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Student Loans: Where Are We, and Where Do We Go from Here?

CONSUMER SESSION

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2018

STUDENT LOANS

WHERE ARE WE AND WHERE DO WE GO FROM HERE?

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Case Law Governing Student Loan Discharge Cases

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- The Origin of Section 523(a)(8)
  - Prior to 1976, student loans were freely dischargeable.
  - In 1977, Congress enacted the Education Amendments of 1976, which included the first exception to discharge for student loans, which is embodied in section 523(a)(8) of the Bankruptcy Code.[1]
    - Under this new legislation, student loans that were less than five years old were not discharged unless the court determined that "payment from future income or other wealth will impose an *undue hardship* on the debtor or his dependents."[2]
  - In 1990, Congress extended the period of nondischargeability from five to seven years.[3]
  - In 1998, Congress eliminated the time based restriction entirely, but retained the "undue hardship" exception.[4]
    - Thus, until 1998, all student loans were discharged after a period of, *at most*, seven years from the date the repayment period commenced.[5]
  - In 2005, Congress further extended the discharge exception to include *private* student loans.[6]

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[1] *See In re Acosta-Conniff*, 2015 WL 1403322, at *3 (Bankr. M.D. Ala. 2015).
[2] *Id.* (citing Pub. L. 94-842, Sec. 439).
[3] *See id.*
[4] *See id.*
[5] *See id.*
[6] *In re Roth*, 490 B.R. 908, 921 (B.A.P 9th Cir. 2013).

- Origins of the Undue Hardship Standard
  - Most cases decided pre-*Brunner* concerned a moderate to small amount of student loan debt.
    - *Johnson v. Edinboro State College*, 728 F.2d 163 (3d Cir. 1984) = Holding student loans in the amount of $1,700 were nondischargeable.
    - *Andrews v. South Dakota Student Loan Assistance Corp.*, 661 F.2d 702 (8th Cir. 1981) = Reversing bankruptcy court judgment discharging a $2,500 student loan.
    - *Moorman v. Commonwealth of Ky. Higher Educ. Assistance Auth.*, 44 B.R. 135 (Bankr. W.D. Ky. 1984) = Holding that stress of repaying $3,700 student loan not an undue hardship.
    - *Betz v. N.Y. State Higher Educ. Servs. Corp.*, 31 B.R. 565 (Bankr. W.D.N.Y. 1983) = Holding that student loan indebtedness totaling $3,400 was not an undue hardship.
  - Bankruptcy courts at this time only had to consider the undue hardship impact student loans would cause on the debtor's life for the five year period following the beginning of the re-payment period.
    - Five years following the beginning of the repayment period the debtor's student loans would be freely dischargeable under the then current version of section 523(a)(8).
  - Judge Pappas highlighted the state of student loan discharge cases during this era:
    - "*Brunner* typified the sort of student loan discharge cases encountered by bankruptcy court as that time. The debtor sought to discharge $9,000 in student loans in a bankruptcy case filed just a few months after she obtained her master's degree, immediately after the grace period before payments became due expired, after only a

few months of unemployment, and having made no efforts to pay anything on the loans."[7]

- Brunner v. New York State Higher Educ. Servs. Corp. (1987)[8]
  - Facts: Ms. Brunner received a Bachelor of Arts degree in 1979 and a Master's degree in Social Work in May, 1982.[9]
    - Approximately seven months after receiving her Master's degree, Ms. Brunner filed for personal bankruptcy, and her debts, exclusive of approximately $9,000 in student loans, were discharged.[10]
    - Two months later, upon the expiration of the nine-month grace period suspending repayment of the student loans, Ms. Brunner filed an adversary action seeking to discharge her student loans.[11]
    - Important to note, five years following the expiration of Ms. Brunner's grace period, Ms. Brunner's student loans would have been freely dischargeable under the version of section 523(a)(8) in effect at the time.
  - Bankruptcy Court Holding: The bankruptcy court found that Ms. Brunner met the standard for undue hardship and discharged her student loans.[12]
  - District Court Holding: The district court reversed, holding "[n]othing in the record supports a finding that . . . [Ms. Brunner's] current inability to find any work will extend

[7] *Roth*, 490 B.R. at 921 (citing *Brunner v. New York State Higher Educ. Servs. Corp.*, 831 F.2d 395, 396 (2d Cir. 1987)).
[8] *Brunner*, 831 F.2d 395 (2d Cir. 1987).
[9] *In re Brunner*, 46 B.R. 752, 753 (S.D.N.Y. 1985).
[10] *Brunner*, 46 B.R. at 753.
[11] *Id.*
[12] *Id.* at 758.

for a significant part of the repayment period of the loan or that she has 'a total incapacity now and in the future to pay [her] debts for reasons not within [her] control.'"[13]

- Second Circuit Holding: The Second Circuit affirmed adopting the three-part test for determining undue hardship proposed by the district court.[14]

