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# Collection of Student Loans: A Critical Examination

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**Erratum**
A correction was uploaded on October 8, 2014 at the request of the author. At page 230 "one-twelfth of fifteen percent" now reads "one-twelfth of ten percent".

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*Doug Rendleman**
*Scott Weingart***

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* Huntley Professor Washington and Lee Law School. Thanks to Scott Weingart for taking the laboring oar that propelled this article forward. This project's genesis was a projected chapter in my book for Virginia lawyers. The subject's importance, complexity, and interest led to this lengthy article. A much shorter Chapter on Student Loan Collection will be published later this year in Doug Rendleman, Enforcement of Judgments and Liens in Virginia (Lexis Third Edition 2014).

** A.B., Princeton University, 2009, J.D., Washington & Lee University School of Law, 2013, Law Clerk for Magistrate Judge Joel Hoppe. Thanks to Phil Schrag for improving our understanding of education-finance and student loans and for reading our draft and making helpful and constructive suggestions. Thanks to Heather Jarvis for advice and encouragement. Thanks to the Journal editors and staff for prompt and efficient work. Thanks finally to the Frances Lewis Law Center for support. 

## *Introduction*

This Article deals with student loans from repayment to collection. Our technical descriptions, beginning with the types of loans and ending with bankruptcy, are crucial to understanding both the system and our policy evaluations in the conclusion. We seek to foster a dialogue culminating in a simpler and fairer system.

Student loans represent a large and growing share of consumer debt. In just the last ten years, aggregate student loan balances have quadrupled[1] due to growth in both college enrollment and tuition.[2] Outstanding student loan

1. FED. RESERVE BANK OF N.Y., *Quarterly Report on Household Debt and Credit*, (Nov. 2013), *available at* http://www.newyorkfed.org/householdcredit/2013-Q3/HHDC_2013Q3.pdf.

2. Meta Brown et al., *Grading Student Loans*, FED. RESERVE BANK OF N.Y. (Mar. 5,

balances now exceed outstanding credit card or auto loan balances.[3] Americans today owe more than $1 trillion in student loans either held or guaranteed by the federal government and about $165 billion in private student loans.[4]

Student debt has serious consequences for borrowers struggling to make ends meet. A recent study found that 40% of students delayed a major purchase, such as a home or car, because of student loan debt, and more than a quarter moved in with parents or family members to save money.[5] A similar proportion dropped out of school or put off continuing their education.[6] One borrower interviewed by the New York Times was working three jobs to pay off the $70,000 of student loan debt she incurred before dropping out of college.[7]

Seventy-one percent of graduates from four-year programs had student loans, with wide variations. Data on private loans are limited; parental borrowing isn't included. Undergraduate debt averages $29,400.[8] Abuses occur in the for-profit sector where 88% of students borrowed with an average debt $39,950.[9] The DOE attempts to reduce abuses with what it calls the "Gainful Employment" test that controls college programs access to federal student aid.[10] Student debts for professional schools like medicine

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2012), http://libertystreeteconomics.newyorkfed.org/2012/03/grading-student-loans.html.

3. *See* FED. RESERVE BANK OF N.Y., *supra* note 1 (discussing the types of debt held by Americans).

4. Rohit Chopra, *Student Loan Debt Swells, Federal Loans Now Top a Trillion*, CONSUMER FIN. PROTECTION BUREAU (July 17, 2013), http://www.Consumer finance.gov/newsroom/student-debt-swells-federal-loans-now-top-a-trillion/; U.S. DEP'T OF EDUC., *Federal Student Aid Portfolio Summary*, http://studentaid.ed.gov/sites/default /files/fsawg/datacenter/library/PortfolioSummary.xls [hereinafter *Federal Student Aid Portfolio Summary*] (last visited Feb. 12, 2014).

5. Charley Stone, Carl Van Horn & Cliff Zukin, *Chasing the American Dream: Recent College Graduates and the Great Recession*, RUTGERS SCH. PLANNING & PUB. POL'Y at 13 (May 2012), *available at* http://media.philly.com/documents/20120510_Chasing _American_Dream.pdf.

6. *Id.*

7. *See* Andrew Martin & Andrew W. Lehren, *A Generation Hobbled by the Soaring Cost of College*, N.Y. TIMES (May 12, 2012), http://www.nytimes.com/2012/ 05/13/business/student-loans-weighing-down-a-generation-with-heavy-debt.html?page wanted=all&_r=0 (discussing the rising debt many students take on to afford college).

8. Beckie Supiano, *Borrowers' Average Debt at Graduation Climbs to $29,400*, CHRON. HIGHER EDUC. (Dec. 4, 2013).

9. *Id.*

10. Kelly Field, *More Programs Would Fall Under New 'Gainful Employment' Proposal*, CHRON. HIGHER EDUC. (Dec. 12, 2013).

and law as well as graduate degrees reach in the $100,000 to $200,000 range, some more.[11] Of the major types of household debt, the rate of delinquent payments is highest among student loans, at 11.5 percent.[12]

This Article will give these borrowers and their attorneys a better understanding of student loan debt. Part I briefly describes the types of student loans that borrowers might have. Part II considers repayment of student loans; it outlines a student's options for avoiding default. Part III discusses how student loans fall into default and what happens once they get there; it includes the government's administrative techniques to collect a defaulted student loan. Part IV describes the borrower's two primary options for getting out of default: consolidation and rehabilitation. Part IV addresses discharge of student loan debt, discussing both statutory discharge and discharge in bankruptcy.

A student loan resembles a labyrinth; it's easy for you to enter, but once you get into trouble, it is difficult, maybe impossible, to exit. We turn to the entrance—what forms may a student loan take?

## *I. Types of Student Loans*

There are two types of student loans: first, "federal" student loans, which are issued pursuant to a federal program and governed by a substantial body of federal law; and second, "private" student loans, which are issued by states, financial institutions, and schools, and are, for most purposes, governed only by generally applicable laws regulating financial credit products.

### *A. Federal Student Loans*

Federal student loans are issued under three programs: the Federal Direct Loan Program,[13] the Federal Perkins Loan Program,[14] and Federal

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11. Audrey Williams June, *The Cost of a Ph.D.: Students Report Hefty Debt Across Many Fields*, CHRON. HIGHER EDUC. (Jan. 16, 2014).

12. Danielle Douglas, *Household Debt Grows, but Americans Seem More Cautious*, WASH. POST (February 19, 2014), at A8.

13. 20 U.S.C. §§ 1087a–1087j (2012). The Direct Loan statute borrows many provisions from sections governing FFEL loans. *See, e.g.*, 20 U.S.C. § 1078-2(a)(2) (providing that Direct loans "have the same terms, conditions, and benefits as loans made to borrowers under" the FFEL program, unless otherwise specified in the sections governing Direct loans).

Family Education Loan (FFEL) Program.[15] Direct and FFEL loans can be further classified into two types of loans: Stafford and PLUS loans. Stafford loans provide more favorable terms to borrowers and are made regardless of credit history, but are subject to annual and aggregate limits that fall short of what many students need.[16] Some Stafford loans are subsidized—which means that the loan principal accrues no interest while the student borrower is attending school. Subsidized Stafford loans are available only to students who demonstrate financial need.[17] As of July 2012, they are not available to graduate students. Stafford loans are by far the most prevalent student loan product, typically comprising between 60 and 80 percent of annual student lending (including private loans).[18]

PLUS loans carry a higher interest rate.[19] They are available only to graduate students or parents of undergraduates.[20] Eligibility for PLUS loans depends on credit history. PLUS loans account for roughly fifteen cents of every dollar in student loans taken out in the last three years.[21]

Under the Direct Loan Program, the federal government lends money directly to students attending qualifying institutions of higher education. Typically, either the school of attendance or an "alternative originator" will originate the loan,[22] and the Department of Education will contract with third parties to service loans.[23] Interest rates for direct loans issued before July 1, 2006 are variable, subject to a cap of 8.25% or 9%, depending on the type of loan.[24] Interest rates for loans issued since July 1, 2006 are fixed at 6.8% for most Stafford loans and 7.9% for PLUS loans.[25] Interest accrues

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14. 20 U.S.C. §§ 1071–1087-4 (2012).

15. 20 U.S.C. §§ 1087aa–ii (2012).

16. *See* 20 U.S.C. § 1078-8(d) (2012) (detailing annual and aggregate limits for student borrowers); *see also* 34 C.F.R. § 685.203.

17. *See* 20 U.S.C. § 1078(a)(2) (2012) (requiring borrowers to submit a statement setting forth the loan amount for which the student shows financial need).

18. COLLEGE BD., *Trends in Student Aid 2013*, TRENDS IN HIGHER EDUC. at 17, https://trends.collegeboard.org/sites/default/files/student-aid-2013-full-report. pdf, (2013) [hereinafter COLLEGE BD.].

19. *See* COLLEGE BD., *supra* note 18, at 9 (analyzing the terms of PLUS loans).

20. *See* COLLEGE BD., *supra* note 18, at 9.

21. *See* COLLEGE BD., *supra* note 18, at 9-12.

22. 20 U.S.C. § 1087b(a) (2012).

23. 20 U.S.C. § 1087f (2012).

24. 20 U.S.C. § 1087e(b)(1)–(6) (2012).

25. 20 U.S.C. § 1087e(b)(7) (2012). Undergraduate Stafford loans issued between July 1, 2006 and July 1, 2013 are subject to reduced rates. 20 U.S.C. § 1087e(b)(7)(D) (2012).

only on the unpaid principal balance.[26] Origination fees for loans issued since 2010 are fixed at 1% of principal amount for Stafford loans and 4% of principal amount for PLUS and consolidation loans.[27] As of the second quarter of 2013, some 24.1 million borrowers owed roughly $553.0 billion on Direct loans.[28]

Students with demonstrated financial need are eligible for Perkins loans.[29] Perkins loans are the most affordable federal student loan product, with interest rates currently fixed at five percent.[30] Like some Stafford loans, they do not incur interest while the student is in school.[31] Under the Perkins program, eligible schools establish a student loan fund, which the federal government helps support through capital contributions.[32] Schools issue loans to eligible students from the fund and are responsible for collecting principal and interest from borrowers.[33] The Perkins program is very limited in scope, accounting for less than 1% of student loan disbursements in recent years.[34] Outstanding Perkins loan balances total to just $8.3 billion.[35]

Under the FFEL program, private financial institutions loaned to students. These loans are insured by guaranty agencies—nonprofit or government entities that bear most of the responsibility for administering the FFEL program—which are reinsured by the Department of Education.[36]

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26. 20 U.S.C. § 1087e(b)(8) (2012).

27. 20 U.S.C. § 1087e(c) (2012).

28. *Federal Student Aid Portfolio Summary*, *supra* note 4.

29. 20 U.S.C. § 1087dd(b)(1) (2012); *see also* 20 U.S.C. §§ 1087kk–vv (2012).

30. *See* 20 U.S.C. § 1087dd(c)(1)(D) (fixing the interest at five percent for loans made after Oct. 1, 1981); *see also* 34 C.F.R. § 674.31(b)(1)(i) (2012) (requiring that the promissory note state the rate of interest of the loan be five percent).

31. 20 U.S.C. § 1087dd(c)(1)(D) (2012); 34 C.F.R. § 674.31(b)(1)(ii) (2012).

32. 20 U.S.C. § 1087cc(a)(2) (2012).

33. *Id.*

34. COLLEGE BD., *supra* note 18, at 10, 17.

35. *Federal Student Aid Portfolio Summary*, *supra* note 4.

36. Guaranty agencies typically served student-borrowers in a particular state or group of states. The guaranty agency for Virginia is the Educational Credit Management Corporation, a nonprofit corporation organized under the law of Minnesota. Some guaranty agencies are arms of state government, a fact that may have several consequences. First, the state action doctrine is more likely to apply, so that agency action must comply with the federal (and perhaps also the state) constitution. Additionally, if the agency acts "under color of state law," a plaintiff suing the agency for a violation of federal law may have a claim under 42 U.S.C. § 1983, provided that the agency is a "person" within the meaning of § 1983. Second, the doctrine of sovereign immunity may bar offensive suits for damages

Since Congress has abolished the FFEL program, the federal government now issues all Stafford and PLUS loans.[37] FFEL regulations remain important, however, as 21.6 million borrowers still owe $437.0 billion on FFEL loans issued before 2010.[38]

### *B. Private Student Loans*

Private student loans are not issued pursuant to a federal program. These loans may come from a variety of sources, including financial institutions, nonprofit organizations, states, and even schools themselves. Private student loans typically carry higher interest rates than federal loans and may also subject buyers to prepayment penalties.[39] For the most part, the law treats these loans as any other credit product, with one key exception, which we turn to below: like federal student loans, many private student loans are exempted from discharge from bankruptcy.[40]

The rate of private student lending has varied substantially over the past decade. In the early and mid 2000s, private student loans grew quickly. In just four years, the share of undergraduate students taking out private student loans tripled.[41] By the 2006–07 and 2007–08 academic years, private student loans accounted for 25% of total student lending.[42] Private student lending fell sharply during the recession, and despite increases in the most recent academic year, it remains at less than 40% of peak levels.[43] In the 2012–13 academic year, these lenders issued roughly $8.8 billion in student loans.[44]

The common understanding is that once a borrower owes a creditor money, she repays the loan. That is our next subject.

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against the agency. Third, judicial review of agency action may be available in state court.

37. Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, § 2201, 124 Stat. 1029, 1074–75 (2010).

38. *Federal Student Aid Portfolio Summary*, *supra* note 4.

39. U.S. DEP'T OF EDUC., *Your Federal Student Loans: Learn the Basics and Manage Your Debt*, FED. STUDENT AID at 8–9 (2010), *available at* https://studentaid.ed.gov/sites/default/files/your-federal-student-loans_1.pdf.

40. *See infra* Part V-B (discussing student loans in bankruptcy).

41. *Private Loans: Facts and Trends*, PROJECT ON STUDENT DEBT (July 2011), http://projectonstudentdebt.org/files/pub/private_loan_facts_trends.pdf.

42. COLLEGE BD., *supra* note 18, at 10.

43. *Id.*

44. *Id.*

### *II. Staying out of Default: Student Loan Repayment*

Because student loan default carries the serious consequences we develop below,[45] a borrower's wisest course of action is not to default in the first place. Fortunately, statutes and regulations offer borrowers an array of tools to avoid defaulting on federal student loans. A borrower may postpone payments on student loans through deferments or forbearances. She may structure repayment of the loan according to a range of payment schedules, some of which set payments based on her income. Her loans may be forgiven after twenty-five years of payments under an income-dependent plan.[46] Finally, a borrower may obtain repayment assistance or cancellation based on service in a public-interest profession.

Most of the statutory repayment options and default-avoidance strategies discussed in this Subparts A, B, and C are available only for FFEL and Direct loans. A Perkins borrower may pursue a different set of statutory default-avoidance options, which we discuss separately in Subpart D. Furthermore, all federal student loan borrowers may obtain relief from full repayment through statutory cancellation and forgiveness discussed in Part V. Borrowers of private student loans generally do not have access to these tools, with the exception of certain Loan Repayment Assistance Programs. Finally, one method of postponing repayment obligations applies to all student loans: filing for bankruptcy.[47]

#### *A. Postponing repayment: deferment and forbearance*

A borrower enjoys a grace period of six months before her first payment is due after ceasing enrollment in school on at least a half-time basis for Direct Stafford loans.[48] The repayment period for Direct PLUS

45. *See infra* Part III (discussing student loans in delinquency and default).

46. See U.S. DEP'T OF EDUC., Income-Based Plan, Fed. Student Aid, available at http://studentaid.ed.gov/repay-loans/understand/plans/income-based (setting forth advantages of the Income-Based Repayment Plan (IBR), including the twenty-five year forgiveness advantage whereby one may be forgiven of their remaining loan balance after twenty-five years of qualifying repayment).

47. *See infra* Part V-B (discussing student loans in bankruptcy).

48. 34 C.F.R. §§ 685.207(b)(1)(ii), (c)(1)(ii) (2009); *see also* 34 C.F.R. § 682.209(a)(2)–(5) (2013) (regulations for FFEL grace periods).

loans begins the day the loan is fully disbursed,[49] but a borrower who is in school may obtain an in-school deferment.[50]

Once a federal student loan enters repayment status, a borrower may postpone repayment by obtaining either a deferment or forbearance. This section begins with deferments, which are typically more favorable to borrowers before moving to forbearance.

A borrower not in default[51] may be eligible for one of a number of deferments of payments on her FFEL and Direct Loans.[52] During a deferment period, "periodic installments of principal and interest need not be paid."[53] In general, a borrower does not automatically receive deferments, but instead must request them from her lender.[54] Interest accrues on unsubsidized FFEL and Direct loans.[55] Moreover, the lender may capitalize—that is, add accrued interest (as well as unpaid insurance premiums for FFEL loans) to the unpaid principal balance.[56] A borrower may avoid capitalization by paying the interest that accrues during the period of deferment.[57]

The grounds for deferment are many. The two most important grounds for deferment are enrollment in school[58] and economic hardship.[59] Others

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49. 34 C.F.R. § 685.207(d) (2009).

50. 34 C.F.R. § 685.204(b)(1) (2009).

51. Borrowers in default must have made repayment arrangements satis-factory to the holder of the loan to be eligible for a deferment. 34 C.F.R. §§ 685.204(h) (Direct), 682.210(a)(8) (FFEL).

52. *Id*.

53. 34 C.F.R. §§ 685.204(a)(1) (Direct), 682.210(a)(1) (FFEL).

54. *See, e.g.*, 34 C.F.R. §§ 685.204(i)(1) (Direct), 682.210(d)(1) (FFEL graduate fellowship deferment), (f)(1) (FFEL temporary total disability deferment), (o)(1) (FFEL parental leave deferment). For most types of deferments, borrowers must provide supporting documentation as well. *Cf.* 34 C.F.R. § 685.204(i)(2) (listing deferments which may be granted for Direct Loans on verbal application alone). In-school deferments may be processed without application from the borrower. 34 C.F.R. §§ 685.204(i)(1), 682.210(c)(1)(ii)–(iv) (FFEL). Additionally, a lender may grant a military service deferment upon application from a borrower's representative. 34 C.F.R. §§ 685.204(i)(1), 682.210(t)(7).

55. 34 C.F.R. §§ 685.204(a)(2) (Direct), 682.210(a)(3)(i)(B) (FFEL).

56. 34 C.F.R. §§ 685.202(b) (Direct), 682.202(b) (FFEL). If a loan is subsidized, capitalization is not a concern during deferments because the interest owed by the borrower does not accrue during the deferment period. 34 C.F.R. §§ 685.204(a)(1) (Direct), 682.210(a)(3)(i)(A) (FFEL).

57. 34 C.F.R. §§ 685.204(a)(2), 682.210(a)(3)(ii).

58. 34 C.F.R. § 685.204(b)(1)(i)(A) (Direct) (generally, enrollment in school means at least one-half the normal full-time work load for the course of study that the borrower is

include active duty military service,[60] pregnancy or parental leave,[61] unemployment,[62] disability of the borrower or a spouse or dependent,[63] and enrollment in a medical internship or residency program.[64] Deferments may also be available to borrowers engaged in certain public interest work.[65] Not all grounds for deferment apply to all loans; some are limited to loans extended during a particular period, and some deferments are only available for a limited period of time.[66]

A borrower struggling to repay loans may also qualify for forbearance, which is "the temporary cessation of payments, allowing an extension of time for making payments, or temporarily accepting smaller payments than previously were scheduled."[67] The purpose of forbearance is "to prevent the borrower or endorser from defaulting on the borrower's or endorser's repayment obligation, or to permit the borrower or endorser to resume honoring that obligation after default."[68]

A borrower who qualifies for forbearance generally has the option to choose which type of forbearance to accept, though temporary cessation of payments is the default option.[69] Interest accrues during any period of forbearance,[70] and, for most FFEL and Direct Loans, is capitalized.[71] A borrower may avoid capitalization by paying interest that accrues during the period of forbearance.[72] Certain grounds for forbearance are administrative and are granted upon either an oral request from the borrower or no request

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pursuing); 34 C.F.R. § 682.210(b)(1)(i), (b)(4), (c), (s)(2) (FFEL) (requiring at least half-time study for deferment). Different regulations apply to loans first disbursed on or after July 1, 2008. 34 C.F.R. §§ 685.204(g); 682.210(v).

59. 34 C.F.R. § 685.204(b)(3), (c); 34 C.F.R. § 682.210(s)(6).

60. 34 C.F.R. § 685.204(e), (f); 34 C.F.R. § 682.210(b)(2)(i), (t), (u).

61. 34 C.F.R. § 682.210(b)(3)(i), (o).

62. 34 C.F.R. § 685.204(b)(2), (c); 34 C.F.R. § 682.210(b)(1)(v), (b)(3)(ii), (h), (s)(5).

63. 34 C.F.R. § 682.210(b)(1)(iv), (f), (g).

64. 34 C.F.R. § 682.210(b)(2)(v), (b)(5)(iii), (n).

65. 34 C.F.R. § 682.210(b)(2)(i)–(iv), (5)(i)–(ii).

66. *See, e.g.*, 34 C.F.R. § 685.204(c) (stating a borrower may only receive three years of either economic hardship or unemployment deferments).

67. 34 C.F.R. §§ 685.205(a) (Direct), 682.211(a)(1) (FFEL), 674.33(d)(1) (Perkins).

68. 34 C.F.R. § 682.211(a)(1)

69. 34 C.F.R. §§ 685.205(a), 682.211(g), 674.33(d)(4).

70. 34 C.F.R. §§ 685.205(a) (Direct), 682.211(e)(2)(iii) (FFEL), 674.33(d)(7) (Perkins).

71. 34 C.F.R. §§ 685.205(a), 682.211(e)(2)(v).

72. *Id.*

at all.[73] In other cases, the borrower must request forbearance from the secretary or lender in writing and, if necessary, provide documentation supporting the request.[74] Unlike deferments, forbearances may be granted to a borrower in default.

As with deferment, grounds for forbearance differ depending on the type of loan. A borrower is entitled to forbearance when her debt burden exceeds 20% of her monthly gross income,[75] while she participates in a medical or dental internship or residency program (provided she is not eligible for deferment),[76] while she serves in a national service position for which she has received an award under the National and Community Service Act,[77] and while she serves in a teaching position that qualifies for teacher loan forgiveness.[78] Forbearance will also be granted to borrowers during a national emergency, as declared by the Secretary, and to borrowers in disaster areas.[79] Certain active duty and post-active duty service members may also be eligible for mandatory forbearance.[80] Finally, if a borrower will be unable to repay the loan within the maximum repayment period (generally ten years) either because of the effect of variable interest rate on a standard or graduated repayment schedule or because of income-sensitive repayment plan, forbearance may be granted for a limited period of time, either three or five years, depending on the circumstances.[81]

In other circumstances, the Secretary will grant forbearance to Direct Loan borrowers, while forbearance on FFEL loans is "discretionary." The

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73. *See* 34 C.F.R. §§ 685.205(b) (setting forth circumstances where the Secretary will grant forbearance without requiring documentation from the borrower), 682.211(i) (mandatory administrative forbearance).

74. 34 C.F.R. §§ 685.205(a), 682.211(f), (h).

75. 34 C.F.R. §§ 685.205(a)(6) (Direct), 682.211(h)(2)(i) (FFEL).

76. 20 U.S.C. § 1087(c)(3)(A)(i)(I) (FFEL); 34 C.F.R. §§ 685.205(a)(3) (Direct), 682.211(h)(1) (FFEL).

77. 20 U.S.C. § 1087(c)(3)(A)(i)(III) (FFEL); 34 C.F.R. §§ 685.205(a)(4) (Direct), 682.211(h)(2)(ii)(A) (FFEL).

78. 34 C.F.R. §§ 685.205(a)(5) (Direct), 682.211(h)(2)(ii)(C) (FFEL).

79. 34 C.F.R. §§ 685.205(b)(8) (2010) (Direct), 682.211(i)(2)(i)–(ii) (2013) (FFEL); *see also* 34 C.F.R. § 682.211(f)(2) (establishing discretionary FFEL forbearance for up to 60 days when borrower's ability to repay has been adversely affected by a disaster or other emergency).

80. *See* 20 U.S.C. § 1078(c)(3)(A)(i)(IV) (2011) (stating that an individual may be "eligible for interest payments to be made on such loan for service in the Armed Forces . . . ."); *see also* 34 C.F.R. §§ 685.205(a)(7), 682.211(h)(2)(ii)(B), (h)(2)(iii) (establishing forbearance for a member of the National Guard).

81. 34 C.F.R. §§ 685.205(b)(7) (Direct), 682.211(i)(5) (FFEL).

Secretary must grant forbearance of direct loans for the period necessary to determine the borrower's eligibility for discharge.[82] FFEL lenders may also grant forbearance for the period necessary to investigate the borrower's death or total and permanent disability.[83] The Secretary must, and a FFEL lender may, grant forbearance for up to sixty days to "collect and process documentation supporting the borrower's request for a deferment, forbearance, change in repayment plan, or consolidation loan."[84] The Secretary must, and a FFEL lender may, retroactively grant forbearance during a properly granted deferment period for which the Secretary or lender later learns that the borrower did not qualify.[85] Forbearance is also available to borrowers during several transitional periods around events like the sale or transfer of a loan or a change in repayment plan.[86] Finally, the secretary will grant forbearance when the borrower demonstrates inability to make payments due to poor health or other acceptable reasons.[87]

### *B. Structuring and extending repayment*

FFEL and Direct Loan borrowers may choose from an extensive menu of loan repayment plans: standard, graduated, extended, income-based, income-contingent, income-sensitive, and pay-as-you-earn. The first three plans—standard, graduated, and extended repayment—set payments solely based on outstanding amount of the loan, and are available to all borrowers. Payments in the remaining four plans are based, at least in part, on a borrower's income. Not all of these plans are available for all types of loans, and most are available only to borrowers who demonstrate some degree of financial hardship.

