings, 86 Fed. Reg. 28,299 (May 26, 2021).

55. See Alexandra D. Lahav, *Rough Justice 1* (Mar. 2, 2010) (unpublished manuscript), <https://ssrn.com/abstract=1562677> [<https://perma.cc/528W-SUPU>] (defining the term as "the attempt to resolve large numbers of cases by using statistical methods to give plaintiffs a justifiable amount of recovery").

56. The Department has a history of using such internal memoranda to direct policy decisions. See Memorandum from William D. Hansen, Deputy Secretary, to Terri Shaw, Chief Operating Officer (Oct. 30, 2002), <https://www.hmbr.com/wp-content/uploads/2015/06/Hansen-Incentive-Compensation-Memo.pdf> [<https://perma.cc/D9ZK-XZ3W>].

responds in favor of the discharge, or argues against the discharge, the court has the final decision as to whether to grant the undue discharge.<sup>57</sup>

A. PROPOSAL 1: PRESUMPTIVE POSITION OF NO-CONTEST

The first option proposes a presumption that the Department will not contest a request for discharge of student loans and is the easier of the two proposals to implement. To effectuate the proposal, the Department should issue guidance that the presumptive position of its agents will be to not contest undue hardship discharge requests. That is, the Department will consent to the discharge of student loans in all adversary proceedings either by consent via stipulation or by not opposing the discharge. Under this proposal, if an attorney in the Department determines that the circumstances of a particular case justify contesting the discharge, the attorney can request that the Department affirmatively approve a strategy to contest the discharge request. Nonetheless, the presumptive position for Department staff, attorneys, and agents will be to not contest.

This policy will save money on discovery, future collections, and decision making and give real relief to all student loan debtors. Some may argue that this approach gives some debtors a “free pass” even though they may plausibly pay their debts in future years. Nonetheless, there are four strong rebuttals to this potential objection.

First, the number of people with student loan debt who file bankruptcy every year is relatively small.<sup>58</sup> Of those people, even fewer are likely to file adversary proceedings to argue for undue hardship discharges. The filing fee for the proceeding is \$293,<sup>59</sup> and debtors’ attorneys will have to charge debtors for the work of filing the discharge request document because debtors still will need to argue to the bankruptcy court that they are entitled to the discharge. The administrative savings to the Department of not going through a longer process to decide which bankruptcy cases to contest may outweigh any potential recoveries.

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57. See Rafael I. Pardo & Michelle R. Lacey, *Undue Hardship in the Bankruptcy Courts: An Empirical Assessment of the Discharge of Educational Debt*, 74 U. CIN. L. REV. 405, 419 (2005) (noting that “the discretion afforded by the Code’s undue hardship discharge provision . . . provides a bankruptcy judge the opportunity to determine whether the educational debt in question should be forgiven”).

58. See *supra* note 40 and accompanying text.

59. *Bankruptcy Court Miscellaneous Fee Schedule*, U.S. COURTS, <https://www.uscourts.gov/services-forms/fees/bankruptcy-court-miscellaneous-fee-schedule> [<https://perma.cc/JJ9L-4Y57>] (last visited July 14, 2021).

Second, based on research about the people who file bankruptcy, those people who file bankruptcy and request an undue hardship discharge likely will be unable to repay much or all of their student loans in the future. By the time people file bankruptcy, more than two-thirds of filers report that they seriously struggled to pay their debts for two or more years and that they have taken multiple actions to reduce their expenses, increase their incomes, and otherwise pay back their debts.<sup>60</sup> In addition, filing bankruptcy comes with negative effects and stigma. A bankruptcy filing may limit future employment, will increase people's cost of credit, and comes with social stigma.<sup>61</sup> In short, people do not take filing bankruptcy lightly. If the Department went through a longer process of deciding which cases to contest, the Department typically would decide that contesting the discharge would not be cost effective.