- The *Brunner* Standard for Dischargeability Under 11 U.S.C. § 523(a)(8)
  - The 'undue hardship' exception of § 523(a)(8) is difficult to apply because the drafters of the Bankruptcy Code did not define undue hardship.
  - The Bankruptcy Code drafters decided that bankruptcy courts had to decide undue hardship on a "case-by-case basis, considering all of the debtor's circumstances."[15]
  - Under the *Brunner* court's three-part test for "undue hardship," the debtor must show:
    - (1) the debtor cannot maintain, based on current income and expenses, a "minimal" standard of living for themselves and their dependents if forced to repay the loans;
    - (2) additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans; and,
    - (3) the debtor has made good faith efforts to repay the loans.[16]
  - Minimal Standard of Living
    - "There is no simple formula by which to assess a debtor's ability to maintain a 'minimal' standard of living."[17]

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[13] *Id.* (quoting *In re Rappaport*, 16 B.R. 615, 617 (Bankr. D.N.J. 1981)).
[14] *Brunner*, 831 F.2d at 396.
[15] *In re Faish*, 72 F.3d 298, 302 (3d Cir. 1995) (citing Kurt Wiese, Note, Discharging Student Loans in Bankruptcy: The Bankruptcy Court Tests of "Undue Harship," 26 Ariz. L. Rev. 445, 447 (1984)).
[16] *In re Cox*, 338 F.3d 1238, 1241 (11th Cir. 2003) (citing *Brunner*, 831 F.2d at 396).
[17] *In re Michaud*, 2014 WL 3362157, at *3 (Bankr. M.D. Fla. 2014).

- Bankruptcy courts generally assess the debtor's income, expenses, and lifestyle to determine whether they cannot maintain a minimal standard of living if a discharge of the student loan debt is not allowed.
- Bankruptcy courts do not require a debtor to live at or below the poverty level to receive a student loan discharge.[18]
- Instead, courts have interpreted "minimal standard of living" to be "a measure of comfort, supported by a level of income, sufficient to pay the costs of specific items recognized by both subjective and objective criteria as basic necessities" and that a debtor should not have "unnecessary and frivolous expenses; however, the debtor should not be forced to live in abject poverty with no comforts."[19]
- The *Thomas* court held the debtor unquestionably satisfied this element because the debtor could not "house, feed, clothe, and transport himself based on his current income, even if he is not required to make any payments on his student loan."[20]
- "Minimal standard of living" based on the debtor's current income and expenses at the time of trial.[21]

o State of Affairs is Likely to Persist for a Significant Portion of the Repayment Period

- Courts have defined the phrase "additional circumstances" to be a "certainty of hopelessness, not simply a present inability to fulfill financial commitment" and to include the following potential considerations:

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[18] *See Michaud*, 2014 WL 3362157, at *3; *In re Wright*, 2014 WL 1330276, at *3 (Bankr. N.D. Ala. 2014).
[19] *Wright*, 2014 WL 1330276, at *3 (citing *Ivory v. United States Dep't of Educ.*, 269 B.R. 890, 899 (Bankr. N.D. Ala. 2001)).
[20] *In re Thomas*, 2014 WL 6968056, at *4 (Bankr. N.D. Ala. 2014).
[21] *Id.* at 4.

1. Serious mental or physical disability of the debtor which prevents employment or advancement;
2. Lack of, or severely limited education;
3. Poor quality of education;
4. Lack of usable or marketable job skills;
5. Underemployment;
6. Maximized income potential in the chosen educational field, and no other more lucrative job skills;
7. Limited number of years remaining in work life to allow payment of loans;
8. Age or other factors that prevent retraining or relocation as a means for payment of the loan;
9. Lack of assets, whether or not exempt, which could be used to pay the loan;
10. Potentially increasing expenses that outweigh any potential appreciation in the value of the debtor's assets and/or likely increases in the debtor's income
11. Lack of better financial options elsewhere.[22]

- Goof Faith Effort to Repay the Student Loans
  - Requires a showing that the debtor made efforts to satisfy the debts by all means—or at least be some means—within the debtor's reasonable control.[23]
  - Courts do not require actual payments to be made on the debt to satisfy the good faith requirement, rather a debtor must establish "either a good faith effort was undertaken

[22] *Wright*, 2014 WL 1330276, at *5 (quoting *Nys v. Educ. Credit Mgmt. Corp.*, 308 B.R. 436, 443 (B.A.P. 9th Cir. 2004)).
[23] *In re Johnson*, 2014 WL 1356600, at *3 (Bankr. M.D. Fla. 2014) (quoting *In re Douglas*, 366 B.R. 241, 259 (Bankr. M.D. Ga. 2007)).

to repay the student loans or that the forces preventing repayment were truly beyond his or her reasonable control.'"[24]

- "Good [f]aith does not require the debtor to have enrolled in an income-contingent repayment program."[25]

- Totality of the Circumstances Test
  - Alternate undue hardship test applied by only the Eighth Circuit
  - Courts consider "(1) the debtor's past, present, and reasonably reliable future financial resources; (2) a calculation of the debtor's and her dependent's reasonable necessary living expenses; and (3) any other relevant facts and circumstances surrounding each particular bankruptcy case."[26]
- Acceptance of the *Brunner* Standard
  - The *Brunner* test has been adopted by a majority of the Courts of Appeals that have specifically addressed the issue of what single standard should be applied to determine whether 'undue hardship' exists under 11 U.S.C. § 523(a)(8).[27]
    - Including the Second, Third, Fourth, Fifth, Sixth, Seventh, Ninth, and Tenth Circuits.
  - The First Circuit is the only Circuit Court which has refused to definitively choose either the *Brunner* or Totality of the Circumstances test.[28]
  - In 2003, the Eleventh Circuit adopted the *Brunner* test for determining when a debtor has proven "undue hardship" to permit dischargeability under section 523(a)(8).[29]