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82. 34 C.F.R. § 685.205(b)(5) (death or total/permanent disability), (b)(6)(i)–(iii) (school related), (b)(6)(iv) (teacher loan forgiveness).

83. *See* 34 C.F.R. §§ 682.211(i)(6) (establishing mandatory 60 day administrative forbearance to investigate the borrower's, or the student's, in case of a parent PLUS loan, death), (f)(7) (establishing additional discretionary 60 day forbearance to investigate borrower's death), (f)(5) (governing when an individual has total and permanent disability).

84. 34 C.F.R. §§ 685.205(b)(9) (Direct); 682.211(f)(11) (FEEL) (stating that interest accrued during this period is not capitalized).

85. 34 C.F.R. §§ 685.205(b)(1), 682.211(f)(1).

86. *See* 34 C.F.R. §§ 685.205(b)(2)–(4), (10); 682.211(f)(2)–(4), (9), (10), (14), (15) (discussing multiple periods of delinquency).

87. *See* 34 C.F.R. § 685.205(a)(1) ("The Secretary determines that, due to poor health or other acceptable reasons, the borrower or endorser is currently unable to make scheduled payments. . . .").

Under standard and graduated repayment plans, a borrower has between five and ten years to repay most Direct and FFEL loans.[88] Under a standard repayment plan, monthly payments are fixed;[89] under the graduated plan, monthly payments change (typically by increasing), over the term of the loan,[90] but the minimum and maximum monthly payments differ by no more than a factor of three.[91]

The extended repayment plan is an intermediate option between the standard and graduated plans and the income-dependent plans. Like the income-dependent repayment plans, it extends the maximum repayment period, typically to twenty-five years.[92] As under standard repayment plans, a borrower must make minimum monthly payments of $50.[93] Payment amounts under extended repayment plans may be either fixed or graduated.[94]

As their names suggest, the income-sensitive, income-based, income-contingent, and pay-as-you-earn plans all set payments based on the borrower's income. An income-sensitive repayment (ISR) plan is available only for a FFEL loan. The ISR plan differs from income-contingent and income-based plans in three significant respects, each of which makes ISR substantially less favorable to the FFEL borrower than IBR: first, the maximum repayment period is extended by only five years under income-sensitive plan, as opposed to fifteen for IBR and ICR, second, a borrower does not become eligible for forgiveness based on payment under an ISR

88. The period is set at ten years for Direct loans, 34 C.F.R. § 685.208(b)(1) (standard), (g)(1) (2013) (graduated), except that the maximum period is longer and depends on the total amount of outstanding student loans for consolidation loans of borrowers who entered repayment after July 1, 2006. *Id.* § 685.208(c)(1) (standard), (h)(1) (graduated), and for loans of borrowers who entered repayment before that date and are paying under graduated repayment plan. *Id.* § 685.208(f)(1). For FFEL loans, the lender fixes the term between five and ten years, 34 C.F.R. § 682.209(a)(7)(i) (2013), except that the repayment period for consolidation loans is between ten and thirty years, depending on the amount of outstanding student loans. *Id.* § 682.209(h).

89. 34 C.F.R. §§ 685.208(b)(1), (c)(1) (2013), 682.209(a)(6)(vi) (2013).

90. 34 C.F.R. §§ 685.208(f)(1), (g)(1), (h)(1), 682.209(a)(6)(vii).

91. 34 C.F.R. §§ 685.208(f)(3), (g)(3), (h)(2), 682.209(a)(6)(ii) (requiring that any single installment may not be more than three times greater than any other installment).

92. 34 C.F.R. §§ 685.208(d)(1), (e)(1), 682.209(a)(6)(ix), (a)(7)(i).

93. *See* 34 C.F.R. §§ 682.209(c)(i) (establishing a "minimum annual payment" on FFELs of $600), FFELs are not subject to this minimum if the borrower and lender agree otherwise. 34 C.F.R. § 682.209(c)(1)(ii). Graduated repayment plans are generally not subject to the $50 minimum. 34 C.F.R. §§ 685.208(f)(3), (g)(3), (h)(2), 682.209(a)(6)(ii).

94. 34 C.F.R. §§ 682.208(e)(1), 682.209(a)(6)(ix).

plan,[95] and, third, the borrower must pay at least the accrued interest each month.[96] As with IBR and ICR, a borrower paying under an ISR plan must provide annual-income information to the lender.[97]

A direct loan borrower may use an Income Contingent Repayment (ICR) plan. ICR plan payments are capped at 20% of the difference between the borrower's adjusted gross income and the relevant federal poverty guideline.[98] Since this limit is higher than the limit for IBR or pay-as-you-earn, a borrower who is eligible for either of those plans is probably better off opting for one of them over an ICR plan. An ICR plan may still be a worthwhile option for some borrowers for two reasons: first, a borrower may enter an ICR plan regardless of hardship, and, second, eligibility extends to *all* Direct loans not in default, including consolidation loans, regardless of whether the consolidation loan was used to repay a parent PLUS loan. As with IBR, accrued interest is capitalized; however, capitalization ceases once the outstanding principal amount is ten percent greater than the original principal amount.[99]

Except for parent PLUS loans and consolidation loans taken out in part to repay a parent PLUS loan, all Direct and FFEL loans that are not in default are eligible for IBR.[100] A borrower must have "partial financial hardship" to enter IBR; a borrower who files an individual tax return is deemed to have partial financial hardship when her payments under a standard repayment plan would exceed payments under IBR.[101] A borrower must certify her family size to the holder of the loan annually, and, for Direct Loans, she must also consent to disclosure of tax return information by the IRS to the loan holder.[102]

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95. *See* 34 C.F.R. § 682.209(a)(6)(viii)(D), (E) (requiring repayment within 15 years).

96. 20 U.S.C. § 1078(b)(9)(A)(iii) (2011); 34 C.F.R. § 682.209(a)(6)(iv).

97. 34 C.F.R. § 682.209(a)(6)(viii)(B), (C).

98. 34 C.F.R. § 685.209(b)(1)(ii)(A)–(B).

99. 34 C.F.R. § 685.209(b)(3)(iv).

100. 34 C.F.R. §§ 685.221(a)(2), 682.215(a)(2).

101. 34 C.F.R. §§ 685.221(a)(4)(i), 682.215(a)(4)(i); *see also* 34 C.F.R. §§ 685.221(a)(4)(ii), 682.215(a)(4)(ii) (establishing requirements for married borrowers filing a joint tax return).

102. *See* 34 C.F.R. §§ 685.221(e)(1), 682.215(e)(1); *see also* 34 C.F.R. §§ 685.221(e)(2), 682.215(d)(1), (e)(7) (stating that borrowers already in IBR who fail to provide the required documentation remain in the plan, but their repayments are recalculated as if the borrower does not have partial financial hardship).

When a borrower who qualifies for IBR enters the plan, monthly payments on all eligible loans are limited to one-twelfth of fifteen percent of the difference between the borrower's adjusted gross income and 150% of the poverty guideline for the borrower's family size.[103] For new borrowers—defined as those who have no outstanding Direct or FFEL loans as of July 1, 2014—monthly payments are one-twelfth of ten percent of the difference between AGI and 150% of the poverty guideline.[104] Payments are applied to accrued interest, collection costs, late charges, and principal, in that order.[105] Interest accrues during IBR, except on subsidized Stafford loans or the subsidized portion of consolidation loans during the first three years of IBR.[106] Unpaid interest accrued during IBR is capitalized when the borrower leaves the plan or no longer qualifies.[107]

If a borrower paying under an IBR plan no longer has partial financial hardship or chooses to stop making income-based payments, her monthly payment is recalculated to equal what it would have been at the time she entered IBR.[108] In that case, the borrower remains in the IBR plan; she may choose to make the reduced payments if she should encounter further hardship; and, in any event, she is not obligated to repay the loan within ten years.[109] If a borrower *leaves* the IBR plan, the ten-year maximum repayment period applies.[110]

In November 2012, the Department of Education rolled out a new income-dependent repayment plan for certain Direct loan borrowers—the "pay-as-you-earn" plan.[111] Pay as you earn is only available to borrowers who first received FFEL or Direct loans on October 1, 2007 or later.[112] Additionally, only Direct loans disbursed after October 1, 2011 (or, in the

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103. 34 C.F.R. §§ 685.221(b)(1), 682.215(b)(1); 34 C.F.R. §§ 685.221(b)(2)(i), 682.215(b)(1)(i) (explaining payments are allocated between lenders based on the amount of outstanding principal on qualifying loans held); *see also* 34 C.F.R. §§ 685.221(b)(2)(ii)–(iv), 682.215(b)(1)(ii)–(iv) (explaining adjustments are also made for certain married filers and borrowers whose calculated payment is less than $10.00).

104. 34 C.F.R. § 685.221(b)(1).

105. 34 C.F.R. §§ 685.221(c)(1)(i)–(iv), 682.215(c)(1)(i)–(iv).

106. 34 C.F.R. §§ 685.221(b)(3), 682.215(b)(4).

107. 34 C.F.R. §§ 685.221(b)(4), 682.215(b)(5).

108. 34 C.F.R. §§ 685.221(d)(1)(i), 682.215(d)(1)(i).

109. 34 C.F.R. §§ 685.221(d)(1)(ii), 682.215(d)(1)(ii).

110. 34 C.F.R. §§ 685.221(d)(2)(i), 682.215(d)(2).

111. 77 Fed. Reg. 66088 (Nov. 1, 2012) (to be codified at 34 C.F.R. parts 674, 682, 685).

112. 34 C.F.R. § 685.209(a)(1)(iii)(A).

case of Direct consolidation loans, applied for after October 1, 2011) are eligible for pay as you earn.[113] As with IBR, a borrower must demonstrate partial financial hardship to repay on a pay-as-you-earn plan.[114] For eligible borrowers, the pay-as-you-earn plan will usually offer the most favorable repayment terms of all income-dependent plans, because it combines the best features of IBR and ICR plans. Monthly payments are limited to one-twelfth of ten percent of the difference between the borrower's adjusted gross income and 150% of the poverty guideline for the borrower's family size—1/3 lower than the current IBR repayment amount.[115] Accrued interest is capitalized when a borrower leaves the pay-as-you-earn plan or no longer has financial hardship, but only up to ten percent of the original principal amount.[116] Finally, if the monthly payment under pay as you earn is insufficient to pay accrued interest, the government will not charge the remaining accrued interest for a period of up to three years.[117]

One important feature of all income-dependent repayment plans is the availability of student loan forgiveness. To qualify for loan forgiveness, a borrower in an income-based or income-contingent repayment plan must make either 25 years of monthly payments or the equivalent of 25 years of payments through actual payments and economic hardship deferments.[118] Borrowers who choose the pay-as-you-earn plan must make only 20 years of payments or the equivalent in payments and economic hardship deferments.[119] The determination of whether a borrower is entitled to forgiveness is made by the guaranty agency for FFEL loans and the Secretary for Direct Loans.[120]

Loan forgiveness offers the borrower who cannot repay her loans a way out of the student loan maze. But it has one major drawback. The internal revenue code generally treats "income from discharge of

113. 34 C.F.R. § 685.209(a)(1)(iii) (2013).

114. 34 C.F.R. § 685.209(a)(1)(v), (2)(i) (2013).

115. 34 C.F.R. § 685.209(a)(2)(i) (2013).

116. 34 C.F.R. § 685.209(a)(2)(iv) (2013).

117. 34 C.F.R. § 685.209(a)(2)(iii) (2013).

118. 20 U.S.C. §§ 1087e(d)(1)(D), 1098e(b)(7) (2010); 34 C.F.R. §§ 685.221(f)(1), (f)(2), 682.215(f)(1), (f)(2) (2013). Payments made to rehabilitate a defaulted loan do not count toward the twenty-five year period. 34 C.F.R. § 682.215(f)(5). "New" (Post-2014) IBR borrowers will have to make only 20 years' worth of payments or the equivalent. 34 C.F.R. § 685.221(f)(1) (2013).

119. 34 C.F.R. § 685.209(a)(6)(ii) (2013).

120. 34 C.F.R. §§ 685.221(f)(2), 682.215(f)(2) (2013).

indebtedness" as taxable income.[121] While debt forgiven under public service forgiveness and cancellation is excluded from taxable income,[122] debt forgiven after 20 or 25 years of repayments is not.

### *C. Public interest repayment assistance and cancellation*

Students who work full time in qualified public-service jobs may be entitled to relief from some of their federal student loan debt. Currently, two federal programs may provide a measure of relief from FFEL and Direct Loan obligations: public-service cancellation and teacher-loan forgiveness. Borrowers in public service jobs may also benefit from one of many federal, state, and privately-funded Loan Repayment Assistance Programs (LRAPs).[123]

Public service cancellation is available to a borrower who is not in default and has made 120 monthly payments after October 1, 2007 on a federal Direct Loan while employed full-time in a public service job.[124] An eligible borrower is entitled to full discharge of her Direct loan. A borrower is employed "Full-time" if she works an average of 30 hours per week over the entire year or over the contractual or employment period, if that period is of at least eight months.[125] Public service jobs include employment with a government agency or a section 501(c)(3) nonprofit.[126] Excluded from

121. 26 U.S.C. § 61(a)(12) (1984).

122. 26 U.S.C. § 108(f)(1) (2013). Loan forgiveness and repayment assistance under most LRAPs, even if funded by a non-federal or non-governmental actor, is also likely to be excluded from taxable income. *See* Rev. Rul. 2008-34. Philip G. Schrag, *Failing Law Schools—Brian Tamanaha's Misguided Missile*, 26 GEO. J. LEGAL ETHICS 387, 415-16 (2013) (tax on loans forgiven).

123. *See Loan Repayment Assistance Programs*, EQUAL JUSTICE WORKS http://www.equaljusticeworks.org/ed-debt/students/loan-repayment-assistance-programs (last visited Feb. 13, 2014) [hereinafter *Loan Repayment Assistance Programs*].

124. *See* 20 U.S.C. § 1087e(m)(1) (2013), (2); 34 C.F.R. §§ 685.212(i) (2010), 685.219(c) (2012). The borrower must also be employed in a public service profession when she submits the application for forgiveness and when the debt is actually discharged. 20 U.S.C. § 1087e(m)(1)(B)(i) (2010); 34 C.F.R. § 685.219(c)(1)(ii) (2012).

125. 34 C.F.R. § 685.219(b)(i)(A), (B) (2013).

126. The more detailed but redundant list in the statute includes many jobs that are also covered under government or nonprofit headings. This list includes employees in emergency management; government; military service; public health, safety and education; law enforcement; social work in a public child or family service agency; public interest law services; early childhood education; public service for individuals with disabilities or the elderly; public or school-based library sciences; and other school-based services. 20 U.S.C. § 1087e(3)(B)(i) (2010). Also listed is employment as teaching faculty, either at a Tribal

coverage is work for businesses organized for a profit, labor unions, or partisan political organizations and work for religious organizations involving religious activity or instruction.[127] Because cancellation for public service is tax-exempt, it is not qualified by the "major drawback" of cancellation under income dependent repayment plans discussed above. FFEL loans are not eligible for cancellation, and payments made under such loans do not count toward the 120-month requirement even if the borrower subsequently consolidates her FFEL loans into a Direct Consolidation loan.

A borrower must apply to receive a public service discharge.[128] An application should be supported with evidence of public service employment during the relevant period.[129]

A separate provision allows limited forgiveness of FFEL and Direct loans for teachers in disadvantaged schools. A borrower, not in default, who has served as a full-time teacher at a qualifying school for five consecutive school years after October 1, 1998 is eligible for limited forgiveness of FFEL and Direct loans.[130] A borrower meeting teaching requirements[131] may receive up to $5,000 total in forgiveness for all Direct and FFEL loans combined. That limit is increased to $17,500 if the borrower is a highly qualified math or science teacher in a secondary school

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College or University or in "high-needs subject area or areas of shortage." 20 U.S.C. § 1087e(3)(B) (2010). Additionally, Department regulations include service for Peace Corps and AmeriCorps. 34 C.F.R. § 685.219(c)(ii) (2012). The authors thank Phil Schrag for the explanation: The Senate bill included the government plus the long list. The House bill included 501(c)(3)s. The conference committee listed all the eligible jobs in both bills, which created the redundancy in the statute.

127. 34 C.F.R. § 685.219(b)(B)(ii) (2012).

128. *See* 34 C.F.R. § 685.219(e) (2012) (stating that after making 120 qualifying payments on eligible loans, a borrower may request loan forgiveness).

129. 73 Fed. Reg. 37694, 37705 (July 1, 2008) (insisting that "it is the borrower's responsibility to gather and maintain the documents to support his or her eligibility for this Federal benefit").

130. 20 U.S.C. §§ 1087j(b) (Direct), 1078-10(b) (FFEL) (2009); 34 C.F.R. §§ 685.217(c) (Direct), 682.216(c) (FFEL) (2010). The standards for qualifying schools are the same as for Perkins discharge. 30 U.S.C. §§ 1087j(b)(1)(A), 1087j(c), 1078-10(b)(1)(A), 1078-10(c)(2) (2008); *see also* 20 U.S.C. § 1087ee(a)(2)(A) (2009) (qualifying school for Perkins discharge). In particular, the school must be qualified to receive funds under Title I of the Elementary and Secondary Education Act of 1965 *and* must be selected by the Secretary based on a determination that at least 30% of children enrolled at the school qualify for title I services. 34 C.F.R. §§ 685.217(c)(1) (Direct), 682.216(a)(2) (FFEL) (2008).

131. 34 C.F.R. § 685.217(c)(3)(i), (c)(4)(i) (2010); 34 C.F.R. § 682.216(c)(3)(i), (c)(4)(i) (2014).

or a highly qualified special education teacher in a primary or secondary school.[132] Interruptions in teaching for military service, FMLA leave, or "a return to postsecondary education, on at least a half-time basis" directly related to the borrower's teaching performance do not count as a break in the five-year period.[133]

A borrower seeking forgiveness must apply on an application form provided by the Secretary to the holder of the loan.[134] If the Secretary holds the loan, he determines the borrower's eligibility; otherwise, the guaranty agency decides.[135] No explicit statutory provision authorizes judicial review of guaranty agency decisions. But judicial procedures should be available to the borrower to contest the agency's decision.

Borrowers who do public interest work after graduation may also qualify for Loan Repayment Assistance Programs, or LRAP. These programs are particularly common at law schools. The sponsor of an LRAP provides funds to eligible students to cover a portion of their monthly student loan payments. LRAPs may be sponsored by schools, states, government and non-profit employers, and the federal government. Unique among the tools discussed in this section, LRAPs may be available to help a borrower repay private student loans. The availability and terms of LRAPs change every year. Some existing LRAPs expire or go unfunded, but new LRAPs are also being created. Borrowers seeking more information on LRAPs should consult the website of Equal Justice Works, which provides information and links for a range of LRAPs.[136]

The Georgetown University Law School has combined its Loan Assistance Repayment Program for public service with Grad PLUS loans and IBR.[137] A GU graduate may work in qualifying employment for ten years with the law school's assistance and secure forgiveness of her loan.[138]

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132. 34 C.F.R. § 685.217(c)(3)(ii), (c)(4)(ii) (2010); 34 C.F.R. § 682.216(c)(3)(ii), (c)(4)(ii) (2014).

133. 34 C.F.R. § 685.217(c)(7), (8) (2014); 34 C.F.R. § 682.216(c)(7), (8) (2010).

134. 34 C.F.R. §§ 685.217(e)(1), (8) (2014); 682.216(f)(1) (2010).

135. 34 C.F.R. §§ 685.217(e), 682.216(f) (2010).

136. *See Loan Repayment Assistance Programs*, *supra* note 123.

137. Philip G. Schrag & Charles W. Pruett, *Coordinating Law School Loan Repayment Assistance Programs with New Federal Legislation*, 60 J. LEGAL EDUC. 583, 599 (2011).

138. *Id. See also* Sarah Zearfiss, Joseph Pollak & Lorraine Lamey, *A Magic Mirror for Student Loans*, 3 Journal of Law (2 J. Legal Metrics) 237 (2013) (describing Michigan Law School's debt-management program, its DebtWizard site, the law school's extended repayment program covering graduates' IBR payments, deferment, and forbearance).

Although the conservative New America Foundation attacked GU's program as a "loophole" that is "offering free rides on the taxpayers' dime,"[139] GU is reducing burdensome student debt, improving its graduates' employment choices, and channeling legal talent into public service.[140]

*D. Repayment of Perkins loans*

Repayment of a Perkins loan must begin no more than nine months after the borrower ceases to be at least a half-time student. The standard repayment period for a Perkins loan is ten years.[141] A school may require that students make a minimum monthly payment, which is set at $40 for Perkins loans made after 1992.[142] Repayment of a Perkins loan may be extended for up to an additional ten years for a borrower who qualifies as a "low-income individual" as defined in statute and regulation.[143] Interest accrues during any extension.[144] A school may also institute incentive repayment programs to reward consecutive payments or early repayment.[145]

*1. Perkins loan deferments and forbearance*

Perkins loan deferment differs from FFEL and Direct loan deferment. Interest does not accrue during a Perkins deferment.[146] Additionally, a borrower in default may obtain a deferment upon entering into a written repayment agreement.[147] Deferment is available to students enrolled at eligible schools, in a graduate or post-graduate fellowship program, or in a

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139. Jason Delisle & Alex Holt, *How Elite Law Schools are Offering Free rides on the Taxpayers' Dime*, CHRON. HIGHER EDUC. (Aug. 13, 2013), http://chronicle.com/article/How-Elite-Law-Schools-Are/141103/. *See also* Luize Zubrow, *Is Loan Forgiveness Divine: Another View*, 59 GEO. WASH. L.REV. 451 (1991) (expressing skepticism about law-school's loan- forgiveness program).

140. William Treanor, *Georgetown Law's Loan Policy is Good for Society as Well as Students*, CHRON. HIGHER EDUC. (Aug. 20, 2013), http://chronicle.com/article/Georgetown-Laws-Loan-Policy/141215/.

141. 20 U.S.C. § 1087dd(c)(1)(A) (2010).

142. 20 U.S.C. § 1087dd(c)(1)(C) (2010); 34 C.F.R. § 674.33(b) (2010).

143. 20 U.S.C. § 1087dd(c)(3)(B) (2010); 34 C.F.R. § 674.33(c) (2010).

144. 34 C.F.R. § 674.33(c)(3) (2009).

145. 34 C.F.R. § 674.33(f)(1) (2009).

146. *See* 34 C.F.R. § 674.34 (b)–(e), (h), (i), (k) (2008).

147. 34 C.F.R. § 674.38(b) (2007).

rehabilitation program.[148] Deferment is also available if the borrower is seeking but unable to find full-time employment,[149] is undergoing economic hardship,[150] or is engaged in active duty military or National Guard service.[151] Finally, a borrower is entitled to deferment while working in Perkins cancellation-eligible occupations.[152]

A borrower applying for a Perkins deferment must apply to the school holding the loan.[153] Regulations do not provide for administrative review by the Department.

Perkins loan forbearance is available if the borrower's monthly student loan obligation exceeds 20% of her monthly gross income, the Secretary authorizes a period of forbearance due to a national emergency or military mobilization, or the school that made the loan "determines that the borrower should qualify for forbearance due to poor health or for other acceptable reasons."[154] A borrower seeking forbearance based on income levels must provide evidence of both debt burden and monthly income.[155] The school and the borrower must agree to the terms of the forbearance in writing.[156] Forbearances must be renewed after no more than twelve months, and Perkins loans may not be forborne for more than three years.[157]

### *2. Perkins Cancellation*

A borrower employed full-time in certain public service professions is eligible for accelerated cancellation of Perkins loans. The following borrowers may be eligible for Perkins discharge: certain teachers and

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148. 34 C.F.R. § 674.34 (b)(1) (2008). Deferment is not permitted under this provision for medical internship or residency programs. 34 C.F.R. § 674.34 (b)(2) (2008).

149. 34 C.F.R. § 674.34(d) (2008).

150. 34 C.F.R. § 674.34(e) (2008). A borrower qualifies for economic hardship deferment of Perkins Loans by showing that she has been granted an economic hardship deferment for a Direct or FFEL Loan, is receiving welfare, is a volunteer in the peace corps, or qualifies based on monthly gross income or monthly gross income less student loan payments. 34 C.F.R. § 674.34(e)(1)–(5) (2008).

151. 34 C.F.R. § 674.34(h) (2008). Military borrowers may also qualify for post-active duty service deferment under 34 C.F.R. § 674.34(i).

152. 34 C.F.R. § 674.34(c) (2008).

153. 34 C.F.R. § 674.38(a) (2007).

154. 20 U.S.C. § 1087dd(e)(1) (2009); 34 C.F.R. § 674.33(d)(5)(ii) (2009).

155. 34 C.F.R. § 674.33(d)(6) (2009).

156. 20 U.S.C. § 1087dd(e)(2) (2009); 34 C.F.R. § 674.33(d)(3) (2009).