Third, even if the Department acquiesces to an undue hardship discharge, the bankruptcy process has additional safeguards. The Office of the United States Trustee has the authority and mandate to serve as a "watchdog over the bankruptcy process."<sup>62</sup> If the United States Trustee views it as appropriate to raise an objection about discharge of student loans, the Trustee has the authority to do so.<sup>63</sup> In addition, the bankruptcy judge gets the final say on whether to grant a discharge of student debts.<sup>64</sup> The Code further provides the judge with the power to dismiss a debtor's case in its entirety if the judge determines that the filing is not in good faith.<sup>65</sup> These potential outcomes will likely deter people from filing bankruptcy solely to discharge student loan debt. For the remaining filers, if the Department went through a longer process of deciding which adversary proceedings to contest, the Department likely would decide that contesting many of the requests for discharge would not be cost effective.

Fourth and finally, because this is a discretionary action, the Secretary of Education can set metrics to trigger reconsideration if the Department sees a significant rise in the number of people filing

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60. *See generally* Pamela Foohey, Robert M. Lawless, Katherine Porter, & Deborah Thorne, *Life in the Sweatbox*, 94 NOTRE DAME L. REV. 219 (2018) (detailing, based on debtors' reports, the lengths that people go to prior to filing bankruptcy to pay their debts).

61. *See id.*

62. *About the Program*, U.S. DEP'T OF JUSTICE, <https://www.justice.gov/ust/about-program> [<https://perma.cc/Q6VQ-V7YN>] (last visited July 14, 2021) (citing H.R. Rep. No. 989, at 88 (1978), as reprinted in 1978 U.S.C.C.A.N. 5787, 5963, 6049).

63. *See generally* 28 U.S.C. § 586.

64. *See supra* note 57.

65. 11 U.S.C. §§ 707(b), 1325(a).

bankruptcy and requesting undue hardship discharges of their student loans. Overall, this proposal will save the Department time and money in evaluating undue hardship discharge requests, most of which likely will yield the Department little recovery, and the proposal can easily be reversed by the Department if there is a significant rise in undue hardship requests.

B. PROPOSAL 2: STREAMLINE CONTESTING DISCHARGE REQUESTS BY USING EASY TO ASSESS, OBJECTIVE CRITERIA

The second option proposes decision steps and criteria for the Department to assess (through its agents) to determine whether to consent to or to contest a student loan discharge request. The proposed criteria require the Department to base its determination on readily accessible information about borrowers, either found in required bankruptcy documents, such as the schedules that individual debtors must file,<sup>66</sup> or based on information that borrowers can easily include in the adversary proceedings filings. This streamlining will save the Department resources in decision making and eliminate the need to request additional discovery.

We propose that the Department's decision criteria proceed in three steps.<sup>67</sup> For cases that meet the criteria of each step, the Department can stipulate to the discharge of federal student loans by affirmatively responding that it consents to the discharge based on undue hardship.

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66. *Bankruptcy Forms*, U.S. COURTS, <https://www.uscourts.gov/forms/bankruptcy-forms> [<https://perma.cc/A52R-VU54>] (last visited July 14, 2021).

67. Many of the criteria proposed in these steps are inspired by and adopted from a letter to the Department signed by Senators Dick Durbin, Jack Reed, and Elizabeth Warren and Representatives Steve Cohen, John Conyers, Elijah Cummings, and Hank Johnson, and academics' response to the Department's request for information from 2018 regarding student loan discharge of which one of this Essay's authors was a primary drafter. *Cohen, 6 Members of Congress Urge Education Secretary to Bring More Fairness to Struggling Students*, CONGRESSMAN STEVE COHEN (March 16, 2014), <https://cohen.house.gov/press-release/cohen-6-members-congress-urge-education-secretary-bring-more-fairness-struggling> [<https://perma.cc/33CJ-WFRW>]; Jiménez et al., *supra* note 53. The National Consumer Law Center also submitted a response to the Department's request for information that proposes many similar criteria. Comments of the National Consumer Law Center to the Department of Education Regarding the Request for Information on Evaluating Undue Hardship Claims in Adversary Actions Seeking Student Loan Discharge in Bankruptcy Proceedings, Docket No. ED-2017-OPE-0085 (May 18, 2018) [hereinafter National Consumer Law Center Comments] <https://www.nclc.org/images/pdf/bankruptcy/comments-undue-hardship-bankruptcy.pdf> [<https://perma.cc/7DZY-GP7G>].