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[24] *Id.* (quoting *In re McGinnis*, 289 B.R. 257, 267 (Bankr. M.D. Ga. 2003)).
[25] *In re Bumps*, 2014 WL 185336, at *3 (Bankr. M.D. Fla. 2014).
[26] *In re Long*, 322 F.3d 549, 554 (8th Cir. 2003).
[27] *Faish*, 72 F.3d at 303.
[28] *In re Nash*, 446 F.3d 188, 190 (1st Cir. 2006).
[29] *Cox*, 338 F.3d at 1241.

- Recent case law makes clear the *Brunner* standard is binding precedent within the Eleventh Circuit
  - *In re Acosta-Conniff*, 686 F. App'x 647, 648 (11th Cir. 2017) - "[T]his circuit has adopted the test set out in Brunner."
  - *In re Wolfe*, 501 B.R. 426, 434 (Bankr. M.D. Fla. 2013) - "[T]his Court is not free to abandon the Brunner test in favor of a legal standard that is not applicable in the Eleventh Circuit."

Undue Hardship Adversary Proceedings Under 11 U.S.C. §523(a)(8): Admin. Remedies and Helpful Practice Tips and Pointers

January 19, 2018

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I. GENERAL BACKGROUND AS TO STUDENT LOANS

A. Higher Education Act of 1965: In 1965, Congress, in response to a perceived need for financial assistance to students in higher education, passed the Higher Education Act of 1965 ("HEA").

B. Federal Student Loan Programs: The HEA governs two federally-backed student loan programs: the Federal Family Education Loan Program ("FFEL Program" or "FFELP") and the William D. Ford Federal Direct Loan Program ("Direct Loan Program" or the "Ford Program). Effective July 1, 2010, Congress eliminated the FFEL Program under the Health Care and Education Reconciliation Act of 2010.

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

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

C. Types of Federal Loans:

1. HEA: Loans under the HEA include Perkins Loans, Stafford (subsidized and unsubsidized) Loans, parent PLUS Loans, graduate PLUS Loans, and Consolidation Loans. Grants include Pell Grants and Supplemental Education Opportunity Grants. The terms of Stafford, parent PLUS, graduate PLUS, and Consolidation loans in both the FFEL Program and the Direct Loan Program are similar except that the Direct Loan Program offers a Public Service Loan Forgiveness program and offers both and an income based and an income contingent

repayment option. *See infra* at IV.

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

D. Private Loans: Private loan programs also exist and provide educational funds to students who have exhausted their federal loan limits or are otherwise ineligible to borrow under the federal loan programs. Private loans are not eligible for the administrative relief discussed below and may not be consolidated under federally-backed consolidation programs. Since 2005, however, private loans enjoy the presumption of non-dischargeability under 11 U.S.C. § 523(a)(8).

E. New House Bill: On December 1, 2017, Congresswoman Virginia Fox proposed a bill that if passed, would revamp many aspects of the HEA. In part, the Bill as proposed would make a number of changes to existing repayment options available under the Direct Loan Program (see discussion below), and would eliminate Public Service Debt Forgiveness (see below). The bill as proposed would not apply to existing loans. At this time, it is unknown whether the Bill will be passed or become law in whole or in part, or at what specific point in time it would go into effect. But practitioners should pay attention to its status for existing borrowers, and its impact on the administrative remedies and repayment options discussed herein.

II. UNDUE HARDSHIP

Under the Bankruptcy Code, educational benefits, overpayments, or loans are presumptively non-dischargeable unless a debtor, after commencing an adversary proceeding, proves that he/she or his/her dependents suffer from an "undue hardship" under 11 U.S.C. § 523(a)(8). In 2003, the Eleventh Circuit adopted the following three-pronged test, first established by the Second Circuit, that a debtor must meet in order to discharge an otherwise non-dischargeable student loan as an undue hardship:

> "(1) that the debtor cannot maintain, based on current income and expenses, a 'minimal' standard of living for herself and her dependents if forced to repay the loans;

> (2) that additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans; and
>
> (3) the debtor has made good faith efforts to repay the loans."

In re Cox, 338 F.3d 1238, 1241 (11th Cir. 2003) quoting *Brunner v. New York State Higher Educ. Services*, 831 F.2d 395, 396 (2nd Cir. 1987).[30] *See also In re Mosley*, 494 F.3d 1320, 1324 (11th Cir. 2007)(court reiterated *Brunner* test as standard in the 11th Circuit). All three prongs of the *Brunner* test must be satisfied before an undue hardship discharge can be granted, such that if any one of the three prongs is not met, a bankruptcy court cannot discharge the student loan indebtedness. As the Eleventh Circuit reasoned: "[c]onsidering the evolution of § 523(a)(8), it is clear that Congress intended to make it difficult for debtors to obtain a discharge of their student loan indebtedness." *In re Cox*, 338 F.3d at 1243,

Note: The 11th Circuit reiterated this past April, 2017 that *Brunner* is the standard in the Eleventh Circuit. *See ECMC v. Acosta-Conniff*, 2017 WL 1396164, *1 (11th Cir. April 19, 2017("this court has adopted the test set out in *Brunner v. New York State Higher Educ. Servs. Corp*., 831 F.2d 395 (2d Cir. 1987)(the '*Brunner* test')."