157. 20 U.S.C. § 1087dd(e)(1) (2009); 34 C.F.R. § 674.33(d)(2) (2009).

education professionals; members of the Armed Forces serving in a combat zone; volunteers under the Peace Corps Act or Domestic Service Act; public-sector firefighters and law enforcement or corrections officers; attorneys in public defender organizations; nurses or medical technicians; and child or family service workers employed by public or private nonprofit agencies who provide services to high-risk children in low-income communities.[158]

A borrower in default may qualify, as long as her loan has not been accelerated.[159] With a few exceptions, a borrower who qualifies is entitled to discharge of 15% of the original principal loan amount in each of the first two years of service, 20% in each of the third and fourth years, and 30% in the fifth year.[160] The borrower is also entitled to discharge of interest accrued on the loan during the qualifying year.[161]

A borrower seeking a Perkins discharge must submit a request for cancellation along with any necessary documentation to the school that issued it by the deadline that the school establishes.[162] A Perkins loan in default may be discharged if it has not been accelerated. A loan in default that has also been accelerated may be discharged for services performed

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158. 20 U.S.C. §§ 1087ee(a)(2)(A) (2009) (teachers in qualified low-income schools or educational service agencies), 1087ee(a)(2)(B) (preschool teachers in Head Start or similar state-sponsored preschools), 1087ee(a)(2)(C) (special education teachers and providers of early intervention services), 1087ee(a)(2)(G) (teachers in math, science, foreign language, bilingual education, or other area of shortage as determined by state education officials), 1087ee(a)(2)(K) (faculty at Tribal College or University), 1087ee(a)(2)(L) (librarian with a master's degree in library sciences, employed either in a Title I school in a public library serving a geographic area that includes a Title I school), 1087ee(a)(2)(M) (speech pathologist with a master's degree employed in a Title I school). *See also* 34 C.F.R. §§ 674.53 (2007), 55 (1994) (regulations for teacher cancellation), 674.57 (2009) (law enforcement and corrections officer and public defender cancellation), 674.58 (2009) (early childhood education cancellation), 674.59 (2009) (military service cancellation), 674.60 (1999) (volunteer service cancellation), 674.56 (2009) (other qualifying employment cancellation). Applicable starting dates for qualifying service differ from program to program.

159. 34 C.F.R. § 674.52(c) (2007).

160. 20 U.S.C. § 1087ee(a)(3)(A)(i) (2009). The exceptions are as follows: volunteers are not entitled to the 30% discharge in the fifth year, *Id.*; § 1087ee(a)(3)(A)(iii), the discharge rate for special education teachers is fixed at 15% per year, *Id.*; § 1087ee(a)(3)(ii), and the discharge rate for service in a combat zone for a complete year ending before August 14, 2008 is fixed at 12.5% per year and capped at 50%. 34 C.F.R § 674.59 (2009).

161. 20 U.S.C. § 1087ee(a)(3)(B) (2009).

162. 34 C.F.R. § 674.52(a) (2007).

before the date of acceleration.[163] The school's decision is not subject to administrative review, but the Department will provide "guidance" to the school if the school so requests.[164] In *De La Mota v. United States Department of Education*, however, the Second Circuit Court of Appeals held that such informal guidance is entitled to no deference in an Article III court.[165]

The DOE does not review adverse school decisions. The *De La Mota* case involved APA review against the agency based on guidance it provided to the school;[166] the court did not address reviewability, standing, or remedies. The problem with APA review, of course, is that the school, not the agency, decides. The prudent course is to sue the Department and the school under different theories—the Department under the APA, either for incorrectly interpreting the statute or for unlawfully withholding cancellation, and the school for injunctive relief for violation of the Higher Education Act, which instructs that Perkins loans "shall be cancelled" if its conditions are met.[167]

## *III. Student Loans in Delinquency and Default*

Given the broad array of default-avoidance tools described in the last section, few, if any, borrowers should find themselves forced to default on their student loans. And the default labyrinth is well worth avoiding. One high-ranking Department official has described default as "an inconvenience for the government, but a tragedy for the borrower."[168] Nevertheless, an incredible number of borrowers default.[169]

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163. 34 C.F.R. § 674.52(c) (2007).

164. De La Mota v. U.S. Dep't of Educ., 412 F.3d 71, 81 (2d Cir. 2005).

165. *Id.*

166. *Id.* at 73.

167. 20 U.S.C. §§ 1087ee(a)(2) (2009).

168. Kelly Field, *Government Doesn't Profit From Student-Loan Defaults, Budget Analysis Shows*, CHRON. HIGHER EDUC. (Feb. 14 2011), http://chronicle.com/ article/Budget-Footnote-Government/126373/.

169. *First Official Three-Year Student Loan Default Rates Published*, U.S. DEP'T OF EDUC. (Sept. 28, 2012), http://www.ed.gov/news/press-releases/first-official-three-year-student-loan-default-rates-published (noting that of the 4.1 million borrowers who entered repayment from October 2009 to September 2010, almost 375,000 defaulted by September 30, 2011); *see also* Scott Cohn, *Surging Student-Loan Debt is Crushing the System*, CNBC.COM (Mar. 27, 2013), http://www.cnbc.com/id/100598257 (noting that 6.8 million federal student loan borrowers are currently in default).

The consequences of default are serious indeed: a borrower who defaults can expect to find herself with lower credit ratings and higher debt because of assessment of collection fees, costs, and penalties. This Part begins by discussing some of these consequences and describing how student loans fall into default in the first place.

Part of what makes federal student loan default particularly difficult for borrowers is the range of collection options available to creditors. The federal government has an arsenal of powerful administrative tools at its disposal to collect student loans, one of which, garnishment, is also available to guaranty agencies. Subpart B describes these administrative tools, as well as some others that may be available to different groups of lenders. Finally, Subpart C deals with issues that arise with student loans in litigation, including the extent of federal preemption in federal student loan collection litigation.

### *A. The Federal Student Loan Default Process and the Consequences of Default*

A borrower who misses a payment on a FFEL or Direct Loan is considered to be in delinquency.[170] Department regulations identify collection efforts FFEL lenders must undertake while a loan is in various stages of delinquency;[171] Direct loan servicers will likely engage in similar efforts. Lenders are required to attempt to contact the borrower multiple times both by phone and mail.[172] The content of the required notices varies, but generally it must inform the borrower of the possibility and consequences of default.[173] At least some of the notices must include information to the borrower about options for avoiding default, including deferment, forbearance, income-sensitive and income-based repayment, and loan consolidation.[174] Lenders must engage in collection activity at least once every forty-five days.[175]

A FFEL or Direct loan is considered to be in default if the borrower is in delinquency for 270 days if the loan is repayable in monthly installments.

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170. 34 C.F.R. § 682.411(b)(1) (2008).

171. 34 C.F.R. § 682.411 (2008).

172. 34 C.F.R.§ 682.411(c)–(f) (2008).

173. 34 C.F.R. § 682.411(d)(2), (e), (f) (2008).

174. 34 C.F.R. § 682.411(d)(1), (e) (2008).

175. 34 C.F.R. § 682.411(b)(2) (2008); *see also* 34 C.F.R.§ 682.411(j) (2008) (definition of collection activity).

Otherwise the loan is in default after 330 days.[176] At least thirty days before filing a default claim on the loan and on or after the 241st day of delinquency, a lender must send the borrower a final demand letter "requiring repayment of the loan in full and notifying the borrower that a default will be reported to a national credit bureau."[177] When the lender places a borrower in default, the lender assigns the claim to the guaranty agency that insured it.

Within forty-five days after being assigned a FFEL loan,[178] the guaranty agency must send the borrower a detailed notice informing her of the status of the loan, demanding that she immediately begin repayment, warning her of impending collection activities, and explaining her rights to challenge adverse guaranty agency decisions regarding the loan as well as her options for removing the loan from default.[179] Guaranty agencies must engage in "reasonable and documented collection activities," which must occur at least once every 180 days for a non-paying borrower.[180] Guaranty agencies must engage in the administrative collection efforts described later in this Part[181] and may also collect loans through litigation.[182]

For direct loans, the process is much simpler. Under the terms of current Direct loan servicing contracts, loan servicers must perform "collection and default aversion activity" for delinquent loans.[183] Once a loan reaches 360 days delinquency, the servicer must transfer the loan to the Department of Education's Debt Management Collection System.[184]

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176. 34 C.F.R. §§ 685.102(b) (1994), 682.200 (1992).

177. 34 C.F.R. § 682.411(f) (2008).

178. 34 C.F.R. § 682.410(b)(6)(ii) (1992).

179. 34 C.F.R. § 682.410(b)(5)(ii)(A), (b)(5)(vi); *see also* 34 C.F.R. 682.410(b)(6)(iv) (requiring a separate notice informing the borrower of options for removing a loan from default).

180. 34 C.F.R. § 682.410(b)(6)(i) (2010).

181. *See* 34 C.F.R. § 682.410(b)(6)(v), (vi) (a guaranty agency must attempt an annual Federal offset against eligible borrowers and must initiate administrative wage garnishment proceedings against eligible borrowers).

182. *See* 34 C.F.R. § 682.410(b)(6)(vii) (a guaranty agency may file a civil suit against a borrower to compel repayment only if the borrower has no wages that can be garnished).

183. *Direct Loan Servicing Contract with Pennsylvania Higher Education Assistance Agency*, U.S. DEP'T OF EDUC. Attachment A-1 at 15 (Jun. 17, 2009), *available at* http://www2.ed.gov/policy/gen/leg/foia/contract/pheaa-061709.pdf [hereinafter PHEAA Contract]; *see generally* U.S. DEP'T OF EDUC., *Loan Servicing Contracts*, FED. STUDENT AID, *available at* http://studentaid.ed.gov/about/data-center/business-info/contracts/loan-servicing (last visited Feb. 13, 2014).

184. PHEAA Contract, *supra* note 183.

There is no "delinquency" period for a Perkins loan, which is considered to be in default when a borrower fails "to make an installment payment when due or to comply with other terms of the promissory note or written repayment agreement."[185] However, schools must engage in "billing procedures" described in Perkins regulations, a series of overdue notices informing the borrower of the delinquency and warning her that the school will process her account for collection and litigation.[186]

If the borrower does not respond to the final demand letter, the school may initiate a series of "collection procedures," starting with reporting the account to a national credit bureau as in default.[187] In addition, a school may accelerate any defaulted loan with thirty days notice to the borrower[188] and may sue the borrower at any time.[189] A school may initially attempt to collect a defaulted loan on its own, but if it is unable to do so it must engage a collection firm or sue the borrower.[190] Schools may also be required to sue defaulting alumni borrowers if other collection methods have failed and litigation is both feasible and cost effective.[191]

The consequences of default for the borrower extend beyond those already described. A borrower in default may find it difficult to obtain other credit products like car loans or mortgages, or even a job or a lease on a home or apartment.[192] Defaults extend the loan repayment period, increasing interest costs for the borrower.[193] Default also makes borrowers ineligible for deferments and certain cancellation and forgiveness programs.[194] A student loan may also be accelerated upon default—the

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185. 34 C.F.R. § 674.2 (2008).

186. 34 C.F.R. § 674.43(b), (c) (2009). Schools may dispense with the initial notices and send a final demand letter 15 days after a missed payment if the borrower has an unsatisfactory repayment history or the school reasonably concludes that the borrower does not intend to repay or to seek deferment, postponement, or cancellation. 34 C.F.R. § 674.43(d). The school must also attempt at least one telephone contact before initiating collection procedures. 34 C.F.R. § 674.43(f).

187. 34 C.F.R. § 674.45(a)(1) (2008).

188. 34 C.F.R. § 674.43(e).

189. 34 C.F.R. § 674.46(a)(3) (2009).

190. 34 C.F.R. § 674.45(c)(1)(ii) (2008).

191. 34 C.F.R. § 674.46(a)(1), (2).

192. *See* Field, *supra* note 168 (noting how defaulting on student loans damage borrowers' credit records).

193. *See id.* (stating that individuals who default on loans have to pay higher interest rates).

194. *See, e.g.*, *supra* notes 53 (deferment), 101 (income-based repayment), 125 (public

entire amount of the loan becomes due immediately.[195] One of the most serious consequences of default and delinquency for the borrower is that lenders may assess collection costs, fees, or penalties that the borrower must pay in addition to any principal and interest. Default also renders a borrower ineligible to receive further federal assistance funds from any Title IV program, not just student loan programs.[196]

### *B. Borrower liability for collection fees and penalties*

Creditors and collection agencies may attempt to charge collection costs, fees, and penalties to the borrower. Any such attempt must be consistent both with the contract that created the loan and with any applicable statutes. Different statutes regarding collection costs apply depending on the type of loan and who is collecting it. For private student loan collection, this means generally applicable state or federal consumer protection laws and any state or federal consumer protection laws aimed at private student lenders. For federal loans, particular federal statutes and regulations apply, depending on who is collecting the loan.

The Department or a guaranty agency may assess "reasonable collection costs" against a borrower who defaults on a FFEL loan.[197] For collection efforts by the Department and guaranty agencies, reasonable collection costs means actual costs incurred in collection.[198] When a Private Collection Agency ("PCA") collects a loan for the Department or a guaranty agency, the costs charged are based on a formula set by a regulation that is designed to estimate the average cost of PCA student loan collection.[199] In 2009, a Department publication indicated an applicable

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service cancellation).

195. 34 C.F.R. §§ 685.211(d)(1) (2013) (Direct); 674.31(b)(8) (2009) (Perkins).

196. 34 C.F.R. § 668.32(g)(1) (2011). Students may become eligible for Title IV assistance again by either repaying the debt in full or making six consecutive months of payments under a repayment agreement entered into with the holder of the loan in accordance with Title IV regulations. 34 C.F.R. § 668.35(a) (2008).

197. 20 U.S.C. § 1091a(b)(1) (2008); *see also* 34 C.F.R. § 30.60 (1988) (listing types of costs chargeable to debtors); 34 C.F.R. § 682.410(b)(2) (2013) (limiting collection costs that may be charged by guaranty agencies).

198. 34 C.F.R. § 30.60(a). "Actual costs" means what it says: the government is not permitted to assess costs that it doesn't actually incur, such as filing fees in federal court. United States v. Spann, 797 F. Supp. 980 (1992).

199. 34 C.F.R. § 30.60(c), (d). The rate is calculated annually. *Id.* § 30.60(d).

rate of 24.34%.[200] Collection costs are calculated based only on principal and interest, and not fees.[201] Payments to guaranty agencies are applied first to the agency's costs in collecting that amount, then to "other incidental charges" like late fees, and finally to accrued interest and principal.[202]

There are limits on imposition and collection of costs and fees. First, the Department of Treasury deducts fees from tax-refund offsets to cover its own administrative costs in running the offset programs, but PCAs do not receive a commission from these offsets.[203] Second, the Department of Education may not impose fees inconsistent with the promissory note or its own student loan regulations, even if a statute generally applicable to the federal government permits those fees.

FFEL Lenders may also tack collection costs onto a borrower's debt if the promissory note provides for imposition of collection costs.[204] These costs may not include "routine collection costs associated with preparing letters or notices or making personal contacts with the borrower."[205] FFEL lenders may also assess late charges on borrowers of up to six cents for each dollar of late installments, if the charge is authorized by the promissory note.[206]

For Perkins Loans, each school is required to assess against borrowers "all reasonable costs incurred by the school with regard to a loan obligation."[207] This must be based on either actual costs for the borrower's loan or average costs "for similar actions taken to collect loans in similar stages of delinquency."[208] Collections are capped at 30% of principal, interest, and late charges collected for first collection efforts and 40% of principal, interest, and late charges for subsequent collection efforts,

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200. U.S. DEP'T OF EDUC., *PCA Procedures Manual: 2009 ED Collections Contract*, FED. STUDENT AID 21 (2009), *available at* http://epic.org/foia/ed/EPIC-ED-2009-PCA-Manual.pdf [hereinafter *PCA Procedures Manual*].

201. *Id.* at 23.

202. 34 C.F.R. § 682.404(f) (2008).

203. *PCA Procedures Manual*, *supra* note 200.

204. *See* 34 C.F.R. § 682.202(g)(1) (2010) (stating a lender may require that the borrower pay costs incurred by the lender or its agents in collecting installments not paid when due if provided for in the borrowers promissory note).

205. *See* 34 C.F.R. § 682.202(g)(2) (referencing costs referred to in paragraph (g)(1)).

206. *See* 34 C.F.R. § 682.202(f).

207. 34 C.F.R. § 674.45(e)(1) (2008).

208. 34 C.F.R. § 674.45(e)(2).

including litigation.[209] Court costs may also be charged and do not count toward the 40% cap.[210] Under certain circumstances, a school may waive some or all collection costs according to the terms of a repayment agreement with the borrower.[211]

### *C. Administrative Collection Procedures*

A borrower who defaults on federal student loans faces an array of non-judicial collection procedures that ordinary private debtors do not. The Department of Education uses three tools. Each diverts money from a different stream originally designated to flow to the borrower and applies that money to satisfy the debt. This section will deal first with garnishment, in which the lender serves an order to the borrower's employer to redirect some of the borrower's wages to the lender. Administrative garnishment is unique in that it is available to guaranty agencies as well as the government. Another administrative collection method is the tax refund offset. Finally, the federal government can redirect benefits due to the borrower under certain federal statutes toward the payment of a defaulted student loan. The remainder of this section takes up administrative collection procedures available on the state level, in particular, state tax refund offsets and professional license suspension.

Except where otherwise stated, these procedures are not available when the borrower has defaulted on a private student loan.

#### *1. Administrative Wage Garnishment*

Two federal statutes—the Higher Education Act of 1965 (HEA) and the Debt Collection Improvement Act of 1996 (DCIA)—provide the Department of Education with authority to garnish wages of a borrower in default on federal student loans.[212] Department regulations provide for garnishment only pursuant to the DCIA.[213] Guaranty agencies may garnish wages, but only under the Higher Education Act.[214] Thus, different bodies

209. 34 C.F.R. § 674.45(e)(3).

210. 34 C.F.R. § 674.45(e)(3)(iii).

211. *See* 34 C.F.R. § 674.47(d) (2009).

212. 20 U.S.C. § 1095a (2006); 31 U.S.C. § 3720D (1996).

213. *See* 34 C.F.R. §§ 34.1–34.30 (2003) (citing as statutory authority the DCIA, and not the HEA).

214. 20 U.S.C. § 1095a(a).

of law govern garnishment of federal student loans, depending on whether the Department or a guaranty agency seeks garnishment.

Many provisions of the DCIA and the HEA are identical. Both statutes cap garnishment at 15% of the borrower's disposable pay.[215] Both statutes require written notice to the borrower thirty days before the start of garnishment[216] as well as an opportunity for a hearing, at which she may contest the existence, amount, or enforceability of the debt or the terms of any applicable repayment schedule.[217] And both statutes require that the would-be garnishor provide the borrower an opportunity to agree to a written repayment agreement "under terms agreeable to" the lender in order to avoid garnishment.[218] Borrowers may request a hearing to contest administrative garnishment at any time.[219] However, garnishment will not be postponed pending the hearing unless the borrower's request is timely.[220]

If a borrower is involuntarily separated from employment and subsequently reemployed within twelve months, her pay may not be administratively garnished until she has been reemployed continuously for twelve months.[221] A borrower may also object to the amount garnished by

215. 20 U.S.C. § 1095a(a)(1); *see also* 31 U.S.C. § 3720D(b)(1).

216. *See* 20 U.S.C. § 1095a(a)(2); 31 U.S.C. § 3720D(b)(2) (requiring notice giving the amount to be collected and the debtor's rights); *see also* Administrative Wage Garnishment, 34 C.F.R. §§ 34.4, 34.5 (2003) (mandating notice and its required components such as the amount outstanding); *see also* Fiscal, Administrative and Enforcement Requirements, 682.410(b)(9)(i)(B) (2010) (requiring notice by mail to the last known address).

217. 20 U.S.C. § 1095a(a)(5), 31 U.S.C. § 3720D(b)(5) (requiring a hearing if the garnishment is timely objected within fifteen days); *see also* 34 C.F.R. §§ 34.6(c)(1)–(2) (2003), 682.410(b)(9)(i)(E), (J) (2010) (allowing the debtor a hearing to contest the repayment schedule).

218. 20 U.S.C. § 1095a(a)(4) (2006); 31 U.S.C. § 3720D(b)(4) (1996); *see also* 34 C.F.R. §§ 34.6(b), 682.410(b)(9)(i)(D) (summarizing that borrowers who agree to a repayment schedule but fail to make payments are subject to immediate garnishment, though they may request a hearing to raise hardship claims); *see also PCA Procedures Manual*, *supra* note 200, at 50, 53.

219. *See* 34 C.F.R. §§ 34.11(c) (2003), 682.410(b)(9)(i)(L) (stating that a hearing must be provided even if the request is not timely).

220. *See* 34 C.F.R. §§ 34.11 (a), (b), 682.410(b)(9)(i)(K) (explaining that a request for a hearing to contest DCIA garnishment is timely if made within 30 days of notice); *see also* 34 C.F.R. § 682.410(b)(9)(i)(K) (detailing that a request for a hearing to contest HEA garnishment is timely if made within 15 days of notice); *see also* 34 C.F.R. §§ 34.11(c)(2), 682.410(b)(9)(i)(L) (describing that the Department or guaranty agency may also postpone garnishment despite an untimely request for a hearing if good cause exists to do so).

221. *See* 20 U.S.C. §1095a(a)(7); 31 U.S.C. § 3720D(b)(6); *see also* 34 C.F.R. §§ 34.6(c)(3), 682.410(b)(9)(i)(G) (detailing that DOE regulations prohibit a guaranty agency from garnishing such a borrower only when the guaranty agency knows that the

arguing that withholding that amount from pay would impose an undue hardship on her or her dependents.[222]

In DCIA garnishment hearings, the burden of proof in establishing defenses or objections rests with the borrower.[223] Department regulations are silent about the burden of proof in HEA garnishment proceedings brought by guaranty agencies.

The Department provides borrowers with a list of objections it will consider in DCIA garnishment proceedings on its Request-for-Hearing form.[224] That form lists the following objections in addition to those already discussed: the delinquent amount of the debt has been repaid in whole or in part, the debt is being paid under the terms of a repayment agreement, the debtor is in bankruptcy, the debt was discharged in bankruptcy, the debt is not the debtor's, the debtor is entitled to statutory discharge of the debt, or the debt is not enforceable under state contract law. All but one of these objections must apply to HEA garnishment, because they raise a dispute as to the existence or amount of the debt or whether the debt is enforceable by garnishment or even enforceable at all. The one exception is entitlement to statutory discharge; however, an informal department manual indicates that a guaranty agency may not garnish if it finds grounds for statutory discharge.[225]

The principal difference between DCIA garnishments by the Department of Education and HEA garnishments by guaranty agencies is in the hearing process itself.

To request a hearing to contest DCIA garnishment, a borrower should use the "Request for Hearing" form provided by the department.[226] The borrower may request an oral hearing, but an oral hearing will be provided only if the borrower can show that "the validity of the claim turns on the credibility or veracity of witness testimony," such that documentary

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borrower is unemployed or has not continuously been employed for 12 months).

222. *See* 34 C.F.R. §§ 34.7(a), 34.14(c), 34.24 (2003) (requiring documentation to show undue hardship after garnishment).

223. *See* 34 C.F.R. §§ 34.14, 34.24(d)(1) ("You bear the burden of proving a claim of financial hardship by a preponderance of the credible evidence.").

224. *See* U.S. DEP'T OF EDUC., *Request For Hearing*, FED. STUDENT AID, https://www.myeddebt.com/borrower/PDFFrames.jsp?fileName=form.AWG.Request.For.Hearing.pdf&pre_fill=Y (2011) [hereinafter *Request*].

225. *See* NAT'L CONSUMER LAW CTR., STUDENT LOAN LAW § 8.3.3.2 (4th ed. 2010 & 2012 supp.) (citing U.S. DEP'T OF EDUC., ADMIN. WAGE GARNISHMENT HANDBOOK (2004)).

226. *See Request*, *supra* note 224.

evidence alone is not adequate to resolve disputed issues.[227] If a borrower is allowed an oral hearing, she may choose whether to have the hearing in-person or over the telephone.[228]

"[A]ny qualified employee" of the Department may conduct a DCIA garnishment hearing.[229] Department regulations characterize these hearings as "informal proceedings," though witnesses are required to testify under oath or affirmation.[230] The hearing official must maintain a summary record of the hearing[231] and, within sixty days, issue a written decision based on the evidence and including the official's "findings, analysis, and conclusions regarding objections raised to the existence or amount of the debt."[232] Reconsideration is available only if the borrower either offers new evidence supporting a previously-made and rejected objection or claims that the garnishment order imposes an undue hardship on her because of a material change in her financial circumstances after the contested garnishment order was issued.[233] Judicial review of garnishment decisions is available under the Administrative Procedure Act.[234]

In an HEA garnishment hearing, a guaranty agency may choose "any qualified individual, including an administrative law judge" to conduct the hearing, as long as that person is "not under the supervision or control of the head of the guaranty agency."[235] The borrower may choose between an oral or written hearing, and may appear by telephone at an oral hearing.[236] The guaranty agency must hold the hearing and render its decision in writing within sixty days of the borrower's request for a hearing.[237]

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227. 34 C.F.R. § 34.9(a)(2) (2003).

228. *See* 34 C.F.R. § 34.9(c)(1), (4) (describing that the borrower bears her own travel costs for an in-person hearing); *see also* § 34.9(c)(5) (stating that the agency bears the costs of telephone calls it places for a telephone hearing).

229. 34 C.F.R. § 34.13(a)(2) (2003).

230. 34 C.F.R. § 34.13(b)(1), (2).

231. *See* 34 C.F.R. § 34.13(b)(3).

232. 34 C.F.R. §§ 34.16(a), 34.17(a).

233. *See* 34 C.F.R. § 34.12(b)–(c) (2003) (stating additionally that filing for reconsideration does not halt the collection process).

234. *See* 34 C.F.R. § 34.17(b) (2003) ("The hearing official's decision is the final action of the Secretary for the purposes of judicial review under the Administrative Procedure Act" (citing 5 U.S.C. §§ 701–06)).

235. 34 C.F.R. § 682.410(b)(9)(i)(M) (2010).

236. *See* 34 C.F.R. § 682.410(b)(9)(i)(J) (stating that if the borrower opts for a hearing by telephone, the guaranty agency is responsible for telephonic charges).