- Step 1: The Department will not contest undue hardship requests filed by student loan borrowers who owe less than \$7,500 in aggregate federal student loans<sup>68</sup> or whose federal student loans first became due more than 25 years ago.<sup>69</sup>
- Step 2: The Department will not contest undue hardship requests filed by student loan borrowers who face certain factors and situations, including:
  - Fifty percent or more of the borrower's income is comprised of Social Security or disability payments.
  - The borrower has been determined by the Social Security Administration or the Department of Veterans Affairs to be eligible for disability benefits and unable to work full-time.
  - The borrower is a family caregiver of an eligible veteran pursuant to 38 U.S.C. § 1720G.
  - The borrower provides for the care and support of an elderly, chronically ill, or disabled household member or member of the borrower's immediate family, and the borrowers' annual household income is at or less than 175 percent of the official poverty guidelines.<sup>70</sup>
  - The borrower attended an institution that closed and did not complete a program of study at that institution because the institution closed while the borrower was enrolled or within a period of time that

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68. This figure is based on a rough assessment of how much debtors will have to expend to request the undue hardship discharge as compared to the amount sought to be discharged. A debtor will have to spend at least about \$1,500 to file the bankruptcy case, plus another at least \$2,000 for the adversary proceeding, even if the Department does not contest the discharge. See Foohey et al., *supra* note 2, at 13; *supra* note 44 and accompanying text. If the student loan amount outstanding is under \$7,500 and the debtor can pay, we anticipate that most debtors will decide it is not worth spending about \$3,500, plus the time, to discharge the debt. This dollar threshold is also a suggestion that the Department can lower or increase.

69. If a debtor has not paid student loans in full after 25 years from the loans first becoming due, the probability that the debtor will be able to pay a significant portion of the loans in the future is very low and it is not worth the Department's time and resources to contest the discharge.

70. The 175 percent or less of the official poverty guidelines used throughout this proposal is a suggested threshold that the Department may increase or lower. For instance, based on data from the Consumer Bankruptcy Project, on which one of this Essay's authors is a co-investigator, about one-third of people who file bankruptcy have income at or below 150 percent of the official poverty guidelines when they file bankruptcy. See Jiménez et al., *supra* note 53, at 10.

would otherwise make the borrower eligible for a closed school loan discharge.

- The borrower has filed a good-faith borrower defense claim against the institution at least one year before filing for bankruptcy or is part of a group claim submitted by a state law enforcement agency.
  - Three or more years have passed since the borrower ceased attending an institution of higher education and the borrower has not obtained a credential from the educational program for which the student loans were borrowed, and the borrowers' annual household income is at or less than 175 percent of the official poverty guidelines.
  - The borrower's annual household income has been at or less than 175 percent of the official poverty guidelines for the current year (as annualized) and the two years prior to filing bankruptcy.<sup>71</sup>
- Step 3: The Department will consider whether to contest undue hardship based on less administratively expensive and more borrower friendly calculations, including:
    - Assessing the borrower's present financial circumstances by relying on the income and expense information disclosed in the bankruptcy to calculate the Code's "means test" calculation of "monthly disposable income" excluding payment of the student loans.<sup>72</sup>
      - If the debtor's "monthly disposable income" is less than \$30 based on this calculation, the Department will not contest the "undue hardship" discharge.
      - Alternatively, if the debtor's "monthly disposable income" is less than \$30 based on this

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71. As part of their bankruptcy cases, debtors must submit Form 107, which requires them to disclose their income for the current year and the two years prior to their bankruptcy filing. *Official Form 107: Statement of Financial Affairs for Individuals Filing for Bankruptcy*, U.S. COURTS (April 2019), [https://www.uscourts.gov/sites/default/files/form\\_b\\_107.pdf](https://www.uscourts.gov/sites/default/files/form_b_107.pdf) [<https://perma.cc/8NFS-T28S>].