With respect to federally backed student loans, counsel for Debtors should consider a number of factors **before** commencing an undue hardship adversary proceeding.

III. ADMINISTRATIVE REMEDIES

There are a number of administrative remedies for student loan borrowers to consider in lieu of seeking an undue hardship discharge through bankruptcy. Unlike relief under 11 U.S.C § 523(a)(8), borrowers may be entitled to administrative relief irrespective of whether they have filed for bankruptcy protection.[31]

A. Total and Permanent Disability Discharge: Borrowers may be eligible to have their federal student loan debt discharged because of a Total and Permanent Disability ("TPD").

1. Eligibility Criteria for a TPD: TPD means that an individual (1) is unable to engage in any substantial gainful activity by reason of any medically determinable physical or

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[30] The "*Brunner* Test" has been adopted in the Second, Third, Fourth, Fifth, Sixth, Seventh, Ninth, Tenth and Eleventh Circuits. The "totalility of circumstances" test has been adopted in the Eighth Circuit. The First Circuit has to date refused to adopt any one test.

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

mental impairment that (i) can be expected to result in death; (ii) has lasted for a continuous period of not less than 60 months; or (iii) can be expected to last for a continuous period of not less than 60 months; or (2) has been determined by the Secretary of Veterans Affairs to be unemployable due to a service-connected disability. 34 C.F.R. § 682.200(b).

2. Requesting a TPD Discharge: There are three ways in which a borrower can request review for a TPD discharge:

a. Doctor certification on a TPD application: A medical doctor or doctor of osteopathy must certify that the borrower meets the definition of TPD as described in § 682.200(b).

b. Certification with a social security award letter: Today, borrowers who receive Social Security Disability Insurance ("SSDI") or Supplemental Security Income ("SSI") benefits may use their SSA award letter in lieu of obtaining a separate certification from a physician on the TPD discharge application. The SSA award letter must state that the borrower's next scheduled disability review will be within 5 to 7 years from the date of the most recent SSA disability determination.

Borrowers may also submit a Benefits Planning Query ("BPQY"). The BPQY provides a summary of SSA disability benefits, including the scheduled date for the next disability review. A BPQY summary can be obtained by calling 1-800-772-1213, if the SSA award letter is unavailable. Borrowers must still complete their section of the TPD application and submit it with their SSA award letter.

c. Veterans with service-connected disabilities: Veterans have been determined by the U.S. Department of Veterans Affairs ("VA") to be unemployable due to a service-connected disability or have a service-connected disability that is 100% disabling are eligible for immediate discharge of their federal student loans. They need only provide their Veteran's Administration disability paperwork along with their TPD application, and like with the SS determination, complete the appropriate section of the TPD application.

3 Agency review of TPD discharge request: ED has designated Nelnet as its disability servicer for all TPD applications submitted after July 1, 2013. Under the TPD process, borrowers must submit a single TPD discharge application directly to ED/Nelnet rather than to their individual loan holders. Borrowers may initiate the TPD process by going to www.disabilitydischarge.com. Once informed of a TPD request, ED/Nelnet will notify the loan holders. Make sure that you are using the current version of the TPD Application as new one is now being used by ED. *See* OMB No. 1845-0065 Exp. Date 9/30/19.

If the TPD request is approved, the account is immediately discharged by ED.[32] The three-year post-discharge monitoring period remains in effect. During this three-year period, borrowers

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[32] Under the Internal Revenue Code (the "Tax Code") as it currently exists, student loan debt forgiven or discharged by TPD may constitute a taxable event. However, under existing tax laws, any forgiven debt is taxable only to the extent the borrower is solvent. It is unknown at this time

cannot earn more than 100% of the federal poverty guidelines for a family of two (in 2017 = $16,240) and cannot have obtained any new federal student loans. Borrowers must notify Nelnet of any address change during the three-year period. Typically, Nelnet will contact the borrower when the three-year mark is approaching to update the disability status and financial status to ensure that the borrower's discharge criteria have not changed. Borrowers, who fail to respond with updated information, will have their TPD request cancelled and their loans reinstated, until they comply with the request for updated information so their account can be finally reviewed.

B. Loan Rehabilitation: Federal regulations allow borrowers who default on repayment of their loan a one-time opportunity to bring their loans out of a default status. Payment amounts are set at a reasonable rate and borrowers must make nine on-time payments over a 10-month period.

Entering a loan rehabilitation agreement has an immediate effect on a borrower's defaulted loans: it stops all collections activity and legal proceedings, prevents wage garnishment, and it may protect a borrower's state and federal tax refunds from IRS offsets. Successfully completing a loan rehabilitation program restores loans to their pre-default status, it reestablishes eligibility for deferment, forbearance, alternative repayment options, title IV financial aid, and shows positive payment progress on a borrower's credit report, which may repair some of the damage done by default.