237. *See* 34 C.F.R. § 682.410(b)(9)(i)(L)–(N) ("The hearing official shall issue a final

The availability and scope of judicial review of guaranty agency decisions is unclear. APA review is not available against guaranty agencies, and neither the HEA nor DOE regulations governing HEA garnishment provide for judicial review of guaranty agency's decisions.[238] If the guaranty agency is an agency of state government, judicial review of the agency's garnishment decisions may be available in state court under the state-law analogue to Administrative Procedure Act. Furthermore, if the guaranty agency is a state actor, the guaranty agency official responsible for issuing the garnishment order may be sued under section 1983[239] or *Ex Parte Young*.[240]

Procedural due process arguments have found some purchase in the courts, and for good reason.[241] Deciding a collections issue through administrative procedure otherwise available only to the government and sending a legally binding notice to an employer looks a lot like state action. And administrative adjudication without judicial review raises serious due process questions. In any event, if the garnishment was unauthorized by federal law, state law may provide a monetary remedy to recover wages improperly garnished.

### *2. Federal Employee Salary Offsets*

When a current or former federal employee has defaulted on federal student loans, the government in effect becomes both garnishor and garnishee. Rather than garnishing itself, the government simply offsets the employee's salary or retirement pay, by an amount up to 15% of disposable pay.[242] The employee is entitled to thirty days' notice and opportunity for a

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written decision at the earliest practicable date, but not later than sixty days after the guaranty agency's receipt of the borrower's hearing request.").

238. *See* Brief for Nat'l Ass'n of Consumer Bankr. at 14, Attorneys as Amicus Curiae Supporting Respondent, Tenn. Student Assistance Corp. v. Hood, 541 U.S. 440 (2004) ("However, unlike federal agency hearings or proceedings before the bankruptcy court, borrowers have no explicit right to judicial review of guaranty agency decisions.").

239. *See* 42 U.S.C. § 1983 (1996) (creating a cause of action to redress deprivation of federal rights by state actors).

240. *Ex parte* Young, 209 U.S. 123 (1908) (holding that state officials who violate federal law may be sued in federal court to enjoin further violation).

241. *See, e.g.*, Hutchins v. United States, CIV-F-02-6256, Memorandum Opinion and Order Re: Defendants' Motion to Dismiss Under Rule 12(b)(1) and Rule 12(b)(6) or, in the alternative, for Summary Judgment under Rule 56 and Request for Judicial Notice (E.D. Cal., Apr. 16, 2004).

242. *See* 5 U.S.C. § 5514(a)(1) (2008) ("The amount deducted for any period may not

hearing where she may contest the existence or amount of the debt or its enforceability by offset, or establish a defense of "extreme financial hardship."[243] The employee may also avoid offset by entering a repayment agreement with the Department.[244]

### *3. Federal Income Tax Refund Offsets*

The Department of Treasury will offset a tax refund to pay a borrower's "past-due, legally enforceable" debts owed to either the Department of Education or a guaranty agency.[245] Before offset may occur, the Department must mail written notice to the debtor of the nature and amount of the debt, the Department's intent to collect by offset, the debtor's procedural rights should she decide to contest the offset, and her opportunity to avoid offset by entering a repayment agreement with the Department.[246] A borrower who wishes to inspect and copy records must so request within twenty days after the date of notice.[247] If the borrower wishes to contest the existence or amount of the debt, she must request review before sixty-five days following the date of notice or, if she timely requested to inspect records, fifteen days after the Department has made the records available for inspection, whichever is later.[248] The borrower must include with this filing any documents that she would like the Secretary to consider at the hearing, and her request for an oral hearing, should she desire one.[249] The Secretary will grant an oral hearing only if the disputed

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exceed 15 percent of disposable pay, except that a greater percentage may be deducted upon the written consent of the individual involved.").

243. 5 U.S.C. § 5514(a)(2); 34 C.F.R. § 31.8 (1988).

244. *See* 5 U.S.C. § 5514(a)(2)(C); 34 C.F.R. § 31.10 (1988) (detailing the procedural requirements for avoiding an offset).

245. 31 U.S.C. § 3720A(a), (c) (1996) (requiring offset when debt is owed to a federal agency or a third party administrating a debt as an agent for the government). These procedures are not available to schools holding Perkins loans that are in default; however, offset is available to the government should the school assign the loan to it.

246. *See* 31 U.S.C. § 3720A(b); 34 C.F.R. §§ 30.22, 30.33 (1988) (listing the elements the notice to the debtor must contain).

247. *See* 34 C.F.R. § 30.33(c) (1988); *see also* 34 C.F.R. § 30.23 (1988) (stating that the debtor must specify which documents they wish to copy).

248. *See* 34 C.F.R. § 30.33(d), (f) (requiring that a debtor who wishes to enter a repayment agreement with the Secretary must enter such an agreement and make the first payment under the agreement by the same deadline).

249. 34 C.F.R. §§ 30.25(a), 30.33(e) (2014); *see also* 34 C.F.R. § 30.24 (explaining the procedures a debtor must follow in order to obtain a review of the existence or amount of

issues cannot be resolved by documentary evidence.[250] If the debt is owed to a guaranty agency, the Secretary may provide for initial review by the guaranty agency. A borrower dissatisfied with the guaranty agency's decision may then seek review with the Secretary within seven days of the guaranty agency's determination.[251] Following any review, the Secretary must provide the borrower with a decision in writing.[252] Judicial review is available under the Administrative Procedure Act.[253]

Defenses to tax-refund offset largely mirror those for other administrative collection procedures. In particular, eligibility for a school-related discharge is a defense to tax refund offset.[254] Hardship is not among listed defenses, and while the agency may consider it at its discretion, borrowers' hardship arguments almost never succeed.[255]

With one exception, taxpayers seeking to recover tax refunds that have already been offset to pay student loan debts must take their grievances up with the Department of Education, not the Treasury Department.[256] The exception is that an innocent spouse must pursue a wrongfully withheld refund based on a jointly-filed return with the IRS.[257]

### *4. Offsets to Federal Benefits*

If a borrower receives benefits from one federal agency but owes debts to another, the creditor agency may in certain circumstances demand a cut

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debt). A borrower who wants an oral hearing must provide reasons why review of documentary evidence is insufficient as well as a list of witnesses the debtor plans to call and what those witnesses will testify to. 34 C.F.R. § 30.25(b).

250. 34 C.F.R. § 30.25(c)(2); *see also* 34 C.F.R. § 30.26 (detailing procedures for an oral hearing).

251. 34 C.F.R. § 30.33(d)(3).

252. 34 C.F.R. §§ 30.24(e)(2), 30.26(c)(4).

253. 5 U.S.C. § 701–06 (2011).

254. *See* NAT'L CONSUMER LAW CTR., *supra* note 225, at § 8.2.4 (discussing a borrower's ability to raise school-related defenses).

255. *See id.* at § 5.2.2.3 (listing the permissible defenses).

256. *See* 26 U.S.C. § 6402(g) (2014) (noting that United States courts do not have jurisdiction over these matters and that they should be brought to the Federal agency to which the reduction was paid); 31 C.F.R. § 285.2(i) (detailing who has power to review tax refund offsets).

257. *See* Burgess v. U.S. Dep't of Educ., No. 105-CV-98, 2006 WL 1047064, at *5 (D. Vt. Apr. 17, 2006) (noting that an injured spouse can pursue an administrative remedy through the Internal Revenue Service).

of the debtor's benefits from the first agency.[258] Like the tax refund offsets, benefits offsets are administered by the Treasury Department based on claims referred by claimant agencies.

Offset is limited to the lesser of (1) the amount of the debt, including interest, penalties, and administrative costs, (2) 15% of the monthly benefit, and (3) the amount by which the monthly benefits exceed $750.[259] But some federal benefits payments are exempted from offset entirely. Federal statutes exempt veterans' benefits,[260] Tier 2 Railroad Retirement benefits,[261] and payments under federal worker compensation programs, including most Black Lung benefits.[262] As for Social Security benefits, Disability Insurance Benefits are subject to offset, but Supplemental Security Income benefits are not.[263] Payments under student financial aid programs are also exempt,[264] but that means little for a student-loan debtor since the Department of Education can garnish these payments on its own.[265] The Secretary of the Treasury has authority to exempt payments under other programs from offset, and he has done so for a wide array of programs.[266] Even if the borrower's benefit is not exempt from offset, she may request an offset for hardship.[267]

Before the Department of Education requests the offset, it must send the borrower notice of its intent as well as provide her an opportunity to review the evidence.[268] The procedures for review are the same as for tax

258. 31 U.S.C. § 3716 (2013).

259. 31 C.F.R. § 285.4(e) (2014).

260. 38 U.S.C. § 5301(a) (2013).

261. 45 U.S.C. § 231m (2013).

262. 30 U.S.C. § 932(a) (2013); *see also* Federal Employees Compensation Act, 5 U.S.C. § 8130 (2013); Longshore and Harbor Workers' Compensation Act, 33 U.S.C. § 916 (2013); Energy Employees Occupational Illness Compensation Program Act, 42 U.S.C. § 7385a (2013). Benefits under Part B of the Black Lung Benefits Act—which applies only to claims made prior to 1974, *see* 30 U.S.C. § 924—are subject to offset. 31 U.S.C. § 3716(c)(3)(A)(ii).

263. 31 U.S.C. § 3716(c)(3)(A); 31 C.F.R. § 285.4(a)(1).

264. 31 U.S.C. § 3716(c)(1)(C). Private parties are also prohibited from seizing or garnishing federal student aid payments, including student loan disbursements. 20 U.S.C. § 1095a(d) (2013).

265. 20 U.S.C. § 1095a(d).

266. 31 U.S.C. § 3716(c)(3)(B). A list of exempt payments can be found on the Treasury Department's website at http://www.fms.treas.gov/debt/dmexmpt.pdf.

267. *See* NAT'L CONSUMER LAW CTR., *supra* note 214, at § 8.4.3.2 (discussing a student debtor's options in requesting an offset).

268. 34 C.F.R. §§ 30.22, 30.24 (2014).

offsets,[269] with the following exceptions. The deadline to reach a repayment agreement with the Secretary or to request review is twenty days after receiving notice, regardless of whether the borrower requested to review records.[270] Documents supporting the borrower's position must be filed by the same deadline, unless she has requested to review the records, in which case she must file any documents fifteen days after the Secretary makes the records available.[271]

### *5. Virginia Statutory Setoff*

The Virginia Setoff Debt Collection Act provides a statutory "setoff" mechanism that allows claimant agencies—arms of state, county, city or town governments, state courts, and the Internal Revenue Service[272]—to collect debts from delinquent debtors from state tax refunds or lottery winnings due to the debtor.[273] A state college or university must use this setoff procedure to collect defaulted student loans, unless it determines that the administrative cost of the procedure exceeds the amount of the delinquent debt.[274] In the student loan context, statutory setoff may affect students or former students who have outstanding Perkins loans, fees, or other debts owed to state educational institutions.

The procedure for setoff works as follows: A school holding a loan on which the borrower is delinquent notifies the Department of Taxation of the borrower's delinquency. The Department of Taxation then determines whether the borrower is owed a tax refund and, if so, notifies the school of the amount of the refund and the address the borrower provided on her tax return.[275] The school must, within ten days, mail written notification to the

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269. The regulations for benefits offsets generally are provided in 34 C.F.R. §§ 30.20–30.28. Those provisions also apply to tax refund offsets "as modified by" 34 C.F.R. § 30.33.

270. 34 C.F.R. § 30.24(a).

271. 34 C.F.R. § 30.24(d).

272. VA. CODE ANN. § 58.1-520 (2013).

273. VA. CODE ANN. §§ 58.1-523 (tax refunds), 58.1-535 (lottery winnings). If the claimant agency—the school in the case of student loans—itself holds funds due to the debtor, they may set off the delinquent debt from those funds before transferring them to the debtor. VA. CODE ANN. § 58.1-535; *see also* Virginia Polytechnic Inst. v. Interactive Return Serv., Inc., 626 S.E.2d 436, 438–40 (Va. 2006) (explaining the application of the Virginia Code). Despite its name, the statutory setoff provision functions as garnishment rather than offset except where the Commonwealth itself is the creditor.

274. VA. CODE ANN. §§ 58.1-521(B), 58.1-522.

275. VA. CODE ANN. § 58.1-524.

borrower of its intention to offset the refund. This notification must also state the basis for the school's claim and inform the borrower of her right to contest the claim and the procedures for contesting it.[276] The borrower has thirty days in which to request a hearing, at which she may dispute the validity and amount of the claim.[277] No setoff may be made during the pendency of the hearing.[278] If the borrower does not request a hearing within the statutory period, any objections to setoff are waived.[279] No individual "involved in the prior circumstances which have culminated in [the] dispute" may hear the debtor's claim.[280] A borrower may seek judicial review of an adverse decision by the school in circuit court within thirty days after that decision becomes final.[281]

The Setoff Debt Collection Act also establishes a priority system for resolving competing claims.[282] Claims by state educational institutions take priority over claims by counties, cities, towns, and the IRS. Among claims of courts or administrative units of state government, such as public colleges and universities, priority is determined by the order in which the claimant agency files notice of its intent to seek setoff with the Department of Taxation.

*6. Professional License Suspension for Virginia Health Care Professionals*

Virginia law allows a creditor of a federal- or state-insured educational loan to, upon thirty days' notice, petition the circuit court in the jurisdiction where the defaulting borrower resides "for an order suspending any license, certificate, registration, or other authorization to engage in a business, trade, profession, or occupation issued to the borrower by any health regulatory board within the Department of Health Profession."[283] The conditions for suspension are relatively stringent. In order to suspend a borrower's license, the court must find that she actually has a license issued by a regulatory authority within the Department of Health Professions, and that she is delinquent in the payment of a loan guaranteed by either the federal

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276. VA. CODE ANN. § 58.1-525.
277. VA. CODE ANN. §§ 58.1-525(B), 58.1-526(A).
278. VA. CODE ANN. § 58.1-526(B) (2013).
279. VA. CODE ANN. § 58.1-525(B).
280. VA. CODE ANN. § 58.1-526(C).
281. VA. CODE ANN. § 58.1-527(A).
282. VA. CODE ANN. § 58.1-530.
283. VA. CODE. ANN. § 54.1-2400.5(A), (B).

government or a state government.[284] The court may not suspend the license if it finds that the creditor has recourse to an alternative remedy "that is likely to result in collection of the delinquency."[285] The court "may refuse to order the suspension" if suspending the borrower's license would result in irreparable harm to her or to her employees or would not result in collection of the delinquency, or she "has made a good faith effort to reach an agreement with the" creditor.[286] If the court finds against the borrower, she must surrender her license within ninety days.[287] A borrower is entitled to have her license reinstated if she pays the delinquency or reaches an agreement with the creditor to pay the delinquency and makes at least one payment pursuant to that agreement.[288]

Initiating a professional license suspension proceeding is an extreme step for a lender. License revocation or suspension may shut off a health care professional's principal source of income, and likely with it her ability to pay her debts. The only conceivable reason a creditor might invoke this provision is to coerce payment from debtors who are able yet unwilling to pay their loans. Nevertheless, lenders in other states have used similar provisions to target debtors who have defaulted on federally-backed student loans.[289]

The borrower's labyrinth, formidable up to this point, becomes even more difficult to escape once she enters court.

### *D. Judicial Collection Procedures*

All educational creditors are entitled to invoke the generally available procedures for collecting unpaid debts. Unsurprisingly, the United States prefers to utilize the array of administrative collection procedures the government has at its disposal over filing suit.[290] Yet, it brings thousands of

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284. VA. CODE. ANN.§ 54.1-2400.5(D) (2013).

285. VA. CODE. ANN.§ 54.1-2400.5(C).

286. *Id.*

287. VA. CODE. ANN. § 54.1-2400.5(D)

288. VA. CODE. ANN. § 54.1-2400.5(E).

289. *See* Emily Bregel, *Loan Defaults Sting Tennessee Nurses*, CHATTANOOGA TIMES FREE PRESS (Jan. 18, 2011), *available at* http://www.timesfreepress.com/news/2011/jan/18/loan-defaults-sting-nurses/?local (explaining that "[d]ozens of Tennessee nurses have had their licenses suspended for ignoring student loans").

290. *See* U.S. DEP'T OF TREASURY, *U.S. Government Receivables and Debt Collection Activities of Federal Agencies: Fiscal Year 2009 Report to the Congress* 14 (2010), *available at* http://fmsq.treas.gov/news/reports/debt09.pdf (indicating that just one percent of

student loan collection cases in federal court each year. Between 2008 and 2012, the government brought around 15,000 actions in federal court to collect on defaulted student loans.[291]

The government's student loan debt collection activity is concentrated in a small number of judicial districts; the top nine districts for student loan cases accounted for more than 86% of filings in 2012.[292] Most of these lawsuits are brought in the government's name by private law firms, pursuant to a statute that allows the justice department to contract collection services to such firms.[293] The uneven distribution of cases is due to the fact that this program has not been implemented in every judicial district.[294]

Private parties may bring collection litigation in their own names. The federal government may assign defaulted student loans to Private Collection Agencies (PCAs),[295] which may sue the borrower in state or federal court. Guaranty agencies and schools holding defaulted Perkins

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federal student loan collections in FY 2009 were made directly through litigation).

291. ADMIN. OFFICE OF U.S. COURTS, *Table C-2A: U.S. District Courts—Civil Cases Commenced, by Nature of Suit, During the 12-Month Periods Ending September 30, 2008 Through 2012* (2012), *available at* http://www.uscourts.gov/uscourts/Statistics/JudicialBusiness/2012/appendices/C02ASep12.pdf. Table C-2A indicates that 15,045 actions were commenced in federal district court with a nature of suit flag indicating "Recovery of Defaulted Student Loans." *Id.* However, a small number of these cases were filed by private parties against the government. ADMIN. OFFICE OF U.S. COURTS, *Table C-9: U.S. District Courts—Recovery of Overpayment and Enforcement of Judgment Cases Filed During the 12-Month Period Ending September 30, 2012* (2012), *available at* http://www.uscourts.gov/uscourts/Statistics/JudicialBusiness/2012/appendices/C09Sep12.pdf.

292. *Id.*

293. *See* 31 U.S.C. § 3718 (2011) (explaining that "[u]nder [certain] conditions . . . a contract [may be formed] with a person for collection service[s] to recover indebtedness owed . . . [to] the United States Government"); *see also* David Jesse, *Beware, Metro Detroit: The Feds are Out -- And Looking for Payback on Late Student Loans*, DETROIT FREE PRESS (Jan. 28, 2013), *available at* http://www.freep.com/article/20121007/NEWS06/101280006/ (describing the private counsel program's history). Private attorneys pursuing debt collection pursuant to a contract with the government are subject to the provisions of the federal debt collection practices act. *Id.* § 3718(b)(6). But the federal government and its own employees are not, 15 U.S.C. § 1629a(6)(C) (2010).

294. Jesse, *supra* note 293 (noting that the student loan program has recently been "expanded to 19 districts nationwide").

295. For more thorough information on private collection agencies and student loans, the reader is encouraged to refer to the Department of Education's 2009 Private Collection Agencies Procedures Manual, *available at* http://epic.org/foia/ed/EPIC-ED-2009-PCA-Manual.pdf.

loans may also attempt to collect loans through litigation.[296] And litigation represents the primary recourse for private student lenders.

The Consumer Financial Protection Bureau will have authority to supervise non-bank student loan servicers beginning in March 2014, which is when this article goes to press. The CFPB will forward borrowers' complaints to the company, which has 15 days to respond.[297] While this article was in its final stages, the Consumer Financial Protection Bureau sued a for-profit alleging misconduct in its practice of channeling its students into private loans that were likely to default.[298]

To access judicial collection procedures like execution and garnishment, the creditor must convert its debt to a judgment. It does this by filing a lawsuit against the borrower. At this stage, the borrower may resort to state law defenses available to any other contract defendant, except those preempted by federal statute.[299]

### *1. Affirmative defenses*

Some state law defenses are expressly preempted. A borrower may not avoid repayment of federal student loans on state-law minority or infancy grounds.[300] Also, borrowers may not assert the statute of limitations against any action to collect on a federal student loan debt brought by the government, a guaranty agency, or (in the case of Perkins loans) a school.[301]

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296. 34 C.F.R. § 682.410 (2014) ("A guaranty agency may file a civil suit against a borrower to compel repayment only if [certain conditions are met]."); *see also* 34 C.F.R. § 674.46(a)(2) ("The institution shall sue the borrower [of a defaulted Perkins loan] if it determines that [certain conditions] are met.").

297. Andy Thomason, *Watchdog Agency to Monitor Largest Nonbank Student-Loan Servicers*, THE CHRONICLE OF HIGHER EDUCATION, December 13, 2013; Michelle Singletary, *Bureau Will Be Powerful Ally in The Corner of Student-loan Borrowers in March*, THE WASHINGTON POST, Dec. 4, 2013 at A14.

298. Kelly Field, Consumer Financial Protection Bureau Sues ITT as Predatory Lender, Feb. 17, 2014.]

299. *Cf.* Gibbs v. SLM Corp., 336 F. Supp. 2d 1, 8–9 (D. Mass. 2004) (holding that state statute of limitations barred borrower's action to avoid repayment of his student loans); *In re* Mason, 300 B.R. 160, 165–69 (Bankr. D. Conn. 2003) (applying Connecticut law to void consolidation that was obtained through duress); 71 Fed. Reg. 45,666, 45,676–77 (Aug. 9, 2006) (arguing that regulations protecting borrowers from forgery are unnecessary "because relief is already available for those instances under the common law (and in many instances, State law) defense of forgery").

300. 20 U.S.C. § 1091a(b)(2), (3) (2008).

301. *Id*. § 1091a(a)(2). One court has held that the bar on statutes of limitations applies to actions brought by third-party assignees (such as collection agencies), *see* Mountain Peaks

What about the equitable defense of laches? Laches under federal law requires that the plaintiff's unreasonable delay caused prejudice to the defendant. Prejudice may not be presumed from the length or unreasonableness of the delay.[302] If, however, state law permits such a presumption, and that presumption might be decisive in the case, the borrower may argue that state law, not federal law, should apply.

The federal statute's text is ambiguous. It says only that "no limitation shall terminate the period" that the lender may have to sue a borrower.[303] Laches is a time bar, but not a "limitation." But the overwhelming weight of authority rejects borrowers' laches arguments against student lenders. Five federal circuits have read the statute broadly to exclude laches.[304] One district court has applied laches to bar a lawsuit to enforce a federal student loan obligation.[305]

A weaker, but still alluring argument against laches in student-loan collection cases where the government is the plaintiff is the "well settled" rule "that the United States is not … subject to the defense of laches in enforcing its rights."[306] Two federal circuits have genuflected at this maxim

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Fin. Servs., Inc. v. Roth-Steffen, 778 N.W.2d 380, 386–87 (Minn. Ct. App. 2010), but a contrary reading of the statute is plausible, too.

302. Save the Peaks Coal. v. U.S. Forest Serv., 669 F.3d 1025, 1033 (9th Cir. 2012) ("A lengthy, unexpected delay that does not result in prejudice is not a sufficient basis for laches to apply."); Cornetta v. United States, 851 F.2d 1372, 1378 (Fed. Cir. 1988) ("Even lengthy delay does not eliminate the prejudice prong of laches test."); *see also* Clearfield Trust Co. v. United States, 318 U.S. 363, 366, 369–70 (1943) ("[D]amages occasioned by the delay must be established and not left to conjecture.").

303. 20 U.S.C. § 1091a(a)(2).

304. *See, e.g.*, United States v. Tuerk, 317 Fed. Appx. 251, 253 (3d Cir. 2009) (explaining that "Congress intended to allow recovery on a broad range of student loan debts by eliminating all limitations"); United States v. Lawrence, 276 F.3d 193, 196 (5th Cir. 2001) (following other circuits in "concluding that § 1091a eliminates all limitation[] defenses for collection of student debts"); United States v. Phillips, 20 F.3d 1005, 1007 (9th Cir. 1994) (explaining that Congress provided for an action to collect on defaulted student loans not subject to statute of limitations); United States v. Glockson, 998 F.2d 896, 897 (11th Cir. 1993) (explaining that amendments to the statute indicated an intent to remove the statute of limitations); United States v. Hodges, 999 F.2d 341 (8th Cir. 1993) (concluding that amendments removed the pre-1991 statute of limitations); *Cf.* Proctor v. U.S. Dep't of Educ., 196 Fed. Appx. 345, 349 (6th Cir. 2006) (declining to decide whether laches is applicable against the government and affirming the district court on the grounds that the defendant could not establish the elements of a laches defense as a matter of law).

305. *See* United States v. Rhodes, 788 F. Supp. 339, 342–43 (E.D. Mich.1992) (applying the equitable defense of laches to a seventeen year old student loan collection).

306. *See* United States v. Summerlin, 310 U.S. 414, 416 (1940) (concluding that the fact that "the claim was acquired by the United States through operation of the National

and rejected defendants' laches arguments.[307] But the rule is far from "well-settled," for the Court has approved the viability of laches as a defense to federal government claims in several cases.[308] The applicability of laches seems to turn largely on whether the federal government acts in a "proprietary" rather than "sovereign" capacity,[309] though the line between what is proprietary and what is sovereign is far from clear.

Courts have generally refused to allow a borrower to raise grounds for statutory discharge as a defense in collection litigation, on the theory that discharge is a matter within the jurisdiction of the agency that courts may consider only on judicial review.[310] A borrower who is facing a collection action but who may also have a viable claim for discharge should promptly seek discharge before the agency and ask the court to stay the collection litigation pending resolution of the administrative discharge petition.

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Housing Act" did not "take the case out of the rule").

307. *See* United States v. Tuerk, 317 Fed. Appx. 251, 253 (3d Cir. 2009) (conveying a belief that, even if the statute did not bar the defense of laches, the plaintiff would be unable to utilize it against the United States); United States v. Di Stefano, 279 F.3d 1241, 1245 n.2 (10th Cir. 2002) (explaining that "laches may not be asserted against the United States in an action brought to enforce a public right or a public interest"). A district court, albeit in dictum, suggested that a guaranty agency's stale claim could be revived by assignment to the Department of Education. United States v. Robbins, 819 F. Supp. 672, 677–79 (E.D. Mic. 1993).