72. *Means Test Forms*, U.S. COURTS, <https://www.uscourts.gov/forms/means-test-forms> [<https://perma.cc/PY7P-GVR6>] (last visited July 14, 2021). For debtors who do not need to file Form B 122A-2, those seeking an undue hardship discharge will need to file this additional form or the Department will need to seek through discovery the necessary additional information to complete the calculation.

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calculation, the Department will stipulate that the debtor is maintaining a minimum standard of living for the purposes of the *Brunner* test.<sup>73</sup>

- Considering the amount the borrower is required to pay toward student loans in an IDR. If the IDR is set at less than \$30 per month, the Department will consider this evidence that the borrower will be unable to pay a sufficient portion of their loans in the future and that the Department will not contest the undue hardship discharge.<sup>74</sup>
- Considering whether the borrower's hardship will persist for more than ten years in determining if the borrower is suffering from circumstances that will make repayment a hardship. If the Department determines that the borrower's hardship will persist for more than ten years, it will stipulate the borrower is suffering from circumstances that will make repayment a hardship for the remainder of the loan term.<sup>75</sup>
- Not requiring proof of "certainty of hopelessness" or "total incapacity," that the debtor pursue employment opportunities in a certain field, or independent medical advice in addition to the debtor's testimony regarding their health in considering the borrower's ongoing hardship.
- Only looking forward regarding the borrower's ability to repay the student loans debts rather than re-litigating the past, including questioning whether the debtor should have sought the degree or family choices, such as the number of children the debtor chose to have.

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73. The \$30 per month figure yields disposable income of \$3,600 over a 10-year period or \$7,200 over a 20-year period. Even if the Department's costs in contesting the undue hardship request are under these amounts, given the variability of people's budgets and finances over decades, it is unlikely that the Department will make more than it expends in contesting the undue hardship request. As with other suggested thresholds, the Department may decide to increase or decrease this dollar threshold.

74. The \$30 per month figure yields a recovery of \$3,600 over a 10-year period or \$7,200 over a 20-year period. This recovery does not merit the Department expending resources in contesting the undue hardship discharge. The Department may decide to increase or decrease this dollar threshold.

75. This and the next two criteria are adapted from National Consumer Law Center Comments, *supra* note 67.

Each step of this proposal is designed to reduce the Department's administrative costs of deciding whether to contest borrowers' requests for undue hardship discharges of their student loan debts. Step 1 requires the least work by the Department. It will result in the Department not contesting undue hardship requests when the Department is likely to spend more arguing against the discharge than it will actually recover from the borrower outside bankruptcy. Step 2 requires somewhat more work by the Department to assess the borrower's disability status, family responsibilities, or history of education. These criteria, however, are information that the debtor can include in adversary proceeding pleadings, which should decrease the need for the Department to expend resources on additional discovery. Step 3 is more likely to result in the Department making complex determinations about whether to consent to the undue hardship discharge, but it will improve the uniformity of the Department's decisions across bankruptcy cases. Overall, this second proposal will result in the Department contesting fewer borrowers' requests for undue hardship discharges of their student loans, but it still will have to spend resources determining whether to contest each discharge request.

#### CONCLUSION

At present, the Department often contests undue hardship discharge requests in borrowers' bankruptcy cases. Many of these borrowers likely are seeking to discharge student loans that the Department stands to make little money on in the future, particularly when compared to the time, money, and effort required by the Department to contest the discharge requests.

The Department can use its current administrative authority to halt its practice of contesting the discharge of student loans in its borrowers' bankruptcy cases. Similarly, the Department can affirmatively stipulate to the discharge of student loans for borrowers in a variety of circumstances, as outlined in this Essay. Importantly, implementation of either of these proposals does not require regulatory reforms. The effects of such a policy change could improve the lives and financial well-being of thousands of distressed student borrowers across the country at a much lower cost to the federal government than previously contemplated.