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

D. False Certification Discharge: A borrower's student loans can be discharged if a school falsely certified the student's eligibility for a federal student loan on the basis of ability to benefit from the education, signed the borrower's name without authorization by the borrower on the loan application or promissory note, or someone else obtained a federal student loan because of identity theft.

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

F. Teacher Loan Forgiveness Program: Teachers who meet the requirements in 34 C.F.R. § 685.217 are eligible for forgiveness of up to $17,500. Typically, this provision is for

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what the tax laws will be in the future in light of the House and Senate's current bills to revamp the Tax Code.

teachers in low-income areas and those who teach math or science at schools designated eligible by the U.S. Department of Education. (Direct Loan Program loans only).

G. Public Service Loan Forgiveness: Borrowers who make 120 qualifying payments under the IBR, ICRP, REPAYE, or 10-year fixed payment schedule while employed in the public sector are eligible to have any balance remaining on their student loan debt forgiven. Public service includes employment with most local, state, federal, tribunal nation, or § 501(c)(3) corporations. This program is available only in the Direct Loan Program. Borrowers who have FFEL Program loans and wish to take advantage of this program, may consolidate their FFEL Program loans into the Direct Loan Program to become eligible. *See* 34 C.F.R. § 685.219.

But note the impact of this in light of the recently proposed new Bill by Congresswoman Foxx.

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

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

Both the FFEL Program and the Direct Loan Program currently have flexible, affordable payment options for borrowers who have financial hardship. These payment options are available whether or not the borrower has filed bankruptcy. Again, practitioners should pay close attention to the status of the Bill that was recently proposed by Congresswoman Virginia Foxx as it would drastically change what repayment options are available and how they would work for consolidations beginning after June, 2019.

A. Consolidation: Consolidation benefits a borrower by spreading the payments over a term of up to 30 years, depending on the total loan balance. Since July 1, 2010, new consolidation loans are available only through the Direct Loan Program. Borrowers who have previously consolidated their loans in the FFEL Program may reconsolidate their loans (even if defaulted) into the Direct Loan Program but not vice-versa. Today, borrowers who wish to consolidate their federal loans into the Direct Loan Program must do so by completing an application on-line.

B. Income-Driven Payments: In addition to fixed, amortized extended and graduated payment terms, there are now three payments options that are based on a borrower's income and family size: the Income Based Repayment plan ("IBR") (available in both the FFEL Program and Direct Loan Program), the Income Contingent Repayment Plan ("ICRP) (available only in the Direct Loan Program), and the REPAYE plan that just went into effect on December 16, 2015 (available only in the Direct Loan Program).

1. Income Based Repayment:

a. Eligible Loans: Most federally-backed loans are eligible for the IBR:

- Direct Subsidized Loans,
- Direct Unsubsidized Loans,
- Direct PLUS loans made to graduate or professional students,
- Direct Consolidation Loans without underlying parent PLUS loans made to parents,
- Subsidized Federal Stafford Loans,
- Unsubsidized Federal Stafford Loans,
- FFEL Program PLUS loans made to graduate or professional students,
- FFEL Program Consolidation Loans without underlying parent PLUS loans made to parents
- Perkins loans that are or have been consolidated into a new consolidation loan.

b. Ineligible Loans: Defaulted student loans, parent PLUS loans, or federal consolidation loans that contain underlying parent PLUS loans or a mix of Stafford loans and parent PLUS loans are not eligible for the IBR in either the FFEL Program or the Direct Loan Program. Private loans that are not federally-backed are not eligible. Stand-alone Perkins loans are also not eligible for the IBR, unless they are included in a consolidation loan that is IBR-eligible.

c. Restoring IBR eligibility to defaulted loans: Borrowers who have defaulted FFEL Program loans and want to opt into the IBR may re-consolidate their defaulted loans into the Direct Loan Program and elect the IBR in the Direct Loan Program. (Re-consolidating removes the default because the borrower has a new loan). Borrowers who have defaulted FFEL Program *and* Direct Loan Program loans may consolidate both sets of loans into a new Direct consolidation loan. Borrowers with defaulted loans also have a one-time opportunity to rehabilitate their loan to remove the default status and regain eligibility for the IBR in either federal student loan program. *See supra* at III.b.

d. Partial Financial Hardship Threshold: Borrowers who have IBR-eligible loans must first demonstrate partial financial hardship ("PFH").[33] Borrowers can demonstrate PFH if the annual amount due on all eligible student loans under a 10-year repayment schedule is more than 15% of their adjusted gross income ("AGI"). Most borrowers whose total loan balance exceeds their annual earnings will satisfy the PFH requirement.

e. IBR Calculation and Terms: The IBR payment is typically calculated using the borrower's AGI, from the most recent federal tax return, and family size.

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[33] As shown *infra*, PFH is not required for the REPAYE.

Borrowers who earn less than 150% of the poverty level for their family size will have a $0 IBR payment but will still be considered "in repayment" and in good-standing. Otherwise, the required monthly loan payment under the IBR is capped at 15% of annual household earnings above 150% of the applicable poverty level divided by 12 months. The IBR payment is recalculated annually based on household AGI and family size.