308. *See, e.g.*, Clearfield Trust Co. v. United States, 318 U.S. 363, 369–70 (1943) (finding that, while laches is available the action brought by the United States, it must be proven and is not presumed due to length of time lapse).

309. *See* United States v. Peoples Household Furnishings, Inc., 75 F.3d 252, 255 (6th Cir. 1996) (citing United States v. California, 507 U.S. 746, 757–59 (1993) (proving that the Supreme Court had distinguished *Summerlin*, but left the general rule intact)); *see also Clearfield Trust*, 318 U.S. at 369 ("The United States does business on business terms") (quoting United States v. Nat'l Exchange Bank, 270 U.S. 527, 534 (1926))).

310. *See, e.g.*, United States v. Wright, 87 F. Supp. 2d 464, 466 (D. Md. 2000) ("Only the Secretary, not this Court, has discretion to [administratively] discharge the loan."); *In re* Scholl, 259 B.R. 345, 349 (Bankr. N.D. Iowa 2001) ("Ultimately, the Secretary of Education is initially responsible for determining whether the student loan described in the present case should be discharged."); *In re* Bega, 180 B.R. 642, 644 (Bankr. D. Kan. 1995) (finding the statute required the plaintiff to follow the administrative regulations in order to obtain a discharge from the Secretary). Some of the grounds for discharge—notably false certification based on identity theft or forgery—overlap with state law contract defenses. The buyer can raise these defenses notwithstanding the availability of the discharge procedure.

### *2. Post-Judgment Remedies*

Once the student-loan creditor has a judgment, it becomes a judgment creditor and may employ the statutory collection tools of fieri facias or execution,[311] garnishment,[312] and judgment lien.[313] A federal judgment creditor may use state-law collection techniques pursuant to Federal Rule of Civil Procedure 69.

The student loan debtor, now also a judgment debtor, has little recourse, unless she can have the judgment vacated. The primary refuges of a defaulting student loan debtor—consolidation and rehabilitation—are not available to the judgment debtor.

Since many student borrowers will not appear even if served, a lawyer will be well advised to be familiar with the procedures to reopen a default judgment. Federal Rule of Civil Procedure 60(b) allows a defendant to obtain relief from a judgment or order for one of the following six reasons:

> (1) mistake, inadvertence, surprise, or excusable neglect;
>
> (2) newly discovered evidence that, with reasonable diligence, could not have been discovered in time to move for a new trial under Rule 59(b);
>
> (3) fraud (whether previously called intrinsic or extrinsic), misrepresentation, or misconduct by an opposing party;
>
> (4) the judgment is void;
>
> (5) the judgment has been satisfied, released, or discharged; it is based on an earlier judgment that has been reversed or vacated; or applying it prospectively is no longer equitable; or
>
> (6) any other reason that justifies relief.[314]

The defendant must move to vacate the judgment within a "reasonable time," and within one year if she seeks to set aside the judgment for one of the first three reasons.[315] The defendant bears the burden of proving not

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311. Doug Rendleman, ENFORCEMENT OF JUDGMENTS AND LIENS IN VIRGINIA, ch. 2 (2d ed. 1994) [hereinafter RENDLEMAN, EJL-V 2D]; Doug Rendleman, ENFORCEMENT OF JUDGMENTS AND LIENS IN VIRGINIA, ch. 3 (3d ed. forthcoming Fall 2014) [hereinafter RENDLEMAN, EJL-V 3D].

312. RENDLEMAN, EJL-V 2D, ch. 3; RENDLEMAN, EJL-V 3D, at ch. 4.

313. RENDLEMAN, EJL-V 2D, ch. 4; RENDLEMAN, EJL-V 3D, at ch. 5.

314. Fed. R. Civ. P. 60(c).

315. *Id.*

only that she meets one of the six reasons and that the motion was timely, but also that she has a meritorious defense and that the plaintiff would not suffer unfair prejudice from vacating the default.[316] However, when a defaulting defendant has shown a meritorious defense, courts construe the enumerated grounds for relief liberally.[317]

## *IV. Exiting Default*

Borrowers unfortunate enough to find themselves in default on their loans have two primary options for exiting of default: consolidation and rehabilitation. Consolidation involves taking out a new loan to pay off the defaulted loan. Rehabilitation involves restoring the defaulted loan to regular repayment status. In addition to these two options, which are discussed in this section, a borrower may also pursue discharges described in the following section.

### *A. Consolidation*

Black's Law Dictionary defines debt consolidation as "[t]he replacement of multiple loans from one or more lenders with a single loan from one lender, usually with a lower monthly payment and a longer repayment period."[318] A federal student-loan borrower may consolidate her federal loans by taking out a consolidation loan. She and her loans must meet the eligibility requirements, and she must apply to the Secretary of Education for a Direct Consolidation loan.[319]

All HEA loans, including consolidation loans themselves, may be consolidated, as may Auxiliary Loans to Assist Students (ALAS), Health Education Assistance Loans (HEAL), and certain loans made under the Public Health Service Act.[320] However, a Direct Consolidation Loan cannot be consolidated by itself, but must be consolidated with another eligible loan.[321] FFEL consolidation loans may be consolidated into a Direct Loan

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316. Park Corp. v. Lexington Ins. Co., 812 F.2d 894, 896 (4th Cir. 1987).

317. Compton v. Alton Steamship Co., 608 F.2d 96, 102 (4th Cir. 1979) (quoting Tolson v. Hodge, 411 F.2d 123, 130 (4th Cir. 1969)).

318. BLACK'S LAW DICTIONARY (9th ed. 2009).

319. 34 C.F.R. § 685.220(e) (2014). Consolidation loans are no longer made under the defunct FFEL program, though borrowers may have FFEL consolidation loans outstanding.

320. 34 C.F.R. § 685.220(b).

321. 34 C.F.R. § 685.220(d)(2).

under some circumstances, in order to allow borrowers to access repayment plans available for Direct Loans but not FFELs.[322] Finally, a Perkins loan may not be consolidated by itself—at least one FFEL or Direct Loan must also be involved.[323]

A Direct Consolidation Loan is divided into subsidized, unsubsidized, and PLUS components, each component representing the portion of the loan that paid off underlying loans of that particular type.[324] The interest rates for each component of a consolidation loan correspond roughly to the interest rates on the type of loan underlying that component.[325]

A borrower not in default may consolidate at any time.[326] A borrower in default may consolidate provided that she either agrees to repay the consolidation loan under an ICR or IBR plan or makes "satisfactory repayment arrangements"—which means three consecutive "on-time voluntary full monthly payments."[327] A borrower may not consolidate loans when she is subject to a judgment on a federal student loan that has not been vacated, or an administrative wage garnishment order on an HEA loan that has not been lifted.[328]

Consolidation is no panacea. Interest and authorized penalties and fees, as well as the principal, of the loans being consolidated are all included in the principal balance of the consolidation.[329] This effectively capitalizes all interest, penalties, and fees of the consolidated loan. Consolidating defaulted loans will cause the borrower's credit report to indicate that the loan was in default but paid in full.[330] Additionally, consolidation can eliminate certain repayment and cancellation options. For example, a Direct Consolidation loan that pays off a Perkins loan and another kind of loan is not eligible for Perkins loan cancellation. Also, a

322. 34 C.F.R. § 685.220(d)(1)(i)(B)(3)–(5).

323. 34 C.F.R. § 685.220(d)(1)(i).

324. 34 C.F.R. § 685.220(c). Perkins and non-HEA loans are consolidated into the unsubsidized component. *Id.* § 685.220(c)(2).

325. 34 C.F.R. §§ 685.220(g) (2014), 685.202(a)(3).

326. 34 C.F.R. § 685.220(d)(1)(ii)(A)–(B).

327. 34 C.F.R. § 685.220(d)(1)ii)(C). The full monthly payment amount must be "reasonable and affordable based on the buyer's circumstances." *Id.*

328. 34 C.F.R. § 685.220(d)(1)(ii)(E)–(F).

329. 34 C.F.R. § 685.220(f)(1), (3).

330. U.S. DEP'T OF EDUC., *Direct Consolidation Loans: Frequently Asked Questions*, http://loanconsolidation.ed.gov/help/faq.html (last viewed Feb. 23, 2014).

consolidation loan that pays off a Parent PLUS loan and any other kind of loan is not eligible for income-based or pay-as-you-earn repayment.

On the other hand, consolidation may be an appropriate course of action for some borrowers. Many borrowers with FFEL loans may become eligible for an income-based or pay-as-you-earn repayment plan by consolidating the FFEL loans into a Direct Consolidation loan. For borrowers in default, consolidation is quicker than rehabilitation, which follows, and it does not require negotiating a repayment schedule with the creditor.

### *B. Rehabilitation*

Rehabilitation allows a borrower who is in default on her student loans to get out of default by making "appropriate and timely monthly payments."[331] A borrower who wishes to rehabilitate her student loans should consult applicable regulations[332] as well as the Department of Education's PCA Procedures Manual, which contains a chapter on loan rehabilitation.[333] Loans that have been reduced to a judgment may not be rehabilitated,[334] and loans that have been rehabilitated once since August 14, 2008 may not be rehabilitated a second time if the borrower subsequently goes into default.[335]

A borrower may rehabilitate a FFEL or Direct Loan by making nine consecutive "voluntary, reasonable, and affordable monthly payments within 20 days of the due date within ten consecutive months."[336] What constitutes a "reasonable and affordable monthly payment" is determined based on the amount owed and the borrower's individual circumstances, including the borrower's income and "reasonable and necessary expenses."[337] Regulations provide that, in order to be rehabilitated, a FFEL

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331. *PCA Procedures Manual*, *supra* note 200, at 87.

332. 34 C.F.R. §§ 685.211(f) (Direct), 682.405, 674.39.

333. *PCA Procedures Manual*, *supra* note 200, at Ch. 9.

334. 34 C.F.R. §§ 685.211(f)(3), 682.405(a)(1).

335. 34 C.F.R. §§ 685.211(f)(4), 682.405(a)(3).

336. 34 C.F.R. §§ 685.211(f)(1), 682.405(a)(2). A borrower who misses one payment will still be entitled to rehabilitation.

337. 20 U.S.C. § 1078-6(a)(1)(B) (2010); 34 C.F.R. §§ 685.311(f)(1), 682.405(a)(2); *See PCA Procedures Manual*, *supra* note 200, at 103. Depending on the size of the loan and whether the loan is a FFEL or Direct Loan, a certain percentage of the balance to be rehabilitated will be considered "reasonable and affordable." *Id.* at 94, 111–12. These "minimum payment amounts" may be reduced in special circumstances. *Id.* at 92, 109–10. A

loan must be sold to an eligible lender.[338] Because the statute only provides that a loan must be sold to an eligible lender if practicable,[339] and because regulations do not require sale of Direct Loans as a condition precedent to rehabilitation, the National Consumer Law Center has characterized this requirement as "ripe for legal challenge."[340]

To rehabilitate a defaulted Perkins loan, a borrower must make nine consecutive on-time monthly payments.[341] The school must return the borrower to regular repayment status within thirty days after receiving the last on-time monthly payment.[342] A Perkins loan that has been reduced to a judgment may not be rehabilitated.[343] Additionally, Perkins loans may be rehabilitated only once.[344]

## *V. Discharging Student Loans*

There are two ways borrowers may potentially discharge their student loan debt: statutory discharge under certain provisions of the Higher Education Act, and discharge in bankruptcy. Neither is particular easy to obtain.

### *A. Statutory Discharge*

#### *1. School-Related Discharges*

Student loans received after January 1, 1986 may qualify for a school-related discharge on one of three grounds: school closure, false certification, and unpaid refund.[345] The common link between these three

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borrower who is subject to unaffordable "minimum payments" could potentially challenge the payments as inconsistent with the statute, which bars a guaranty agency or the Secretary from requiring the buyer to pay "more than is reasonable and affordable based on the borrower's total financial circumstances." 20 U.S.C. § 1078-6(a)(1)(B). Since the minimum payment amounts are set forth in a manual, rather than a formal rule, they should receive Skidmore-Mead deference, rather than Chevron deference, on judicial review.

338. 34 C.F.R. § 682.405(a)(2)(ii).

339. 20 U.S.C. § 1078-6(a)(1)(A)(ii).

340. NAT'L CONSUMER LAW CTR., *supra* note 217, at § 6.3.5.

341. 34 C.F.R. § 674.39(a)(2).

342. 34 C.F.R. § 674.39(b)(1).

343. 34 C.F.R. § 674.39(a).

344. 34 C.F.R. § 674.39(e).

345. 20 U.S.C. § 1087(c) (2010).

grounds for discharge is that they involve a school's misconduct or failure to perform contractual obligations.[346]

If the decision-maker is satisfied that the borrower has met the requirements set forth in statute and regulation, the borrower's obligation to repay the loan is discharged. In exchange for discharge, the borrower assigns all claims to a refund for the discharged sum to the Secretary[347] and agrees to cooperate with the Secretary's efforts to enforce these rights.[348]

*Closed School.* School closure discharge relieves borrowers of the obligation to repay federal loans taken out to finance an educational program that they were unable to complete because the school offering the program closed.[349] A borrower is not eligible for discharge, however, if she completes or is in the process of completing her course of study either through a "teach-out" at another school or by transferring credits from the closed school to another school.[350]

To obtain a discharge, a borrower must submit to the holder of the loan a request for discharge along with a sworn statement declaring that she meets each of the criteria for eligibility.[351] A borrower may be ineligible for discharge if she obtained the loan by fraudulent means.[352] The borrower

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346. False certification because of identity theft, which was not in the original school-related discharge provision but added later, is arguably an exception to this general observation.

347. 34 C.F.R. §§ 685.214(e), 685.215(c)(6)(ii), 685.216(c)(1)(iii)(B), 682.402(d)(5), 682.402(e)(5), 682.402(*l*)(4)(iii)(B), 674.33(g)(7). Administrative unpaid refund and false certification discharges are not available for Perkins loans, but borrowers should be able to raise these matters as defenses or counterclaims in litigation.

348. 34 C.F.R. §§ 685.214(d), 685.215(c)(6)(ii), 685.216(c)(1)(iii)(B), 682.402(d)(4), 682.402(e)(4), 682.402(*l*)(4)(iii)(B), 674.33(g)(6).

349. 20 U.S.C. § 1087(c); 34 C.F.R. §§ 685.214(b), 682.402(d)(2), 674.33(g)(2). The borrower qualifies for discharge if she was attending the school when it closed or if she withdrew from the school not more than 90 days before it closed, a deadline that can be extended in extraordinary circumstances at the Secretary's discretion. 34 C.F.R. §§ 685.214(f)(1), 682.402(d)(1), 674.33(g)(4)(i)(B). A school's closure date is the date on which the school "ceases to provide education instruction in all programs, as determined by the Secretary. 34 C.F.R. §§ 685.214(a)(2)(i), 682.402(d)(1)(ii)(A), 674.33(g)(1)(ii)(A). The Secretary maintains a list of closure dates on its website. www2.ed.gov/offices /OSFAP/PEPS/docs/closedschoolsearch.xlsx.

350. 34 C.F.R. §§ 685.214(c)(1)(iii), 682.402(d)(3)(ii)(C), 674.33(g)(4)(i)(C). Regulations define a teach-out plan as "a written plan developed by an institution that provides for the equitable treatment of students if [the institution] ceases to operate before all students have completed their program of study…." 34 C.F.R. § 602.3.

351. 34 C.F.R. §§ 685.214(c)(1), 682.402(d)(3)(ii), 674.33(g)(4)(i).

352. 34 C.F.R. § 674.33(g)(5) (Perkins). The regulations for Direct and FFEL loans do not contain such a provision.

must state whether she has made any claims against third parties relating to the school closure, transfer any claims against third parties to the Secretary, or the Secretary's designee, and promise to comply with the cooperation requirement.[353]

If the Secretary holds a loan, he determines eligibility for closed-school discharge in the first instance.[354] A school that holds a Perkins loan initially determines the borrower's eligibility for discharge of that loan, but the borrower has the right to de novo review before the Secretary.[355] Judicial review of the Secretary's closed-school discharge decision is available under the APA.[356]

For FFEL loans held by lenders or guaranty agencies, the guaranty agency makes the final determination of eligibility.[357] Regulations do not provide for review of guaranty agency closed-school discharge determinations by either the Department or the courts.[358] FFEL loans may be discharged without application if the borrower has received a closed-school discharge on a Direct or Perkins Loan.[359]

*False Certification and Identity Theft*. A borrower may obtain a false certification discharge where the student's eligibility for federal student loans "was falsely certified by the eligible institution or was falsely certified as a result of a crime of identity theft[.]"[360] False certifications fall into three general categories. First, the school certifies an ineligible student as eligible for a loan. Second the school, without authorization from the student, signs a student's name to a student loan-related document or otherwise authorizes a transaction on the student's behalf. Third, the school certifies a student's eligibility for a student loan as a result of identity theft.

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353. 34 C.F.R. §§ 685.214(c)(2), (3) (Direct); 682.402(d)(3)(i), (iii), (iv) (FFEL); 674.33(g)(4)(ii), (iii) (Perkins).

354. 34 C.F.R. § 685.214(g)(5), (6).

355. 34 C.F.R. § 674.33(g)(8).

356. 5 U.S.C. § 701–706.

357. 34 C.F.R. §§ 682.402(d)(6)(i)(G), (H), 682.402(d)(6)(ii)(E), (F).

358. The Department of Education's Student Aid website indicates that the holder of the loan makes the "final decision" in all cases except those involving false certification and forged signature for FFEL or Direct Stafford Loans. U.S. DEP'T OF EDUC., *Forgiveness, Cancellation, and Discharge*, FED. STUDENT AID, http://studentaid.ed.gov/PORTALSWebApp/students/english/discharges.jsp (last visited Feb. 13, 2014).

359. 34 C.F.R. § 682.402(d)(8). Perkins loans are also subject to discharge by the Secretary without application in limited circumstances. 34 C.F.R. § 674.33(g)(3).

360. 20 U.S.C. § 1087(c)(1).

False certification of ineligible students is a serious and still a common problem.[361] It may involve a range of misconduct, from assisting students in obtaining GEDs and diplomas from diploma mills[362] to blatant tampering with and encouraging cheating on standardized eligibility tests.[363] If a school certifies a student who does not meet the criteria set forth in 20 U.S.C. § 1091 or 34 C.F.R. § 668.32, then the student is entitled to a false certification discharge.[364]

Recent changes in eligibility regulations should curtail some of the worst abuses. From January 1, 1986 to July 1, 2012, a non-high-school graduate could take out a student loan if the school certified the student's "ability to benefit" as defined by statute at the time of certification and enrollment.[365] However, under the 2011 amendments to the Higher Education Act, only those with a high school diploma "or the recognized equivalent" or those who have completed a secondary school education, as determined by state law, in a home-school setting are eligible to receive student loans.[366]

Even if she meets federal eligibility requirements, a student may be ineligible for loans for job-specific training programs because state law bars her from holding the position for which the training program is intended. If a school certifies a student who is not qualified under state law for the intended occupation because of criminal history, physical or mental

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361. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-09-600, PROPRIETARY SCHOOLS: STRONGER DEPARTMENT OF EDUCATION OVERSIGHT NEEDED TO HELP ENSURE ONLY ELIGIBLE STUDENTS RECEIVE FEDERAL STUDENT AID, 22–25 (2009), *available at* http://www.gao.gov/new.items/d09600.pdf; *see also*, OFFICE OF INSPECTOR GENERAL, U.S. DEP'T OF EDUC., JURY RETURNS GUILTY VERDICTS IN FRAUD CASE (June 30, 2004), http://www2.ed.gov/about/offices/list/oig/invtreports/mi062004.html (detailing a fraud scheme that cost the Department of Education approximately $1,000,000).

362. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 247, at 26–28 (describing the problems associated with diploma mills and GED assistance).

363. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, *supra* note 247, at 22–25 (telling that numerous nefarious practices occur and how they might result in otherwise ineligible students receiving federal aid).

364. *See* Jordan v. Sec'y of Educ., 194 F.3d 169, 171 (D.C. Cir. 1999) ("[T]he statutory scheme is designed to place obligations . . . on the government, which must police schools to ensure that their certifications are accurate, or failing that must compensate defrauded students.").

365. *See* 34 C.F.R. § 682.402(e)(13) (setting out different ability to benefit tests that apply for loans taken out at different times).

366. 20 U.S.C. § 1091(d). Certification based on home school education alone is available for loans received on or after July 1, 2000, provided the student meets the specified requirements. 34 C.F.R. §§ 668.32(e)(4), 682.402(e)(13)(ii)(A).

condition, age, or other reason accepted by the Secretary, the student is entitled to discharge of the loan.[367] The student must be ineligible under the law of the state of the *student's* residence at the time of *certification*.[368] This narrow ground for discharge applies only if the borrower's education "specifically and exclusively" prepares her only for professions that state law will not let her practice.[369]

A borrower seeking discharge of a student loan for false eligibility certification must present evidence corroborating the claim in her applications.[370] Potential sources of evidence include Freedom of Information Act aimed at the Department of Education's investigative reports, records from the school and (if applicable) the testing company, testimony of current or former school officials who knew of or participated in the fraud, and testimony or applications for false certification discharge from other borrowers that attended the school.

When a school, without authorization, signs a student's name to a loan application or promissory note, the student is entitled to discharge of the entire amount of the unauthorized loan.[371] Additionally, when a school endorses a student loan check in the borrower's name or authorizes on the borrower's behalf an electronic transfer of student loan funds, the student may be entitled to discharge the amount of the check or transfer.[372] To apply for a discharge of an unauthorized loan or payment, the borrower must state that she did not sign or authorize the transaction and provide five authentic signature specimens, including two specimens dating from within one year of the contested signature.[373] To qualify for an unauthorized payment discharge, the borrower must state that she neither actually

367. 34 C.F.R. §§ 685.215(a)(1)(iii), 682.402(e)(13)(iii)(FFEL).

368. *Id*.

369. *See* Johnson v. U.S. Dep't of Educ., 580 F. Supp. 2d 154, 157–58 (D.D.C. 2008) (affirming Secretary's denial of discharge to borrower for loans taken out for college's paralegal studies program, because although borrower's criminal record precluded him from employment as a paralegal, the program provided him with skills applicable to other jobs).

370. U.S. DEP'T OF EDUC., DEAR COLLEAGUE LETTER, GEN-95-42 (Sept. 1995), *available at* http://www.ifap.ed.gov/dpcletters/doc0340_bodyoftext.htm; *see also* Gill v. Paige, 226 F. Supp. 2d 366, 373–74 (E.D.N.Y. 2002) (upholding the Department's policies regarding burdens of proof).

371. 34 C.F.R. §§ 685.215(a)(1)(ii), (b)(1), 682.402(e)(1)(i)(B), (e)(2)(i).

372. 34 C.F.R. §§ 685.215(a)(1)(iii), (b)(2), 682.402(e)(1)(i)(C), (e)(2)(v).

373. 34 C.F.R. §§ 685.215(c)(2)(i)–(ii), (c)(3)(i)–(ii), 682.402(e)(4)(iii)(A), (B), (e)(4)(iv)(A), (B).

received the funds disbursed nor had the disbursement applied as a credit to charges she owed to the school.[374]

Discharge for identity theft may be available for Direct loans as well as FFEL loans received on or after July 1, 2006.[375] The criteria for identity theft discharge are onerous. To be eligible for an identity theft discharge, a borrower must certify that the borrower did not sign the promissory note or authorize the use of her identification in any way to obtain the loan and that she did not receive or benefit from the proceeds of the loan knowing that it had been obtained without her authorization.[376] The borrower must also supply "a copy of a local, [s]tate or [f]ederal court verdict or judgment . . . conclusively determin[ing]" that she was the victim of identity theft by a perpetrator named in that judgment or verdict. If that judgment or verdict does not "expressly state that the loan was obtained as a result of the crime," the borrower must also provide authentic signature specimens or other means of identification corresponding to the type of identification used to obtain the loan moved fraudulently and a statement of facts that demonstrate that eligibility was falsely certified as a result of the identity theft.[377]

To obtain discharge under any of the false certification provisions, the borrower must submit a sworn statement to the holder of the loan asserting facts necessary to qualify for discharge.[378] The borrower must also state whether she has made a claim against any third party relating to the false certification,[379] assign pertinent causes of action to the Secretary or the Secretary's designee, and promise to cooperate with any investigative and enforcement efforts.[380] Initial decision-making authority rests with the Department for any loans it holds, and with the guaranty agency for FFEL loans that have not yet been assigned to the Secretary.[381] For decisions made by the guaranty agency, the borrower is entitled to request review by

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374. 34 C.F.R. §§ 685.215(c)(3)(iii), 682.402(e)(4)(iv)(C).

375. 20 U.S.C. § 1087(c)(1); 34 C.F.R. §§ 685.215(a)(1)(iv),682.402(e)(1).

376. 34 C.F.R. §§ 685.215(c)(4)(i), (ii), 682.402(e)(4)(v)(i), (ii).

377. 34 C.F.R. §§ 685.215(c)(4)(iii), (iv), 682.402(e)(4)(v)(iii), (iv).

378. 34 C.F.R. §§ 685.215(c), 682.402(e)(3).

379. 34 C.F.R. §§ 685.215(c)(5), 682.402(e)(3)(i).

380. 34 C.F.R. §§ 685.215(c)(6), 682.402(e)(3)(vi), (vii).

381. Procedures for false certification discharge are detailed at 34 C.F.R. § 685.215(d) for Direct loans and 34 C.F.R. § 682.402(e)(6)–(11).

the Secretary.[382] Review of the Secretary's decision is available under the APA.