Borrowers may contact their lender/servicer at any time if they experience a change in financial circumstances that could impact their required IBR payment. The IBR repayment period is 25 years. At the conclusion of the 25-year repayment period, any remaining balance is forgiven.[34] *But see infra* IV.B.4 (discussing 10-year repayment term for the existing Public Service Loan Forgiveness Program).

Although interest continues to accrue at the contract rate in the IBR, the government will pay unpaid accrued interest on FFEL Program or Direct Loan Program subsidized loans for up to three consecutive years from the date the borrower enters the IBR. Also, during a period of PFH, interest that accrues but is not covered by the IBR payment will not be capitalized, even if interest accrues during a deferment or forbearance.

i. Documenting income: Borrowers who do not file, or are not required to file, a federal tax return may provide alternative documentation of their income such as pay stubs, letter(s) from employer(s) stating income, bank statements, etc. Untaxed income such as SSDI, SSI, child support, federal or state public assistance are not included in the IBR calculation. Borrowers who have no income or have only untaxed income may self-certify their income on the IBR request form at Section 5.10.

ii. Special rule for married borrowers: Married borrowers who file separate tax returns may have their IBR payments based on their own respective incomes but may still count each other and any dependents in the family size.

2. Income Contingent Repayment: Like the IBR, the ICRP, which is available only in the Direct Loan Program, is recalculated annually and the payment amount is based on 20% of the difference between a borrower's AGI and 100% of the federal poverty level for the family size. If the AGI is below 100% of the poverty level for the borrower's family size, then the ICR payment is $0.

Interest continues to accrue at the contract rate and is capitalized until the loan balance is 10% higher than the original loan balance when the borrower entered repayment. After that, interest continues to accrue but is not capitalized. Interest that accrues during forbearance or deferment does not count toward the 10% capitalization rule.

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[34] Under the Tax Code as it currently exists, student loan debt forgiven at the end of the IBR (and ICRP, unless it is forgiven under the Public Service Loan Forgiveness Program, discussed *infra*) term may constitute a taxable event. As noted above, this is a nonissue in most cases because any forgiven debt is taxable only to the extent the borrower is solvent. And again, it is not yet known what the ramifications will be, if any, under the bills passed by the House and the Senate.

The ICRP is the only income-driven payment option available to parent PLUS loan borrowers or to borrowers who have defaulted loans in the Direct Loan Program. The ICRP is always based on household income regardless of tax filing status. The term is 25 years. *But see infra* at III.B.3. After 25 years, any balance that is remaining is forgiven by the Secretary of Education. *See infra*. Note 6.

3. REPAYE:

a. Eligible Loans: Same as the IBR

b. Ineligible Loans: Same as the IBR.

c. Restoring IBR eligibility to defaulted loans: Same as the IBR

d. Partial Financial Hardship Threshold: Unlike the IBR, there is no partial financial hardship threshold for REPAYE.

e. REPAY Calculation and Terms: Like the IBR, the REPAYE payment is calculated using the borrower's AGI, from the most recent federal tax return, and family size. Borrowers who earn less than 150% of the poverty level for their family size will have a $0 REPAYE payment but will still be considered "in repayment" and in good-standing. However, the formula for calculating the REPAYE monthly payment is different from the IBR. The required monthly loan payment under the REPAYE is capped at 10% of annual household earnings above 150% of the applicable poverty level divided by 12 months. Like the IBR, the REPAYE payment is recalculated annually based on household AGI and family size.

Borrowers may contact their lender/servicer at any time if they experience a change in financial circumstances that could impact their required REPAYE payment. The REPAYE repayment period is 20 years for undergraduate loans, and 25 years for consolidation of graduate loans or a combination of graduate and undergraduate loans. At the conclusion of the 20 or 25-year repayment period, any remaining balance is forgiven. *But see infra* III.B.3 (discussing 10-year repayment term for the Public Service Loan Forgiveness Program).

Although interest continues to accrue at the contract rate in the REPAYE, the government will pay unpaid accrued interest on Direct Loan Program subsidized loans for up to three consecutive years from the date the borrower enters the REPAYE. Following the 3-year period, ED charges 50% of the remaining accrued interest on subsidized loans during periods of negative amortization. If monthly payment does not cover all interest, unpaid interest is capitalized when the borrower leaves the plan except that amount capitalized under these conditions is limited to 10% of the original principal balance at time borrower entered REPAYE Plan.

i. Documenting income: Same as IBR.

ii. Rules for married borrowers: The rules for married borrowers under the REPAYE are different than the IBR. Under the REPAYE, a borrower must provide income documentation for both the borrower and his or her spouse regardless of whether the borrower files a joint or separate Federal income tax return unless the borrower and his or her

spouse (1) are separated or (2) the borrower is unable to reasonably assess the borrower's spouse's income information.

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

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

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

During a deferment period, the government pays the interest accruing on subsidized loans. The borrower is responsible for interest that accrues on unsubsidized loans during a deferment. The borrower may pay the accruing interest on any unsubsidized loans or have it added to the principal when the deferment expires.

Forbearance postpones or reduces the monthly repayment for a limited, specific period, during which interest on subsidized and unsubsidized loans continues to accrue and is owed by the borrower. If the interest is not paid during the forbearance, it is added to the principal balance when the forbearance period ends.

V. PRACTICE TIPS AND POINTERS

Once an attorney determines that he or she will commence an adversary proceeding seeking an undue hardship of the debtor's student loans, there are a number of practical issues that should be addressed.

A. Who Has the Debtor's Loans? ED maintains an information repository called National Student Loan Data Systems ("NSLDS"). NSLDS is a database that contains information, including chain of custody, interest rate, loan type, loan status, etc., regarding every *federal* student loan a person has borrowed. Lenders, servicers, and guarantors have access to borrower NSLDS reports if they hold the loan. Borrowers may access their own NSLDS reports by going to www.nslds.ed.gov. They must first obtain a PIN at www.pin.ed.gov. Attorneys should work with their clients before filing an adversary to make sure that they include all of the debtor's federally-backed student loans.

B. Know *Who* to Name: When initiating a dischargeability action, debtors (with the assistance of their counsel if represented) should review the NSLDS to determine what entities hold a valid interest in their federally-backed loans. Debtors (and in many instances, their attorneys) often mistakenly name their student loan servicers in lieu of ED, the lender, and/or the guarantor likely because the servicer was the last entity who contacted them. Servicers do not hold any right, title, or interest in the loans and, therefore, are not proper parties in a dischargeability adversary proceeding.

For federally-backed loans obtained through the Direct Loan Program, ED is usually—if not always—the only party to hold a valid interest in a Direct Loan. But, in the FFEL Program, debtors who have non-defaulted loans should be sure to name both the lender *and* the guarantor. Naming just the lender will be problematic because the guarantor has a contingent interest in the student loan debt and is a creditor in its own right. Thus, the guarantor is entitled to separate notice and a right to defend its rights separate and apart from the lender. *See, e.g., Alfes v. Educ. Credit Mgmt Corp. (In re Alfes),* 709 F. 631 (6th Cir. 2013). In many adversary proceedings, the guarantor will seek to intervene or be substituted as a party defendant with respect to the federally-backed loan(s) it receives. That being said, it is the responsibility of the plaintiff to name the correct parties.

C. Is the Undue Hardship Adversary Ripe?: A Section 523 complaint, other than one under 11 U.S.C. §523(c), may be filed at any time. *See* Federal Rule of Bankruptcy Procedure 4007(b). That being said, even though a section 523(a)(8) complaint is permitted to be filed at any time does not necessarily mean that it should be filed prior to the time of discharge. In the typical chapter 7 case, that is not necessarily an issue since the discharge (assuming an objection to discharge is not filed under 11 U.S.C. §727) is likely to be granted relatively close in time to the filing of the bankruptcy case.

In a chapter 13 case, the issue is different since the debtor will not obtain a general discharge of any debts until all required payments under a chapter 13 plan are made and completed. For that reason, an undue hardship determination, if any, should not be made in a chapter 13 case until the debtor has received or is very close to receiving his or her chapter 13 discharge after making her required plan payments, assuming that any chapter 13 plan is even approved by the bankruptcy court. *See, e.g., In re Bender*, 368 F.3d 846 (8th Cir. 2004)(court affirmed district court decision that an undue hardship determination in a chapter 13 case made three-and-a-half years before the debtors would be entitled to a chapter 13 discharge was not ripe for adjudication as it presupposes the debtor will receive a discharge at all); *In re Rubarts*, 896 F.2d 107 (5th Cir. 1990)(undue hardship determination is not ripe until plan completion because dischargeability is not available until plan completion). *But see In re Coleman*, 560 F.3d 1000 (9th Cir. 2009)(undue hardship determination was ripe a year after the plan was confirmed but substantially in advance of plan completion).

From a practical standpoint, waiting until the end or near the end of the chapter 13 plan makes sense because even if the debtor is successful in obtaining an undue hardship judgment, the debt will not be discharged when the judgment is entered. Rather, the discharge of the debt is conditioned on the debtor actually obtaining the underlying general discharge in the main chapter 13 case. For that reason, most courts addressing the ripeness issue in the context of a chapter 13

case hold that it would be a waste of judicial resources (and those of the parties) to undergo the time and expense of litigating the undue hardship adversary until close to the time of discharge.

D. **Partial Discharge**. In some cases, debtors will include a separate count or request in their complaint to obtain a partial discharge of the underlying student loan debt, and will likely cite to the Bankruptcy Court's equitable powers under 11 U.S.C. §105. The Eleventh Circuit, however, in *In re Cox supra,* made clear that the use of section 105 is inappropriate for a partial discharge. Rather, the Eleventh Circuit held that in order to obtain even a partial discharge, a debtor must establish an undue hardship under 11 U.S.C. §523(a)(8) and satisfy all three prongs of the *Brunner t*est.

VI. INDUSTRY RESOURCES

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

VII. PANELIST CONTACT INFORMATION

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2018 Alexander L. Paskay Memorial Bankruptcy Seminar January 19, 2018

Student Loan Issues

Proposed New Legislation on Student Loan Dischargeability

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Currently, there are numerous pending bills in both the House of Representatives ("House") and the U.S. Senate ("Senate") that will impact student loans in general, such as:

(a) Student loan refinancing;

(b) Repayment options;

(c) Consumer protections and student loan servicers and accountability; and

(d) Tax treatment of student loans, deductibility for the payment of interest on student loans.