*Unpaid Refunds.* A student who takes out a FFEL or Direct loan toward a program but completes less than 60 percent of the program for which that loan is designated is eligible for a refund from the school.[383] The amount of the refund depends on the date the student leaves the school.[384] If the amount of the unpaid refund exceeds the remaining balance of the loan, the student is entitled to be reimbursed for the excess.[385]

To receive an unpaid-refund discharge, the student must submit an application to the holder of the loan or a guaranty agency if the loan was made under the FFEL program.[386] The application must include a sworn statement declaring that the borrower meets each of the criterion for eligibility; additionally, the borrower must state whether any other applications for discharge of the loan are pending, transfer any claims against third parties to the Secretary, or the Secretary's designee, and promise to comply with the cooperation requirement.[387] The borrower is not entitled to discharge if she is still attending the school; she and the Secretary, for a Direct loan, or the guaranty agency, for a FFEL loan, must attempt to resolve the unpaid refund for 120 days before she becomes eligible for discharge.[388]

### *2. Discharges for Death and Disability*

The Secretary, guaranty agency, or educational institution will discharge a loan upon receiving an original or certified copy of a death certificate of either the borrower or in the case of a parent PLUS loan, the student.[389]

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382. 34 C.F.R. § 682.402(e)(11).

383. 34 C.F.R. §§ 685.216, 682.402(l)–(o).

384. 34 C.F.R. §§ 685.216(d); 682.402(o)(2).

385. 34 C.F.R. §§ 685.216(b); 682.402(l)(3).

386. 34 C.F.R. §§ 685.216(c); 682.402(l)(4).

387. 34 C.F.R. §§ 685.216(c); 682.402(l)(4)(ii).

388. 34 C.F.R. §§ 685.216(a)(2); 682.402(*l*)(2).

389. 20 U.S.C. §§ 1087(a)(1) (FFEL), 1087dd(c)(1)(F)(i) (Perkins); 34 C.F.R. §§ 685.212(a) (Direct), 682.402(b) (FFEL), 674.61(a) (Perkins). Loans may be discharged based on other reliable evidence of death in extraordinary circumstances. 34 C.F.R. §§ 685.212(a)(2) (Direct), 682.402(b) (FFEL), 674.61(a) (Perkins).

Student loans may also be discharged if the *borrower* becomes totally and permanently disabled, as defined by the Secretary.[390] A borrower seeking a disability discharge must submit an application to the lender, for a FFEL loan, or to the Secretary, for a Direct or Perkins loan.[391] The application must include a certification by a physician that the borrower is totally and permanently disabled and must be submitted within 90 days of the physician's certification.[392] In lieu of such a certification, Direct and Perkins borrowers may submit a notice of award of Social Security disability benefits from the Social Security Administration indicating that the borrower's next scheduled disability review will be within five to seven years.[393]

Once a borrower has notified the Secretary or the loan holder that she intends to seek a disability discharge, collection activity must be suspended for up to 120 days pending receipt of her application.[394] After the borrower has submitted an application, collection activities must be suspended until the Secretary or loan holder reaches its decision.[395]

If a FFEL loan is held by a guaranty agency or lender, and the loan holder approves the discharge application, the loan must be assigned to the Secretary.[396] A guaranty agency or lender may, consistent with Department guidance, request additional evidence, and even seek review by an independent physician in making the determination.[397]

If the agency or lender does determine that the student is permanently and totally disabled, the Secretary makes an independent, or, for Direct or Perkins loans, initial, determination of her eligibility.[398] If the Secretary

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390. 20 U.S.C. §§ 1087(a)(1) (FFEL), 1087dd(c)(1)(F)(ii) (Perkins); 34 C.F.R. §§ 685.213(b) (Direct), 682.402(c) (FFEL), 674.61(b) (Perkins). "Totally and permanently disabled" is defined at 34 C.F.R. § 682.200.

391. 34 C.F.R. §§ 685.213(b)(1), 682.402(c)(2), 674.61(b)(2)(iv).

392. 34 C.F.R. §§ 685.213(b)(2)(i), (b)(3), 682.402(c)(2), 674.61(b)(2)(iv)(A), (b)(2)(v). A streamlined application process, requiring only documentation from the Department of Veterans Affairs, is available to veterans. *See* 34 C.F.R. §§ 685.213(c), 682.402(c)(9), 674.61(c).

393. 34 C.F.R. §§ 685.213(b)(2)(ii), 674.61(b)(2)(iv)(B).

394. 34 C.F.R. §§ 685.213(b)(1)(ii); 674.61(b)(2)(ii)(D).

395. 34 C.F.R. §§ 685.213(b)(3)(ii); 682.402(c)(7), 674.61(b)(2)(ix)(B).

396. 34 C.F.R. §§ 682.402(c)(2).

397. *See* U.S. DEP'T. OF EDUC., *New Total and Permanent Disability Discharge Procedures for Title IV Loans – Effective July 1, 2002* (May 2002), *available at* http://ifap.ed.gov/dpcletters/GEN0203.html.

398. 34 C.F.R. §§ 685.213(b)(4), 682.402(c)(3), 674.61(b)(3).

determines that the borrower is permanently and totally disabled, the Secretary discharges the loan; otherwise, the loan is due and payable to the Secretary under the terms of the promissory note.[399] If the borrower's application is insufficient to prove disability, the Secretary may require her to submit additional evidence or arrange for additional review of her condition by an independent physician at the government's expense.[400]

The borrower must return any loan disbursements made between the date the physician certifies her disability and the date of her discharge. Her discharge request will not be processed until she does so.[401] A borrower who has received a disability discharge must notify the Secretary of any change of address and of her annual earnings from employment, if the Secretary requests the information or if those earnings are great enough to trigger reinstatement.[402] A loan discharged for permanent and total disability may be reinstated if she has earnings above 100% of the poverty guideline for a family of two, receives a new TEACH grant or federal student loan, except for a consolidation loan including loans that were not discharged, fails to return loan disbursements received after the date of disability but before the date of discharge, or receives a notice from the Social Security Administration indicating that she is no longer disabled or that her continuing disability review will no longer be the five- to seven-year period indicated in the notice of award of disability benefits.[403] The Secretary must provide the borrower with notice of the reinstatement and an explanation of reasons and when she must begin repayment.[404]

If the agency or lender does not approve the discharge application, it must notify the borrower, and it may resume collection activity.[405]

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399. 34 C.F.R. §§ 685.213(b)(4)(iii)–(iv), 682.402(c)(3), 674.61(b)(3)(v)–(vi). A Perkins loan that is discharged must be assigned to the Secretary. 34 C.F.R. § 674.61(b)(3)(iv).

400. 34 C.F.R. §§ 685.213(b)(4)(ii), 682.402(c)(3)(ii), 674.61(b)(3)(ii).

401. 34 C.F.R. §§ 685.213(b)(5) (Direct), 682.402(c)(4) (FFEL), 674.61(b)(4) (Perkins).

402. 34 C.F.R. §§ 685.213(b)(8) (Direct), 682.402(c)(7) (FFEL), 674.61(b)(7) (Perkins).

403. 34 C.F.R. §§ 685.213(b)(7)(i) (Direct), 682.402(c)(6)(i) (FFEL), 674.61(b)(6)(i) (Perkins).

404. 34 C.F.R. §§ 685.213(b)(7)(iii) (Direct), 682.402(c)(6)(iii) (FFEL), 674.61(b)(6)(iii) (Perkins).

405. 34 C.F.R. § 682.402(c)(7)(iii), (v).

### *B. Discharge of Student Loans in Bankruptcy*

Most insolvent debtors may find a refuge in the Bankruptcy Court where they may cast their debts off and end creditors' collection techniques. This refuge is unavailable to many student-loan borrowers.

"The principal purpose of the Bankruptcy Code is to grant a 'fresh start' to the 'honest but unfortunate debtor.'"[406] To accomplish this purpose, the Code allows a debtor to discharge most unpaid debts, if the conditions for discharge are met.[407]

Some debts, however, may not be discharged. Bankruptcy Code Section 523 lists the exceptions to the general rule.[408] The student loan exception provides that, "[u]nless excepting such debt from discharge . . . would impose an undue hardship on the debtor and the debtor's dependents," discharge is not available for:

> "(A)(i) An educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution; or
>
> (ii) an obligation to repay funds received as an educational benefit, scholarship, or stipend; or
>
> (B) any other educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who was an individual."[409]

The creditor bears the burden of proof by a preponderance of evidence to demonstrate that its debt falls into one of these three categories.[410] In order to obtain "undue hardship" discharge of a loan falling under the exception, the debtor must bring an adversary proceeding against the creditor in question.[411] The burden of proving undue hardship falls on the debtor.[412]

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406. Marrama v. Citizens Bank of Massachusetts, 549 U.S. 365, 367 (2007) (quoting Grogan v. Garner, 498 U.S. 279, 286–87 (1991)).

407. 11 U.S.C. §§ 727, 1328; *Marrama*, 549 U.S. at 367.

408. 11 U.S.C. § 523(a).

409. 11 U.S.C. § 523(a)(8).

410. Grogan v. Garner, 498 U.S. 279 (1991) (holding that the creditor bears the burden of proving by a preponderance of the evidence that an exception to dischargability applies).

411. United Student Aid Funds, Inc. v. Espinosa, 130 S. Ct. 1367, 1373 (2010). Prior to *Espinosa*, some Chapter 13 debtors attempted to obtain discharge of student loans by filing a plan listing student loan debts among those that will be discharged once the debtor makes

Section 523(a)(8) presents two key issues that debtors, creditors, and courts must address: First, what is the scope of the exception, that is, what debts does it exclude from discharge absent undue hardship? Second, what constitutes "undue hardship" that will allow discharge of a debt covered by the section's literal terms? This section addresses those questions in turn.

*1. The Scope of the Discharge Exception*

Subsection (A)(i) excludes all federal student loans, as all of these are made, Direct, or guaranteed or insured, FFEL, by the federal government, or made under a program funded in part by the federal government, Perkins and its predecessors. It also excludes loans made, insured, or funded by state or local governments; loans funded by nonprofits; and overpayments of educational benefits.[413] The weight of authority has applied subsection (A) to bar discharge of debts held by non-student student-loan debtors like parents' PLUS loans).[414]

What is now subsection (A)(ii) was added to section 523(a)(8) as part of the Crime Control Act of 1990,[415] and was designed to extend the exception's coverage "to debts which are similar in nature to student loans."[416] The prototypical situation covered in subsection (A)(ii)—which excludes "obligations to repay funds received as an educational benefit, scholarship, or stipend"—involves a student who accepted a scholarship or stipend requiring her agreement to perform certain service following graduation, and subsequently failed to perform that service.[417] Some courts have construed this provision more broadly to apply to actual loans.[418] That

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the required payments under the plan. *See, e.g.*, *In re* Banks, 299 F.3d 296, 301 (4th Cir. 2002). In *Espinosa*, the Supreme Court held that if a student-loan creditor receives notice of such a plan and fails to object, the creditor is bound by it and the loans are discharged. 130 S. Ct. at 1372. However, the Court openly criticized the tactic, which it characterized as a "bad-faith attempt to discharge student loan debt without the undue hardship finding Congress required," and endorsed imposition of sanctions against debtors and attorneys who would employ it in the future. *Id.* at 1382.

412. *In re* Frushour, 433 F.3d 393, 400 (4th Cir. 2005).

413. *See, e.g.*, *In re* Merchant, 958 F.2d 738 (6th Cir. 1992).

414. *See, e.g.*, *In re* Pelkowski, 990 F.2d 737 (3d Cir. 1993); *In re* Wilcon, 143 B.R. 4 (D. Mass. 1992).

415. *See* Pub. L. No. 101-647, § 3621 (1990).

416. 136 CONG. REC. H13288-02, H13289 (daily ed. Oct. 27, 1990) (statement of Rep. Brooks), 1990 WL 168500.

417. *See, e.g.*, *In re* Burks, 244 F.3d 1245 (11th Cir. 2001).

418. *See, e.g.*, *In re* Carow, 2011 WL 802847 (Bankr. D.N.D. Mar. 2, 2011); *In re*

is a dubious reading, to say the least; it would render the subsequently-enacted subsection (B) irrelevant and leave subsection (A)(i) with nothing to do beyond forbidding discharges of debts arising from benefit overpayments (if (A)(ii) doesn't cover that, too). In any event, this provision should not apply unless the student actually received monetary payments from the creditor.[419] If the creditor simply provided educational services to the obligor in exchange for the student's promise to perform certain services after graduation, it will not fall under subsection (A)(ii).

Subsection (B) was added in 2005 as part of the Bankruptcy Abuse Prevention and Consumer Protection Act,[420] and exempts "qualified educational loans," as defined by section 221(d)(1) of the Internal Revenue Code, from discharge. In short, if interest payments on the loan qualify for a tax deduction, the loan cannot be discharged. To constitute a qualified educational loan, the "indebtedness [must be] incurred by the taxpayer solely to pay qualified higher educational expenses."[421] "Qualified educational expenses" is based on the cost of attendance, as defined by a provision in the old version of the Higher Education Act.[422]

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Skipworth, 2010 WL 1417964 (Bankr. N.D. Ala. Apr. 1, 2010) (holding bank loan borrowed to pay for bar review course is excepted from discharge under § 523(a)(8)(A)(ii)).

419. *See, e.g.*, *In Re* Rezendes, 318 B.R. 436, 444–45 (Bankr. N.D. Ind. 2004); *In Re* Ray, 262 B.R. 544, 551 (Bankr. N.D. Okla 2001); *but see, In re* Udell, 454 F.3d 180 (3d Cir. 2006) (holding that Air Force Academy graduate who failed to perform active duty service obligation could not discharge obligation to reimburse the government for costs of his education except upon a showing of undue hardship); *In re* Mehlman, 268 B.R. 379 (Bankr. S.D.N.Y. 2001) (suggesting that this provision applies to tuition payments made by New York City Board of Education to NYU on behalf of student who agreed to perform service obligations upon graduation).

420. Pub. L. No. 109-8, § 220, 119 Stat. 23, 59 (2005).

421. 26 U.S.C. § 221(d)(1). The expenses in question must also be incurred on behalf of the taxpayer, her spouse, or a person who was a dependent of the taxpayer when the debt was incurred; be paid or incurred within a reasonable period of time after the indebtedness is incurred; and be "attributable to education furnished" while the recipient was an eligible student. *Id.*

422. 26 U.S.C. § 221(d)(2) reads in full:

> "The term "qualified higher education expenses" means the cost of attendance (as defined in section 472 of the Higher Education Act of 1965, 20 U.S.C. 1087ll, as in effect on the day before the date of the enactment of the Taxpayer Relief Act of 1997) at an eligible educational institution, reduced by the sum of—
>
> (A) the amount excluded from gross income under section 127, 135, 529, or 530 by reason of such expenses, and
>
> (B) the amount of any scholarship, allowance, or payment described in section 25A (g)(2).

Subsection B expanded the educational debt exception to discharge to include most private educational loans. But a private loan may be dischargeable in some circumstances. First, a "mixed-use" private loan, that is, a loan not *solely* incurred for qualified educational expenses, is dischargeable.[423] Second, the educational institution must have met eligibility requirements for participation in Title IV assistance programs.[424] Thus, a loan to attend an unaccredited school should be fully dischargeable. Third, the student must have been enrolled in a program leading to a recognized educational credential at an eligible institution of higher education, a course of study necessary for enrollment in such a program, or in a program necessary for a professional teaching credential or certification required by state law for employment as a teacher.[425] The student must also have carried "at least half the normal full-time work load for the course of study the student" pursued"[426] and may not have been enrolled in a primary or secondary school at the time.[427] Fourth, a loan the borrower incurred to pay the educational expenses of another person who is neither a spouse nor a dependent as defined by the tax code should be dischargeable.[428] Fifth, debtors have successfully argued that loans taken out when the borrower

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> For purposes of the preceding sentence, the term "eligible educational institution" has the same meaning given such term by section 25A (f)(2), except that such term shall also include an institution conducting an internship or residency program leading to a degree or certificate awarded by an institution of higher education, a hospital, or a health care facility which offers postgraduate training.

423. 26 C.F.R. § 1.221-1(e)(4) ex. 6 (stating that a private loan that is, in part, for residential improvements and, in part, for educational expenses does not qualify as an education loan).

424. 26 U.S.C. § 221(d)(2) ("eligible educational institution" is as defined in 26 U.S.C. § 25A(f)(2), but also includes postgraduate internship and residency programs leading to degree or certificate offered by an institution of higher education, hospital, or health care facility that offers postgraduate training); 26 U.S.C. § 25A(f)(2) ("eligible educational institution" means an institution described in 20 U.S.C. § 1088 as in effect in 1997 and that is eligible to participate in title IV). 20 U.S.C. § 1088 (1997) (amended 1998).

425. 26 U.S.C. § 221(d)(3) ("The term 'eligible student' has the meaning given such term by section 25A (b)(3)."); 26 U.S.C. § 25A(b)(3)(A) (defining an eligible student as one who meets the criteria of 20 U.S.C. § 1091(a)(1), as in effect in 1997); 20 U.S.C. § 1091(a)(1) (1997) (amended 1998).

426. 26 U.S.C. § 25A(b)(3)(B).

427. 20 U.S.C. § 1091(a)(1) (1997) (amended 1998) (providing that a student must "be enrolled or accepted for enrollment" in a postsecondary institution to receive financial assistance).

428. 26 U.S.C. § 221(d)(1)(A), (d)(4).

was not "a taxpayer" fall outside the plain language of section 221 of the Internal Revenue Code and thus outside the scope of the exception.[429] Finally, some courts have held that loans for business, rather than educational, purposes fall outside the scope of the exception.[430]

Courts have addressed the question of what constitutes a "loan" for the purposes of subsections (A)(i) and (B). The Second Circuit in *In re Renshaw* defined a loan as "(i) a contract, whereby (ii) one party transfers a defined quantity of money, goods, or services to another, and (iii) the other party agrees to pay for the sum or items transferred at a later date."[431] The agreement must be reached prior to or contemporaneous with the transfer.[432] The Third, Seventh, and Ninth circuits have expressly adopted the *Renshaw* approach.[433] Other courts take an arguably broader approach, looking to the intent of the parties and to the "substance of the transaction."[434] Some courts have not expressly required a prior or contemporaneous agreement to repay.[435]

Whatever approach a court claims to take, an extension of credit from an institution to a student pursuant to a prior or contemporaneous agreement will usually be found to constitute a "loan" within the meaning of the discharge exception.[436] By contrast, a debt arising from a student's

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429. *See In re* LeBlanc, 404 B.R. 793 (Bankr. M.D. Pa. 2009) (finding that a nonresident alien who did not file a tax return while at school was not a "taxpayer" and was entitled to discharge of private student loan).

430. *See, e.g.*, *In re* Hawkins, 317 B.R. 104 (B.A.P. 9th Cir. 2004); *In re* McFadyan, 192 B.R. 328 (Bankr. N.D.N.Y. 1995).

431. *In re* Renshaw, 222 F.3d 82, 88 (2d Cir. 2000) (citing *In re* Grand Union Co., 219 F. 353, 356 (2d Cir. 1914)).

432. *Id.*

433. *In re* Chambers, 348 F.3d 650 (7th Cir. 2003); *In re* Mehta, 310 F.3d 308 (3d Cir. 2002); *In re* Hawkins, 317 B.R. 104 (9th Cir. B.A.P. 2004), aff'd and adopted 469 F.3d 1316 (9th Cir. 2006). Bankruptcy courts that have examined Renshaw have also found it persuasive. *See, e.g. In re* Moore, 407 B.R. 855 (Bankr. E.D. Va. 2009); *In re* Gakinya, 364 B.R. 366 (Bankr. W.D. Mo. 2007); *see also In Re* Johnson, 222 B.R. 783 (Bankr. E.D. Va. 1998) (adopting the test from *In Re Grand Union Co.*, 219 F.3d 353 (2d Cir. 1914), which *Renshaw* also relied on).

434. *In re* DePasquale, 225 B.R. 830 (1st Cir. B.A.P. 1998); *In re* Johnson, 218 B.R. 449 (8th Cir. B.A.P. 1998).

435. *See, e.g.*, *In re* Merchant, 958 F.2d 738 (6th Cir. 1992) (holding that an extension of credit amounts to a loan when "(1) the student was aware of the credit extension and acknowledges the money owed; (2) the amount owed was liquidated; and (3) the extended credit was defined as 'a sum of money due to a person.'" (citing *In re* Hill, 44 B.R. 645 (Bankr. D. Mass. 1984))).

436. *See, e.g.*, McKay v. Ingleson, 558 F.3d 888 (9th Cir. 2009); *In re* Renshaw, 222

failure to pay tuition and fee bills typically does not constitute a loan.[437] Finally, scholarships and other educational benefits conferred on the condition that the student perform some obligation after graduation may also be considered loans, if the terms of the agreement provide for their treatment as such should the student default.[438]

### *2. "Undue Hardship"*

Whichever paragraph of section 523(a)(8) exempts a student loan from discharge, the debtor may still be entitled to discharge the loan if repayment would "impose an undue hardship on the debtor and the debtor's dependents."[439] Nine circuits, including the Fourth Circuit,[440] apply the narrow three-prong test established in *Brunner v. New York State Higher Education Services Corporation*.[441] To satisfy the *Brunner* test, the debtor must "show that (1) she cannot maintain a minimal standard of living and repay the loans, (2) additional circumstances demonstrate that she will not be able to repay the loans for a substantial part of the repayment period, and (3) she attempted to repay the loans in good faith."[442] The debtor must establish all three prongs by a preponderance of the evidence.[443] Through hundreds of cases, courts have attempted to sharpen each prong of the *Brunner* test. This section cites only a sampling of those cases.

As the large number of reported decisions suggests, the *Brunner* inquiry is fact-intensive.[444] Although the *Brunner* test has a reputation for

F.3d 82 (2d Cir. 2000); *In re* Merchant, 958 F.2d 738 (6th Cir. 1992); *but see In re* Coole, 202 B.R. 518 (Bankr. D.N.M. 1996) (no "loan" unless money changes hands).

437. *See, e.g.*, *In re* Mehta, 262 B.R. 35 (D.N.J. 2001); *In re* Feyes, 228 B.R. 887 (Bankr. N.D. Ohio 1998).

438. *See, e.g.*, U.S. Dep't of Health & Human Servs v. Smith, 807 F.2d 122 (8th Cir. 1986); *In re* Mehlman, 268 B.R. 379 (Bankr. S.D.N.Y. 2001).

439. 11 U.S.C. § 523(a)(8).

440. *In re* Frushour, 443 F.3d 393 (4th Cir. 2005); *see also In Re* Oyler, 397 F.3d 382 (6th Cir. 2005); Educ. Credit Mgmt. Corp. v. Polleys, 356 F.3d 1302 (10th Cir. 2004); *In re* Gerhardt, 348 F.3d 89 (5th Cir. 2003); *In re* Cox, 338 F.3d 1238 (11th Cir. 2003); Goulet v. Educ. Credit Mgmt. Corp., 284 F.3d 773 (7th Cir. 3003); *In re* Brightful, 267 F.3d 324 (3d Cir. 2001); *In re* Rifinio, 245 F.3d 1083 (9th Cir. 2001); Matter of Robertson, 999 F.2d 1132 (7th Cir. 1993); *but see In re* Long, 332 F.3d 549 (8th Cir. 2003) (applying a "totality of the circumstances" test); *In re* Bronsdon, 435 B.R. 791 (B.A.P. 1st Cir. 2010).

441. 831 F.2d 395 (2d Cir. 1987).

442. *In re Frushour*, 443 F.3d at 398 (citing *Brunner*, 831 F.2d at 396).

443. *Frushour*, 443 F.3d at 400.

444. Educ. Credit Mgmt. Corp. v. Buchanan, 276 B.R. 744, 752 (N.D.W. Va. 2002); *In*

being harsh on debtors, many debtors have nevertheless discharged some or all of their student loans.[445] Unfortunately, many borrowers do not even file an adversary proceeding to discharge their student loans in bankruptcy.[446] The world of undue hardship litigation is one of uncertainty more than futility.[447] In this world, the skilled and experienced litigator can make a noticeable difference for her client.[448]

Three Fourth Circuit cases examine the *Brunner* test in Chapter 7 bankruptcy: *In re Frushour*, *In re Mosko*, and *In re Spence*. All three of these decisions rejected the debtor's attempt to discharge the debt. *Spence*, the most recent case, is illustrative of the tough sledding that faces student loan debtors seeking to discharge those debts. There, the Fourth Circuit held that the debtor—a woman in her late sixties with $160,000 of student loan debt who could not find a job paying more than her $26,000 annual salary—was not entitled to an undue hardship discharge.[449] The elderly Ms. Spence, the court reasoned, failed to meet prong two, because she had not shown an inability to obtain a higher paying job.[450] She had also failed to

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*re* Bedra, 405 B.R. 461, 463 (Bankr. N.D. Ohio 2008); *see also* Rafael I. Pardo & Michelle R. Lacey, *The Real Student-loan Scandal: Undue Hardship Discharge Litigation*, 83 AM. BANKR. L.J. 179, 190–91, 210 (2009) (suggesting that the high number of adjudicated proceedings in undue hardship cases is a product of doctrinal uncertainty).

445. *Cf.* Jason Iuliano, *An Empirical Assessment of Student Loan Discharges and the Undue Hardship Standard*, 86 AM. BANKR. L.J. 495, 507 (2013) (finding that twenty-five percent of debtors who sought student loan discharge in 2007 were granted full discharge, and another fourteen were granted partial discharge); Pardo & Lacey, *supra* note 444, at 212–13 (finding that more than half of 115 debtors who sought discharge of student loans in five-year period in the Western District of Washington had some or all of their student loans discharged).

446. Iuliano, *supra* note 445, at 523 (observing that "99.9 percent of bankrupt student loan debtors do not even try to discharge their student loans").

447. Pardo & Lacey, *supra* note 444, at 190–91, 210 (suggesting that high number of adjudicated proceedings in undue hardship cases is a product of doctrinal uncertainty); *but see* Iuliano, *supra* note 445, at 522 (finding that a borrower's medical hardship, employment status, and prior year income are useful predictors of whether borrower will succeed in discharging student loans).