Below are some links which provide online resources that summarize the current status of the proposed legislation:

- www.coheao.com/tracking-federal-student-loan-proposals/
- http://studentloanbilltracker.com/
- https://www.nasfaa.org/legislative_tracker_loans_repayment
- www.congress.gov.

At the time these seminar materials were prepared and went to press, both the House and Senate were considering tax reform legislation which directly impacts student loans. For instance, the current version of the House bill on Tax Reform strips away almost all tax breaks afforded to students and teachers concerning student loans. Certain paid interest deductions, qualified tuition reductions as non-taxable and tuition waivers have been eliminated.

It remains to be seen what proposed legislation affecting student loans is ultimately passed and signed into law.

- https://www.forbes.com/sites/anthonynitti/2017/12/08/like-learning-youll-hate-the-house-tax-bill/#6af9751b7e70.

H.R.2366 - DISCHARGE STUDENT LOANS IN BANKRUPTCY ACT OF 2017

Summary:

This bill amends the federal bankruptcy code to permit a borrower to discharge in bankruptcy a nonprofit, government, or private student loan, or an obligation to repay an educational benefit, scholarship, or stipend.

Sponsor: Rep. Delaney, John K. [D-MD-6] (Introduced 05/04/2017)

Latest Action: House - 06/07/2017 Referred to the Subcommittee on Regulatory Reform, Commercial And Antitrust Law.

Date	All Actions
06/07/2017	Referred to the Subcommittee on Regulatory Reform, Commercial And Antitrust Law. Action By: Committee on the Judiciary
05/04/2017	Referred to the House Committee on the Judiciary. Action By: House of Representatives
05/04/2017	Introduced in House Action By: House of Representatives

H.R.2527 - PRIVATE STUDENT LOAN BANKRUPTCY FAIRNESS ACT OF 2017

Summary:

This bill amends the federal bankruptcy code to allow private education loans to be discharged in bankruptcy regardless of whether a debtor demonstrates undue hardship. Under current law, student loans may be discharged in bankruptcy only if the loans impose an undue hardship on the debtor.

Sponsor: Rep. Cohen, Steve [D-TN-9] (Introduced 05/18/2017)

Latest Action: House - 05/18/2017 Referred to the Subcommittee on Regulatory Reform, Commercial And Antitrust Law.

Date	All Actions
05/18/2017	Referred to the Subcommittee on Regulatory Reform, Commercial And Antitrust Law. Action By: Committee on the Judiciary
05/18/2017	Referred to the House Committee on the Judiciary. Action By: House of Representatives
05/18/2017	Sponsor introductory remarks on measure. (CR E661-662) Action By: House of Representatives

05/18/2017 Introduced in House
Action By: House of Representatives

H.R.137 - STOPPING ABUSIVE STUDENT LOAN COLLECTION PRACTICES IN BANKRUPTCY ACT OF 2017

Summary:

This bill amends the federal bankruptcy code to allow an individual whose student loan debt is discharged due to undue hardship to recover court costs and attorney's fees for the discharge proceeding if the court finds that the position of the creditor opposing the discharge was not substantially justified.

Sponsor: Rep. Conyers, John, Jr. [D-MI-13] (Introduced 01/03/2017)

Latest Action: House - 01/12/2017 Referred to the Subcommittee on Regulatory Reform, Commercial And Antitrust Law.

Date	All Actions Except Amendments
01/12/2017	Referred to the Subcommittee on Regulatory Reform, Commercial And Antitrust Law. Action By: Committee on the Judiciary
01/03/2017	Referred to the House Committee on the Judiciary. Action By: House of Representatives
01/03/2017	Introduced in House Action By: House of Representatives

S.1262 - FAIRNESS FOR STRUGGLING STUDENTS ACT OF 2017

Summary: **Exceptions to Discharge**

Section 523(a)(8) of title 11, United States Code, is amended by striking "dependents, for" and all that follows through the end of subparagraph (B) and inserting "dependents, for an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit or made under any program funded in whole or in part by a governmental unit or an obligation to repay funds received from a governmental unit as an educational benefit, scholarship, or stipend;".

Sponsor: Sen. Durbin, Richard J. [D-IL] (Introduced 05/25/2017)

Committees: Senate - Judiciary

Latest Action: Senate - 05/25/2017 Read twice and referred to the Committee on the Judiciary.

H.R.3630 - STUDENT LOAN BORROWERS' BILL OF RIGHTS ACT OF 2017

Summary: To establish student loan borrowers' rights to basic consumer protections, reasonable and flexible repayment options, access to earned credentials, and effective loan cancellation in exchange for public service, and for other purposes.

Sponsor: Rep. Wilson, Frederica S. [D-FL-24] (Introduced 07/28/2017)

Committees: House - Education and the Workforce; Ways and Means; Judiciary; Oversight and Government Reform

Latest Action: House - 07/28/2017 Referred to the Committee on Education and the Workforce, and in addition to the Committees on Ways and Means, the Judiciary, and Oversight and Government Reform, for a period to be subsequently determined by the Speaker, in each case for consideration of such provisions as fall within the jurisdiction of the committee concerned