448. Pardo & Lacey, *supra* note 444, at 219–21 (finding that experience level and identity of debtor's attorney to be statistically significant predictors of the percentage of the borrower's student loan debt discharged in bankruptcy); *but see* Iuliano, *supra* note 445, at 521–22 (finding no correlation between whether a borrower had an attorney and discharge of student loans). *Accord* Kevin J. Smith, *Should the "Undue Hardship" Standard for Discharging Student or Educational Loans Be Expanded?*, 18 BARRY L. REV. 333, 340 (2013) (arguing that discharge is underused).

449. *Spence*, 541 F.3d at 542–43.

450. *Id.* at 544.

make a good faith effort to repay her loans, because she stopped actively seeking a higher-paying job and because she did not consider loan consolidation or reduced payment plans.[451]

Substantively, the first prong of the *Brunner* test should be the easiest for the debtor to meet. Debtors are not required to live a life of asceticism and destitution.[452] The line, rather, "lies somewhere between poverty and mere difficulty."[453] Thus, debtors living above the poverty line may satisfy the first prong.[454]

Debtors may face three significant hurdles in establishing this prong. First, a debtor whose monthly income exceeds her monthly expenditures may have trouble establishing this prong. Indeed, one court has suggested that the debtor usually *must* show expenses in excess of income to satisfy this prong.[455] A debtor must strike the right balance: cut your expenses enough to be able to claim that your standard of living is "minimal," but not too much that the court deems only a partial discharge necessary, or worse, refuses any discharge at all.

Second, a creditor may challenge a debtor's expenses as unnecessary to meet a minimum standard of living. A "minimal standard of living" should include at least (1) clean shelter with climate-regulated heating and cooling, (2) basic utilities, including telephone, (3) food and personal hygiene products, (4) means of transportation, (5) life insurance and health insurance, or at least the ability to pay medical and dental expenses, and (6) "modest recreation."[456]

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451. *Id.* at 545.

452. *See In re* McLaney, 314 B.R. 228, 233 (Bankr. M.D. Ala. 2004) ("[The] minimal standard of living … standard does not condemn the debtors to a life of abject poverty."); *In re* Bene, 474 B.R. 56 (Bankr. W.D.N.Y. 2012).

453. *McLaney*, 314 B.R. at 234.

454. *In re* Alston, 297 B.R. 410, 415 (Bankr. E.D. Pa. 2003) ("It is well established that maintaining a minimal standard of living does not mean that the debtor has to live at a poverty level to repay her student loan."). While living at or below the poverty line itself may not guarantee that the debtor satisfies prong one, it is the rare debtor who is found not to qualify for undue hardship because of present sub-poverty income. *But see In re* Claxton, 140 B.R. 565 (Bankr. N.D. Okla. 1992).

455. *In re* Velarde, 2009 WL 2614688 (Bankr. E.D. Va. 2009) (holding that debtor who, by "cutting [expenses] to the bone," managed to eke out a monthly surplus did not satisfy *Brunner* prong one); *but see In re* Wallace, 443 B.R. 781 (Bankr. S.D. Ohio 2010) (finding that debtor's whose estimates of monthly income that exceeded expenses satisfied prong one with respect to monthly loan payments in excess of $20 per month, where debtor omitted some necessities from the monthly budget presented to the court).

456. *In re* Crawley, 460 B.R. 421, 436 (Bankr. E.D. Pa. 2011) (citing *In re* Ivory, 269

Decisions run the gamut of these items, some finding claimed expenditures reasonable and others finding them unreasonable. Creditors have challenged debtors' claimed housing expenses,[457] some arguing that the debtor should find housing in a less expensive neighborhood.[458] When creditors challenge food expenses, courts usually find debtors' claims reasonable,[459] but not always,[460] especially if unless the debtor dines out frequently.[461] Additionally, almost all courts regard cell phone bills as reasonable, especially if the debtor does not use landline telephone.[462]

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

457. *Compare In re* Wallace, 443 B.R. 781, 788 (Bankr. S.D. Ohio 2010) (finding $300 monthly rent paid to debtor's father reasonable), *and In re* Paul, 337 B.R. 730 (Bankr. D. Mass. 2006) (finding $1,000 rent reasonable for three-bedroom apartment occupied by debtor, her parents (who paid for utilities), her 16-year-old sister, and her three children), *with In re* Clark, 341 B.R. 238 (Bankr. N.D. Ill. 2006) (finding $1,600 monthly rental of single family home for family of five excessive).

458. *Compare In re* Gharavi, 335 B.R. 492, 500 (Bankr. D. Mass. 2006) (finding $1,400 monthly rent not unreasonable for debtor living with dependent; debtor "wants to live in a safe neighborhood"), *with In re* Chappelle, 328 B.R. 565, 573 (Bankr. C.D. Cal. 2005) (holding unreasonable debtor's $807.50 monthly contribution toward rent for studio apartment in "high-rent district" she shared with her boyfriend).

459. *See, e.g.*, *In re* Jorgensen, 479 B.R. 79, 87 (B.A.P. 9th Cir. 2012) (allowing $625 per month for food based on debtor's health problems); *In re* Wallace, 443 B.R. 781, 786 n.3 (Bankr. S.D. Ohio 2010) (suggesting that $200 per month on food is "clearly inadequate" to support a minimal standard of living and describing $300 as "more reasonable"); *In re* Rhodes, 418 B.R. 27, 35 (Bankr. D. Conn. 2009) ("[Debtor's] weekly food budget, amounting to $53.48, is pitiful."); *In re* McLaney, 375 B.R. 666, 674 (M.D. Ala. 2007) (declaring that a $348 monthly food budget amounts to "an almost impossible $1.30 per meal" for a family of three); *In re* Lebovitis, 223 B.R. 265, 272 (Bankr. E.D.N.Y. 1998) ($1,600 monthly to feed family of nine not excessive).

460. *See, e.g.*, *In re* Bott, 324 B.R. 771, 777 (Bankr. E.D. Mo. 2005) (finding $600 on food for debtor with two dependent children excessive and suggesting $400 as a reasonable figure); *see also In re* Clark, 341 B.R. 238, 250 (Bankr. N.D. Ill. 2006) (finding $905 monthly expenses for debtor, husband, and three children excessive).

461. *See, e.g.*, *In re* Gibson, 428 B.R. 385, 390 (Bankr. W.D. Mich. 2010) ("Eating out is a luxury, in the court's view."); Cockels v. Mae, 414 B.R. 149, 156 (E.D. Mich. 2009) (concluding that the Bankruptcy Court did not err when it found Debtor Cockels' food expenses to be excessive and could be reduced by eating out less); *see also* Educ. Credit Mgmt. Corp. v. Young, 376 B.R. 795, 800 (E.D. Tenn. 2007) (finding $650 monthly food expenditure for debtor and 12-year-old son unreasonable given the debtor's "penchant for eating out"); *but see In re* Wallace, 443 B.R. 781, 795 (Bankr. S.D. Ohio 2010) (allowing discharge where debtor listed $100 monthly expenditure for "Food (eating out)").

462. *See, e.g.*, *In re* Nixon, 453 B.R. 311, 329 (Bankr. S.D. Ohio 2011) (finding $67 for cell phones and $68 for landline telephones reasonable); *In re* Brooks, 406 B.R. 382, 390 (Bankr. D. Minn. 2009) ("A cellular telephone is not a luxury when it is a debtor's only phone . . . ."); *In re* Pollard, 306 B.R. 637, 646 (Bankr. D. Minn., 2004) (stating that the use of a cellular phone is not a luxury)*; but see In re* Mosko, 515 F.3d 319, 325 (4th Cir. 2008)

Courts also sensibly accommodate debtors' responsible transportation expenses, including purchases of used automobiles.[463]

Recreational and discretionary expenditures are a fertile source of litigation. While almost all courts agree that "people are not robots, and require at least minimal opportunity for recreation and relaxation,"[464] they do not agree on what types or amounts of recreational expenses should be permitted.[465] Debtors who can tie expenses typically regarded as recreational to a work-related purpose tend to fare well.[466] Courts have typically regarded items like health club memberships[467] and premium

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(finding monthly expenses of "$75 for internet, $80 for cell phones, $60 for satellite television, $68 for a YMCA membership, and an undisclosed amount for cigarettes" to be "generally unnecessary to maintain a minimal standard of living").

463. *See In re* Marcotte, 455 B.R. 460, 472 (Bankr. D.S.C. 2011) (finding $3,800 purchase of used Jeep Wrangler reasonable); *In re* Williams, 301 B.R. 62, 73 (Bankr. N.D. Cal. 2003) (finding married debtors reasonably required two cars, as sometimes they were unable to commute to work together). Debtors who splurge on transportation tend to fare poorly. *See, e.g.*, *In re* Armstrong, 394 B.R. 43, 54 (Bankr. M.D. Pa. 2008) (finding purchase of 2004 Pontiac Montana for $36,000 excessive).

464. *In re* Woody, 494 F.3d 939, 951 (10th Cir. 2007) (finding $17 monthly for "Cable/ Satellite/Internet" and $95 for "Recreation/Entertainment" were reasonably necessary to minimal standard of living).

465. *Compare In re* Mosko, 515 F.3d 319, 325 (4th Cir. 2008) ("Such items [as internet, cell phones, satellite TV, and a YMCA membership] are generally unnecessary to maintain a minimum standard of living."), *and In re* Bott, 324 B.R. 771, 777 (Bankr. E.D. Mo. 2005) ("Plaintiff should not be allowed to have such luxuries [as a $40 per month cable TV subscription] if she cannot afford to make payments to ECMC."), *with In re* Frushour, 433 F.3d 393, 400–01 (4th Cir. 2005) ("In short, the mere fact of Frushour's Internet and cable expenses would not disqualify her from an undue hardship discharge."); *In re* Nixon, 453 B.R. 311, 329 (Bankr. S.D. Ohio 2011) (finding expenses of $126 internet, $67 for cell phones, and $68 for landline telephones reasonable, "because they permit the Plaintiffs to have a source of entertainment and allow Elisabeth to apply for employment online"); *In re* Innes, 284 B.R. 496, 505 (Bankr. D. Kan. 2002) (allowing discharge to debtors who used much of one year's tax refund on "a single frugal summer vacation").

466. *See, e.g.*, *In re* Jorgensen, 2012 WL 171599, at *2 (Bankr. D. Haw. Jan. 20, 2012) (finding debtor's $75 monthly cellular and $50 monthly high speed internet bills reasonable, because "[r]eady access to online data at all times, at work, at home, and while traveling, is indispensable to [her] work as a professor").

467. *See, e.g.*, *In re* Weldon, 2008 WL 4527654, at *3 (W.D. Wash. 2008) (stating that debtor could make significant monthly payments if she ceased health club payments and other expenditures); *In re* Kitterman, 349 B.R. 775, 778 (Bankr. W.D. Ky. 2006) (suggesting debtor's health club membership was not a necessary expense); *In re* Pincus, 280 B.R. 303 (Bankr. S.D.N.Y. 2002) (stating a gym membership was not necessary when debtor's employer provided a gym free of charge)*; but see In re* Gerhardt, 276 B.R. 424, 429 (Bankr. E.D. La. 2002), rev'd on other grounds, 348 F.3d 89 (5th Cir. 2003) (stating that the health club membership was necessary to help debtor alleviate back and arm pain).

cable television subscriptions[468] as unnecessary. Courts are split on whether cigarette expenses may be counted toward a minimal standard of living, though *Mosko* suggests that they are not.[469] Litigants have also disputed charitable expenditures,[470] contributions to retirement accounts[471] and life insurance policies,[472] and expenses of dependent children.[473]

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468. *See, e.g.*, *In re* Russotto, 370 B.R. 853, 857 (Bankr. S.D. Fla. 2007) (stating that Debtor's $130 cable bill was not a reasonable expense); *In re* Pobiner, 309 B.R. 405, 417 (Bankr. E.D.N.Y. 2004) (deeming "premium cable channels" a "luxur[y]"); *but see In re* Jones, 495 B.R. 674, 686–87 (Bankr. E.D. Pa. 2013) (stating that a $293 per month for cable and phone bill not excessive).

469. *See, e.g.*, *In re* Brooks, 406 B.R. 382, 386 (Bankr. D. Minn 2009) (deciding that cigarettes are an unreasonable luxury expense); *In re* Campton, 405 B.R. 887, 891 (Bankr. D. Ohio 2009) ("[C]igarettes are not expenditures normally necessary to maintain a minimum standard of living . . . ."); *see also In re* Mosko, 515 F.3d 319, 325 (4th Cir. 2008) (finding lack of good faith based on certain expenditures, including "an undisclosed amount for cigarettes," that "are generally unnecessary to maintain a minimum standard of living"); *but see In re* Gharavi, 335 B.R. 492, 499–500 (Bankr. D. Mass. 2006) (finding $175 monthly cigarette expense reasonable and cataloguing cases).

470. *Compare* Educ. Credit Mgmt. Corp. v. Rhodes, 464 B.R. 918, 924 (W.D. Wash. 2012) ("Without concluding that all religious or charitable contributions are *per se* unreasonable under § 523(a)(8), this Court grants far less deference to such voluntary contributions than to a debtor's contract-based obligations to his creditors."), *In re* Bush, 450 B.R. 235, 244 (Bankr. M.D. Ga. 2011) (stating that a $320 monthly charitable contribution is excessive), *and In re* Simone, 375 B.R. 481, 504 (Bankr. C.D. Ill. 2007) (stating that no discharge for debtor who made over $7,000 in charitable donations the previous year), *with* Cumberworth v. U.S. Dep't of Educ., 2005 WL 1387981, at *4 (Bankr. N.D. Iowa June 7, 2005) (noting that Debtor's charitable spending is discretionary but not unreasonable). Most courts appear willing to treat tithes as reasonable in certain circumstances. *See, e.g.*, *In re* Larson, 426 B.R. 782, 789–90 (Bankr. N.D. Ill. 2010) (stating that a $80 monthly tithe is reasonable); *In re* McLaney, 375 B.R. 666, 681 (M.D. Ala. 2007) (stating that a $220 monthly tithe is reasonable and there was no Congressional intent to label all tithes as unreasonable); *In re* Durrani, 311 B.R. 496, 503–04 (Bankr. N.D. Ill. 2004) (deciding that a $226 monthly tithe is a reasonable expense); *see also In re* Lebovitis, 223 B.R. 265, 273 (Bankr. E.D.N.Y. 1998) (holding that the Religions Liberty and Charitable Donation Protection Act of 1997 requires treating tithes of up to 15% of gross income as reasonable); *but see In re* Fullbright, 319 B.R. 650, 652 (Bankr. D. Mont. 2005) (deciding a discharge was not appropriate and deeming a tithe of $430 per month discretionary), *and In re* Lynn, 168 B.R. 693, 700 (Bankr. D. Ariz. 1994) (deciding a discharge was not appropriate and stating the tithe was unreasonable because her church gave her the option of ceasing donations in certain circumstances).

471. *See, e.g.*, *In re* Craig, 579 F.3d 1040, 1045 (9th Cir. 2009) ("[T]he determination of whether retirement contributions are a 'reasonably necessary' expense is to be made using 'a case-by-case approach.'").

472. *See, e.g.*, *In re* Weldon, 2008 WL 4527654, at *3 (W.D. Wash. 2008) (criticizing expenditure on life insurance premium as excessive).

473. *See In re* Gill, 326 B.R. 611, 631–34 (Bankr. E.D. Va. 2005) (discussing different approaches courts have taken regarding expenditures on adult children).

Frugality in some areas may excuse borderline expenses in others,[474] so a wise debtor will call the court's attention to the deepest cuts she has made in her budget. Finally, it should go without saying that debtors must actually incur or reasonably anticipate incurring the expenses they claim.[475]

A thorny problem that has divided the courts is whether the availability of income-contingent repayment affects the debtor's ability to satisfy this prong of the Brunner test. Some courts have held that a debtor who has enrolled in ICR or who may be eligible to enroll in it, and who owes or would owe monthly payments of $0 under the plan, is not entitled to discharge because the repayment obligation does not affect the debtor's ability to maintain a minimal standard of living.[476] One circuit judge has opined that all low-income student loan debtors should be required to enter ICRP rather than file for bankruptcy.[477] Other courts, reasoning that a debtor with a zero repayment is not actually being "forced to repay the student loan," have rejected this approach.[478] Still other courts apply a totality of the circumstances approach, considering the availability of income dependent repayment plans alongside other relevant facts.[479]

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474. *See, e.g.*, *In re* Lewis, 276 B.R. 912, 917 (Bankr. C.D. Ill. 2002) (finding that debtor satisfied prong one despite car payment "at the high end of the range of reasonable" in light of her "otherwise frugal lifestyle and budget shortfalls").

475. *See, e.g.*, Educ. Credit Mgmt. Corp. v. Jesperson, 571 F.3d 775, 780 (8th Cir. 2009) (noting that the bankruptcy court erred in imputing $1,000 fair market rent to debtor whose brother allowed him to live at his apartment rent free); *In re* Clark, 341 B.R. 238, 251 (Bankr. N.D. Ill. 2006) (noting that home maintenance expenditure of $260 per month for debtor who does not own home).

476. *In re* Greene, 484 B.R. 98, 104 (Bankr. E.D. Va. 2012); *In re* Geyer, 344 B.R. 129, 132–33 (Bankr. S.D. Cal. 2006).

477. Krieger v. Educ. Credit Mgmt. Corp., 713 F.3d 882, 885 (7th Cir., 2013) (Manion, J., concurring).

478. *In re* Durrani, 311 B.R. 496, 505 (Bankr. N.D. Ill. 2004) ("The question framed by *Brunner* in this first prong is whether Durrani can maintain a minimal standard of living if she is required *to repay this loan,* not whether she has any surplus in her budget available for a monthly payment."); *In re* Coatney, 345 B.R. 905 (Bankr. C.D. Ill. 2006); *In re* Booth, 410 B.R. 672 (Bankr. E.D. Wash. 2009); *see also* Terrence L. Michael & Janie M. Phelps, *Judges?!—We Don't Need No Stinking Judges!!!: The Discharge of Student Loans in Bankruptcy Cases and the Income Contingent Repayment Plan*, 38 TEX. TECH L. REV. 73, 74 (2005) ("Government agencies argue that, due to the existence of programs such as the ICRP, the nondischarge of a student loan can never constitute an undue hardship.").

479. *In re* Bene, 474 B.R. 56, 60 (Bankr. W.D.N.Y. 2012) (determining that the availability of the Ford Program is just one of a "'totality of factors' that the Court must apply in a § 523(a)(8) analysis"); *see also* Krieger v. Educ. Credit Mgmt. Corp., 713 F.3d 882, 884 (holding the debtors need not agree to a repayment plan as a matter of law, and adding that "[w]hat remains is a predominantly factual understanding").

The second prong of the *Brunner* test—that "additional circumstances exist indicating that [the debtor's] state of affairs is likely to persist for a significant portion of the repayment period"[480]—is probably the most difficult for Fourth Circuit debtors to meet. *Frushour* describes this prong as "the heart of the *Brunner* test" because it "reflects the congressional imperative that the debtor's hardship must be more than the normal hardship that accompanies any bankruptcy."[481] This "demanding requirement … necessitates that a certainty of hopelessness exists that the debtor will be able to repay the student loans," and is satisfied only in "rare circumstances."[482] Such rare circumstances might include, but are not limited to, "'illness, disability, a lack of useable job skills, or the existence of a large number of dependents.'"[483]

In *Frushour*, the Fourth Circuit, over a vigorous dissent from Judge Hamilton, reversed the Bankruptcy Court's decision discharging the student loan debt of a forty-something single mother who earned around $10,000 per year.[484] The debtor regularly worked from home, marketing her services as an interior designer and decorative painter, in order to avoid paying childcare costs for her seven-year-old son.[485] The court discounted the debtor's current situation, insisting that the inquiry under *Brunner* prong two is prospective.[486] The debtor had worked in higher-paying jobs in the past, and could not show that she would be unable to obtain a higher paying job in the near future based on prior inability to obtain such a job, because she was not actively seeking higher-paying employment at the time.[487] "[G]iven her college education, real estate license, and restaurant management experience," the court concluded that she had not shown a

480. Brunner v. New York State Higher Educ. Servs. Corp., 831 F.2d, 395, 396 (2d Cir. 1987).

481. *In re* Frushour, 433 F.3d 393, 401 (4th Cir. 2005) (citing *In re* Rifino, 245 F.3d 1083, 1087 (9th Cir. 2001)).

482. *Id.* (internal quotations and citations omitted)*; but see In re* Carnduff, 367 B.R. 120, 128 (9th Cir. B.A.P. 2007) (declining to adopt "certainty of hopelessness" standard, because debtor need only prove inability to repay in the future by preponderance of evidence).

483. *Id.* (quoting *In re* Oyler, 397 F.3d 382, 386 (6th Cir. 2005)).

484. *Id.* Both the Pardo and Lacey and Iuliano studies found existence of a medical condition to be a statistically significant predictor of discharge. Pardo & Lacey, *supra* note 444, at 216–18; Iuliano, *supra* note 445, at 509–10.

485. *Frushour*, 433 F.3d at 396–97.

486. *Id.* at 401.

487. *Id.*

likelihood "that her present circumstances will extend for the rest of her repayment period or that she will not be able to pay off her loans at some future date."[488]

*Frushour* raises the possibility that a debtor's failure to maximize income may defeat her attempts to establish the second prong of the *Brunner* test, a position that courts in other circuits have taken in refusing to discharge debts of ministers,[489] public defenders,[490] and musicians.[491] Debtors in public service positions are well-advised to emphasize the importance of health and other benefits and to point out that such benefits may be unavailable in private, for-profit-sector jobs,[492] and to add any other facts which might influence a reasonable person to avoid switching jobs, for example proximity to the debtor's current residence. However, they should avoid sharing altruistic motives for working in public or private non-profit sectors. While her disposition toward service may win the debtor admiration from the judge,[493] it may not earn her a discharge of her student loans.[494]

Many claims of undue hardship involve debtors with one or more medical conditions. A debtor who bases a hardship claim on medical or mental-health conditions must tie her condition to her inability to obtain and maintain a particular level of employment, and must show that the condition will persist for a significant portion of the repayment period.[495]

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488. *In re* Frushour, 433 F.3d 393, 401 (4th Cir. 2005).

489. *See In re* Oyler, 397 F.3d 382, 386 (6th Cir. 2005) ("The Bankruptcy Court erred by not considering that Oyler's decision not to maximize his earnings, though commendable, was voluntarily made after he also voluntarily incurred the debt that he now wishes to discharge.").

490. *See In re* Bender, 338 B.R. 62 (Bankr. W.D. Mo. 2006); *In re* Evans-Lambert, 2008 WL 1734123 (Bankr. N.D. Ga. Mar. 25, 2008).

491. *See In re* Gerhardt, 348 F.3d 89 (5th Cir. 2003).

492. *See In re* Avant, 2006 WL 3782168, at *1 (Bankr. W.D. Mo. Dec. 21, 2006) ("[The Debtor] further testified that she cannot obtain insurance on her own or through another employer, so she is stuck at her current job, which offers little opportunity for advancement.").

493. *See Bender*, 338 B.R. at 70 ("The Debtor testified that he enjoys her current position because it allows him to give something back to society. While that is a commendable sentiment, he also gives back by repaying her student loans.").

494. *See id.* (denying an undue hardship discharge).

495. *See In re* Tirch, 409 F.3d 677, 681–682 (6th Cir. 2005) (explaining that because Tirch did not provide evidence that her problems would persist for a significant portion of the loan repayment period, she did not satisfy *Brunner*'s second prong); *see also In re* Mosley, 494 F.3d 1320, 1325 (11th Cir. 2007) ("[T]he crucial requirement is that the debtor

The borrower need not produce a medical professional's expert testimony to obtain an undue hardship discharge.[496] Indeed, a debtor's credible testimony alone should suffice when the creditor does not contest it.[497]

*Brunner*'s "good faith" prong is also an imposing hurdle to debtors in the Fourth Circuit. "Good faith efforts" refers to the debtor's "'efforts to obtain employment, maximize income, and minimize expenses.'"[498] It also requires that the debtor's hardship be caused by factors beyond her control.[499] Courts have noted overlap between the second and third prongs, in that both involve consideration, directly or indirectly, of whether the debtor has maximized her income.[500] The expense-minimization inquiry also frequently overlaps with prong one's analysis of whether a debtor's present expenses are necessary to a minimum standard of living.

Courts may have made the good-faith prong far stiffer than the *Brunner* court intended it to be. In *Brunner*, the debtor filed for bankruptcy seven months after leaving school and within a month of when her first payment came due.[501] Construing the good-faith prerequisite to cover only the situation in which the debtor seeks to discharge her student loans as soon as she is obliged to repay them, without even the slightest effort toward repayment, better accounts for the state of the law that the *Brunner* court found. For then, student loans could be discharged like any other debt

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show how his medical conditions prevent him from working. . . ."); *In re* Davis, 373 B.R. 241 (W.D.N.Y. 2007) (rejecting undue hardship claim based on debtor's alleged depression where debtor admitted that her ailment "never caused her to lose a job or miss an interview or employment opportunity"); *In re* Congdon, 365 B.R. 433 (Bankr. D. Vt. 2007) ("In this Court's view, the fatal gap in the Plaintiff's case was [her] failure to present any corroborating evidence that she has an impairment (or a cluster of impairments) that are likely to persist well into the future.").

496. *See In re* Barrett, 487 F.3d 353 (6th Cir. 2007); *In re* Mason, 464 F.3d 878 (8th Cir. 2006) (noting testimony of debtor and his mother sufficient to establish existence of learning disability where creditor did not dispute its existence); *but see In re* Davis, 373 B.R. 241 (W.D.N.Y. 2007) (noting lack of corroboration of debtor's testimony about her depression in rejecting undue hardship claim).

497. *See, e.g.*, *In re* Alliger, 78 B.R. 96 (Bankr. E.D. Pa. 1987).

498. *In re* Mosko, 515 F.3d 319, 324 (4th Cir. 2008) (quoting O'Hearn v. Educ. Credit Management Corp., 339 F.3d 559, 564 (7th Cir. 2003)); *accord* Hedlund v. Educational Resources Institute, Inc., 718 F.3d 848, 852 (9th Cir. 2013).

499. *See In re* Frushour, 433 F.3d 393, 402 (4th Cir. 2005).

500. *See In re* Myers, 2010 WL 890444, at *4 (Bankr. E.D.N.C. 2010) ("This component of the third Brunner prong frequently overlaps with the analysis of the second prong, under which the court must determine whether the debtor's state of affairs is likely to persist.").

501. *See In re* Brunner, 46 B.R. 752, 758 (Bankr. S.D.N.Y. 1985).

five years after becoming due.[502] It would also parallel more closely the meaning of the term "good faith" in other legal contexts.[503] But, at least in the Fourth Circuit, and at least for now, these arguments will find no quarter but in the rarefied setting of an *en banc* Court of Appeals.

A debtor's failure to make student loan payments while she is able will almost certainly prove fatal to her undue-hardship claim.[504] In *Mosko*, for example, the court refused to allow an undue hardship discharge for a couple with a young son, because the debtors had made no payments during a year in which they had an adjusted gross income of over $64,000 and during which time their net monthly income exceeded reasonable expenses by $480.[505]

Courts may find that failure to seek the best paying job possible defeats the debtor on this prong as well as the second. Courts have described the quantum of effort borrowers must satisfy as that of "strenuous"[506] and "best efforts."[507] A debtor who desires discharge should extend her job search beyond her field of preference[508] even beyond the field for which her education and training prepare her.[509] A debtor's failure

502. *See id.* at 753–56; *see also id.* at 755 ("The propriety of a requirement of good faith is further emphasized by the stated purpose for § 523(a)(8): to forestall students, who frequently have a large excess of liabilities over assets solely because of their student loans, from abusing the bankruptcy system to shed these loans.").

503. *See* RESTATEMENT (SECOND) OF CONTRACTS § 205 & cmts. a–e (1981) (discussing covenant of good faith and fair dealing in the context of contract law). What courts have required to satisfy *Brunner's* "good faith" prong is a level of performance that looks more like the duty of "best efforts" implied in exclusive contracts. *Cf.* U.C.C § 2-306 (2002).

504. *See In re* Mosko, 515 F.3d 319, 326 (4th Cir. 2008) ("[T]he payments the Moskos made on their student loans are insufficient to demonstrate good faith because they failed to make payments on their student loans during a time period when their income substantially exceeded their necessary expenses."); *see also In re* Fields, 286 Fed. Appx. 246, 250 (6th Cir. 2007) (rejecting undue hardship claim because debtor's failure to make payments did not result from factors beyond her control); *In re* McNemar, 352 B.R. 621, 624 (Bankr. N.D. W. Va. 2006) (rejecting undue hardship claim because of debtor's voluntary cessation of payments on loan).

505. *See Mosko*, 515 F.3d at 326.

506. *In re* Farrish, 272 B.R. 456, 462 (Bankr. S.D. Miss. 2001).

507. *In re* Flores, 282 B.R. 847, 854 (Bankr. N.D. Ohio 2002).

508. *In re* Lohr, 252 B.R. 84, 88 (Bankr. E.D. Va. 2000) ("Good faith attempts to maximize income require the debtor to take advantage of opportunities for work when it has been available and diligently look for work, whether or not in the debtor's chosen field, when it has not been available.").

509. *In re* Pobiner, 309 B.R. 405, 421 (Bankr. E.D.N.Y. 2004) ("[Pobiner] not only failed to actively pursue jobs in the legal field other than as a licensed attorney, but also failed to actively pursue jobs in any other field.").

to tap non-employment sources of income may also prevent her discharge.[510]

All three Fourth Circuit cases emphasize that the debtor's consideration, and perhaps even pursuit, of consolidation and reduced-payment plans are a required part of good faith efforts.[511] The court in *Frushour* explained that "[t]he debtor's effort to seek out loan consolidation options that make the debt less onerous is an important component of the good-faith inquiry" because "it illustrates that the debtor takes her loan obligations seriously, and is doing her utmost to repay them despite her unfortunate circumstances."[512]

The debtor can take some minor solace in lower courts' rejection of a per se rule requiring a debtor to pursue alternative repayment plans.[513] At least one other circuit has rejected requiring participation in an income-contingent repayment plan as extra-textual and contrary to statutory purpose.[514] Indeed, an income-based repayment plan that allows debt to pile

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510. *See, e.g. In re* Thoms, 257 B.R. 144 (Bankr. S.D.N.Y. 2001) (denying undue hardship discharge where debtor failed to seek child support payments from her child's father).

511. *In re* Spence, 541 F.3d 538, 545 ("Ms. Spence did not fully explore the possibility of loan consolidation programs that offer reduced payments based upon the debtor's limited income."); *In re* Mosko, 515 F.3d 319, 326 (4th Cir. 2008) ("Finally, the Moskos failed to adequately pursue loan consolidation options."); *In re* Frushour, 433 F.3d 393, 404 (4th Cir. 2005) ("Frushour. . . refused to consider loan consolidation programs that would have required from her a monthly payment of near zero based on her current income."). Lower courts in the Fourth Circuit have found that debtors who failed to pursue income contingent repayment plans also fell short of satisfying *Brunner* prong one, when the debtor could make payments required under such a plan while maintaining a minimal standard of living. *See, e.g.*, *In re* Boston, 2011 WL 4712078 (Bankr. W.D.N.C. Oct. 5, 2011); *In re* Straub, 435 B.R. 312 (Bankr. D.S.C. 2010).

512. *Frushour*, 433 F.3d at 402.

513. *See* Hooker v. Educ. Credit Management Corp., 368 B.R. 502, 505 (W.D. Va. 2007) (holding that debtor's failure to investigate ICRP did not preclude finding of good faith and reversing Bankruptcy Court order denying undue hardship discharge); *In re* Brown, 2007 WL 1747135, at *5 (Bankr. N.D. W. Va. June 15, 2007) ("[T]he Debtor's failure to seek out loan repayment options is not solely dispositive. . . . Rather, it is only one component of a broader examination of a debtor's good faith efforts.").

514. As the Sixth Circuit explained in one case:

> Congress recently enacted [the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005,] the most sweeping reform of bankruptcy law since the enactment of the Bankruptcy Code in 1978. Yet Congress left § 523(a)(8)'s "undue hardship" language intact. Had Congress intended participation in the ICRP-implemented in 1994-to effectively repeal discharge under § 523(a)(8), it could have done so. In addition, requiring enrollment in the ICRP runs counter to the Bankruptcy Code's aim in providing debtors a 'fresh start.

up while the debtor makes minimal payments seem contrary to the entire concept of bankruptcy. It is no answer that income-based repayment schemes provide for discharge of the debt at the end of a fixed period, which is twenty-five years for ICRPs. The cancelled debt is treated as taxable income and the borrower is essentially forced to "trad[e] one non-dischargeable debt for another."[515]

Whether or not *Frushour*, *Mosko*, and *Spence* were correctly decided, they represent settled Fourth Circuit precedent. Thus a debtor in bankruptcy in the Fourth Circuit who has pursued repayment and consolidation strategies stands a significantly better chance of obtaining an undue hardship discharge.[516] A borrower who has not should be prepared to offer a good reason for her failure.[517]

## *VI. It Could be Worse*

Although we have developed the student borrower's plight at length, we are aware that other debtors encounter serious collection techniques. To begin, some judgment creditors may exploit collection techniques against consumer debtors to create the equivalent of debt imprisonment.[518]

A delinquent family-support debtor risks coercive contempt, potentially leading to confinement. In 2011, the United States Supreme Court approved allegedly indigent family-support debtors' coercive contempt confinement without appointed lawyers.[519]

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*In re* Barrett, 487 F.3d 353, 364 (6th Cir. 2007) (internal citations, quotations, and footnotes omitted); *see also* Hedlund v. Educ. Res. Inst., Inc., 718 F.3d 848 (9th Cir. 2013) (holding that partial discharge was not clearly erroneous, even though debtor failed to pursue ICRP); *In re* Roth, 490 B.R. 908, 920–21 (B.A.P. 9th Cir. 2013) (concluding that a debtor's failure to pursue income-based repayment should not be counted against her, given her advanced age, poor health, and limited employment prospects).

515. *In re* Barrett, 487 F.3d 353, 364 (6th Cir. 2007); Schrag, *supra* note 123, at 415–16 (2013).

516. *See, e.g.*, *In re* Dykstra, 362 B.R. 221 (Bankr. D. Md. 2007).

517. *Cf. In re* Robinson, 416 B.R. 275 (Bankr. E.D. Va. 2009) (noting that the debtor in Chapter 13 case failed to show good faith in refusing to consider consolidation or repayment plans based only on her desire to avoid having debt reflected in her credit report, which she alleged would prevent her from obtaining affordable and stable rental housing).

518. Lea Shepard, *Creditors' Contempt*, 2011 BYU L. REV. 1509; Note, *Body Attachment and Body Execution: Forgotten but Not Gone*, 17 WILLIAM & MARY L.REV. 543 (1976).

519. Turner v. Rogers, 131 S.Ct. 2507 (2011).

Dealing with a voluntarily unemployed child-support debtor, California's highest court rejected arguments that contempt was imprisonment for a civil debt and involuntary servitude.[520] Family support, the court said, is not a debt for purposes of the constitutional provision that forbids debt imprisonment.[521] Nor may a debtor who can choose his employer claim involuntary servitude.[522] In effect, the court told the voluntarily unemployed debtor, who according to the trial judge could "flip burgers," to get a job or go to jail.[523] The *Brunner* undue-hardship test to discharge student loans, in effect, embodies the "get-a-job" half of the *Moss* court's ruling.[524] Like a student borrower, a delinquent family-support debtor is subject to pre-judgment license suspension, offset, and garnishment.[525] Nor may a child-support debtor discharge his obligation in bankruptcy.[526]

Moreover, a health-professional who defaults on a National Health Service Corps loan may be charged with "liquidated" damages.[527] There is no statute of limitations on the government's filing suit or collecting a judgment. The government may recover the amount loaned, plus the number of uncompleted months times $7500 and interest at the maximum legal rate.[528] A borrower's bankruptcy discharge will be excruciatingly difficult; none at all for seven years from when repayment is required and then only if the bankruptcy court finds that not discharging the defendant's debt would be "unconscionable."[529]

The reasons that family support and Health Services Corps loans are difficult to avoid don't apply to student loans. A custodial parent may encounter brutal need. A non-custodial parent's duty to support his child is a "fundamental parental obligation" based on "fundamental societal norms and fair dealing, and [a debtor who doesn't pay] necessarily intentionally does an act which prejudices the rights of his children."[530] The Health

520. Moss v. Superior Court, 950 P.2d 59, 76 (Cal. 1998).
521. *Id.*
522. *Id.* at 72.
523. *Id.* at 63.
524. *See supra* notes 439–517 and accompanying text.
525. RENDLEMAN, EJL-V 3D, supra note 311.
526. 11 U.S.C. 523(a)(5),(15). *See also* 42 U.S.C. § 656(b).
527. 42 U.S.C. § 254o(b)(1)(A).
528. 42 U.S.C. § 254o(c)(1).
529. 42 U.S.C. § 254o(d)(3)(a).
530. *Moss*, 950 P.2d at 76.

Services Corps sends doctors to medically underserved communities where the population's health needs may be unmet.

## *VII. Conclusion*

Above, we have been careful to articulate the student-loan collection scheme and to reduce our evaluation of the programs. We will turn to the latter in our closing remarks.

Our first observation about collection of student loans is that complexity breeds confusion. Divided government and compromises have created almost geologic layers of programs. The programs duplicate and overlap when they aren't apparently contradictory. The complexity spawns management that undermines efficiency and public trust.

Confusion also hurts borrowers, who struggle to understand the complex student loan system. How else to explain why so many borrowers fall behind on payments and ultimately default when the consequences of default are so severe and the tools for avoiding delinquency and default (e.g. deferments, forbearance, income-dependent and extended repayment plans) are so many? Or why so few debtors in bankruptcy seek discharge of their student loans? Borrowers who don't understand the system must make binding decisions often behind a veil of ignorance.

We find it hard to know whether the whole system actually works or is dysfunctional. In addition to harboring four student-loan borrowers, the senior author chaired the AAUP Government Relations Committee for four years and served twice on the AALS Government Relations Committee. He teaches in law school classrooms, which he shares with well over a million dollars in student debt. The junior author is repaying his own student loans delete-of his own. Yet, even after this lengthy and technical project, we aren't sure that we understand the whole system.

Congress should view the educational finance system as a whole, the colleges' and states' contributions, students' and parents' contributions, loans and grants. It should consolidate and rebalance grant and loan programs with similar missions. Consolidation should reduce the duplication and complexity that make it harder to assist the supposed beneficiaries.

Abolishing the FFEL program, so that all Stafford and PLUS loans are made by the government under the auspices of the Direct loan program, was a step in the right direction. Just as it removed guaranty agencies and private lenders from the student loan system when it abolished the FFEL program, Congress should also consider reforming the Perkins loan program to take institutions of higher education out of the federally guaranteed lending business. Going further, Congress should harmonize repayment provisions for all federally guaranteed loans. For example, a borrower should be able to choose one repayment plan for all of his loans, and obtain cancellation for all concurrently issued loans at the same time.

In the end, legislative reform might create a single student loan with a fixed interest rate based on the government's cost of borrowing and a single income-based repayment plan. The agency ought to divert delinquent borrowers into IBR and other income-dependent plans. In 2013, the DOE made a start by emailing borrowers about IBR. Also, a forgiven or discharged student loan should not be taxable income. Finally, dispensing with private debt collectors would also improve the student-loan program.

Eliminating the confusion and complexity will eliminate many traps for the unwary. If Congress legislates better, the executive will execute better. But confusion and complexity are not the biggest problems.

The senior author worked his way through college and law school. Thus one lower-income student and law student became a lawyer, indeed a professor. That "social contract" with state appropriations, need-based scholarships, and low tuition didn't exist for the junior author. Educational expenses outstripped inflation. College costs are up, while the Great Recession pushed state support and family incomes down.

The original goal of access to higher education has been eroded. Accomplishing the goal of access would require adding increased Pell Grants for low-income students to loan programs. Also, the high tuition in the United States compares unfavorably with low or no tuition in other countries.[531]

Students' future earning ability and loans replaced low tuition as financing education was projected into the future through loan repayment. The student borrowers who were not "creditworthy" would not have been able to borrow under normal credit conditions. Nor can a creditor take a security interest in a student borrower's increased earning capacity. But, because of the creditor's advantages in collection, a student loan is effectively secured by human capital.

531. Schrag, *supra* note 123, at 405.

A defaulting borrower, and there are tens of thousands of them, must deal with stress and a negative credit rating.[532] And assembly-line collection companies will be likely to employ abusive collection tactics.[533]

Over several centuries, legislatures and courts have worked out the law of debtor and creditor. In the race of collection, the judgment is the creditor's starting line, except for prejudgment attachment. Qualifying most creditors' rights are the debtor's contract defenses, the debtor's exemptions, the statute of limitations time bar, and the bankruptcy discharge. Many of these qualifications were eliminated or diminished for the student-loan debtor. Once she enters the collection labyrinth, the borrower's exits are few and difficult to find.

Of the student-loan creditor's advantages, the most difficult provision to justify—and the most disruptive—is the restriction of her bankruptcy discharge. The student loan exception stands out in the bankruptcy code. Most exceptions to discharge target wrongful or punishment-worthy conduct[534] or domestic relations obligations like child support and alimony.[535] Other debtors of the federal government face far lower hurdles, if any, to discharge. Debtors may even receive a discharge for tax debts in many circumstances, provided that they have not engaged in tax evasion. As one consumer advocate put it, the discharge exception relegates student loan borrowers to "a special circle of bankruptcy hell reserved for dads who avoid child support and tax evaders."[536]

What should Congress do with the bankruptcy discharge? One option is to do nothing. Supporters of the status quo argue that discharge is unwarranted either because student borrowers are deadbeat debtors undeserving of discharge, or because the debts to the government should be more difficult to discharge than debts to other creditors.

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532. Daniel Austin, *The Indentured Generation: Bankruptcy and Student Loan Debt*, 53 SANTA CLARA L. REV. 329, 407 (2013).

533. *Id.* at 407–08 (noting the types of abusive practices include "incessant phone calls to home and work numbers at all hours, bullying, misrepresentation, and threats").

534. *See, e.g.*, 11 U.S.C. § 523(a)(2) (2010) (fraudulently obtained debts), (a)(4) (theft), (a)(6) (intentional torts), (a)(8) (debts arising from federal fines, penalties, forfeiture), (a)(9) (personal injury caused by driving, flying, or boating while legally intoxicated), (a)(13) (criminal restitution).

535. *Id.* § 523(a)(5) ("domestic support obligations"), (a)(15) (alimony).

536. Tyler Kingkade, *Private Student Loan Bankruptcy Rule Traps Graduates With Debt Amid Calls For Reform*, HUFFINGTON POST (Aug. 15, 2012, 9:51 AM), http://www.huffingtonpost.com/2012/08/14/private-student-loans-bankruptcy-law_n_1753462.html.

Although debtor-focused arguments animated Congress's push to impose the heightened "undue discharge" standard for student loans,[537] they are largely unpersuasive. Fears of student borrowers "filing for bankruptcy immediately upon graduation, thereby absolving themselves of the obligation to repay their student loans"[538] are largely unfounded. There is no empirical evidence that a student loan borrower is likely to commit fraud by borrowing to finance an education and then filing bankruptcy the day after she graduates.[539] Moreover, under general statutes that would remain in place, a fraudulently obtained debt cannot be discharged.[540] A more nuanced argument posits that a student debtor had time to think about borrowing and surely considered repayment.[541] But this is contrary to observation and social science.[542]

Slightly more persuasive are the arguments that focus on the creditor rather than the borrower. As one court explained, excepting student loans from discharge "help[s] ensure the financial integrity of the student loan program," and also "help[s] ensure 'public support for the [student loan] program by preventing debtors from easily discharging their debts at the expense of the taxpayers who made possible their education.'"[543] Unlike

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537. Cazenovia College v. Renshaw, 222 F.3d 82, 87 (2d Cir. 2000).

538. Tenn. Student Assistance Corp. v. Hornsby, 144 F.3d 433, 436–37 (6th Cir. 1998).

539. "[T]here are no compelling empirical data to buttress the myth that students defraud creditors any more than other debtors." John A. E. Pottow, *The Nondischargeability of Student Loans in Personal Bankruptcy Proceedings: The Search for a Theory*, 44 CAN. BUS. L.J. 245, 266 (2007); Richard Fossey, *"The Certainty of Hopelessness:" Are Courts Too Harsh Toward Bankrupt Student Loan Debtors?*, 26 J.L. & EDUC. 29, 34 (1997) (arguing that Congressional fears of student abuse of bankruptcy laws were unjustified given that no empirical evidence existed showing students were acting in bad faith). Smith, *supra* note 448, at 337 (finding no evidence of abuse).

540. *See* 11 U.S.C. § 523(a)(2)(A) (2010) (prohibiting discharge of individual debt obtained by "false pretenses, a false representation, or actual fraud . . . .").

541. Douglas G. Baird, *Discharge, Waiver, and the Behavioral Undercurrents of Debtor-Creditor Law*, 73 U. CHI. L. REV. 17, 28 (2006) ("Unlike ordinary extensions of consumer credit . . . . [t]he decision to take [an education] loan is part of a larger decision (leaving or not entering the workforce and moving) that is made only after considerable thought and care.").

542. *See* Austin, *supra* note 508, at 357 (explaining that the "skyrocketing cost" of education and the unavailability of jobs in certain fields combine to undermine students' expected future earnings); DANIEL KAHNEMAN, THINKING FAST AND SLOW 249–53 (2011) (coining the terms "planning fallacy" and "optimism bias" to explain "failures of forecasting" that can lead to dramatic differences between a plan and the eventual outcome).

543. *In re* Miller, 409 B.R. 299, 308 (E.D. Pa. 2009) (third alteration in original) (quoting *In re* Frushour, 433 F.3d 393, 400 (4th Cir. 2005)).

arguments directed at borrowers, these arguments have some basis in fact. Bankruptcy filers in 2007 alone held a total of around $5 billion in student loan debt,[544] but almost none of that debt was successfully discharged in bankruptcy.

Of course, to say that the government should not bear the $5 billion annual cost of student loan discharge is to say that bankrupt student borrowers should. For the most part, supporters of non-dischargability do not persuasively explain why student loan debt should be treated differently from other federally-held or backed debts. A dollar of government-held debt discharged in bankruptcy hurts the public fisc the same, whether the debt is from student loans, Small Business Administration loans, or unpaid taxes. If the bankruptcy law's fresh-start policy is strong enough to justify excusing the income tax delinquent or failed SBA borrower from repaying their debts, is it not strong enough to warrant forgiving the defaulting student loan borrower as well?

Many observers have suggested that the policy of fresh start should lead to broadening a student-loan borrower's bankruptcy discharge.[545] Policymakers have joined this chorus. In the fall of 2013, Senator Elizabeth Warren, without specifying details, advocated that student borrowers should be able to discharge the loans in bankruptcy like home mortgages and medical debts.[546] Senator Warren and her colleagues in Congress can choose from a smorgasbord of proposals.

First, Professor Austin favors reduction of debt to "actual fair market value," which he defines as "the amount that an investor would pay to purchase the respective student loan obligation."[547] Second, Congress can

544. *See* Iuliano, *supra* note 435, at 504, 510 (estimating, based on the 2007 Consumer Bankruptcy Project, that 238,446 individuals with student loan debt filed for bankruptcy in 2007, and that these individuals held, on average, $20,538 in student loan debt).

545. *See, e.g.*, Jean Braucher, *Mortgaging Human Capital: Federally Funded Subprime Higher Education*, 69 WASH. & LEE L. REV. 439, 474 (2012) (advocating dischargeability of federal student loans, subject to a five or seven year waiting period).

546. Tyler Kingkade, *Elizabeth Warren Calls for Big Changes to Student Loans*, HUFFINGTON POST (Sept. 29, 2013, 4:09 PM), http://www.huffingtonpost.com/2013/09/29/elizabeth-warren-student-loans_n_4013321.html (quoting Senator Warren as saying, "I'd like us to go a long way toward letting people deal with student loans the same way they deal with home mortgages and medical debts."); *see also* Elizabeth Warren, *A Principled Approach to Consumer Bankruptcy*, 71 AM. BANKR. L.J. 483, 491 n.16 (1997) (claiming that the National Bankruptcy Review Commission's 1997 recommendation to permit dischargeability of student loans "go[es] a long way toward restoring the scope of the bankruptcy discharge").

547. Austin, *supra* note 532, at 417–18.

return to the law between 1976 and 1998 when student debts were dischargeable after five or seven years.[548] This would adequately address concerns about the hypothetical student loan debtor who graduates on Tuesday and files for bankruptcy on Wednesday. Third, Congress put the discharge of private student loans under undue hardship in 2005 despite the fact that this is not needed to protect the taxpayer.[549] Congress could make private loans dischargeable again.[550] Senator Durbin has introduced legislation to implement that idea.[551]

To these options, we would add two more. Our initial proposal is a minimalist one based on the idea that student loan debt will continue to be excruciatingly difficult to discharge. Under present law, a Chapter 13 debtor may pay a priority debt[552] in full before paying general unsecured debts.[553] But, unlike many other non-dischargeable debts, a student loan is not a priority debt. Congress should give student loans priority status so that the debtor may pay them ahead of unsecured debts.[554] Second, Congress might consider modifying the student loan exception to shift the burden of bringing an adversary proceeding to contest discharge from the debtor to the creditor.

The simplest and we think the wisest option, however, is to treat a student loan like other unsecured debt, for example a credit-card debt. Our colleague Professor Margaret Howard analogizes educational debts to credit-card debts and argues that the debtor should be able to discharge the

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548. *Id.* at 416; Braucher, *supra* note 545, at 473.

549. *See* Austin, *supra* note 532, at 364 (noting that the 2005 Bankruptcy Abuse Prevention and Consumer Protection Act extended the student loan discharge exception to all education loans, including those with no federal guaranty).

550. *See* Austin, *supra* note 532, at 415 (suggesting that making private student loans dischargeable might "strike a useful middle ground, as there are no forgiveness programs for private loans, and lenders can refuse to make new loans" to borrowers deemed uncreditworthy).

551. Fairness for Struggling Students Act of 2013, S. 114, 113th Cong. (2013). In the House, Representative Steve Cohen has introduced a similar bill. Private Student Loan Bankruptcy Fairness Act of 2013, H.R. 532, 113th Cong. (2013). Smith, *supra* note 448, at 349 (2013) (agreeing that debtors should be allowed to discharge private student loans).

552. *See* 11 U.S.C. § 507 (2010) (listing claims that have priority and not including student loans).

553. *See* 11 U.S.C. § 1322(a)(2), (4) (2010) (mandating full payment of claims entitled to priority, except in limited circumstances).

554. Braucher, *supra* note 545, at 473–75. *See also* Smith, *supra* note 448, at 352 (2013) (calling for treatment of student debt as a priority debt in Chapter 13, like back taxes).

debts in the same way. She writes that Congress based the "undue hardship" bar on discharge on anecdote and overgeneralization.[555] If fortune favors, we favor Professor Howard's solution.

The divided hyper-partisan Congress that gave us the confusing and unfair student-loan system we have isn't, Professor Austin insists, about to ameliorate the student debtor's plight.[556] Politics is the art of the possible, but politics isn't our job. Our role as scholars is not to anticipate Congress's response, but it is to address the issues as we see them, and to discover and then explain what justice requires. We hope that someday the wise and humane solutions we propose will become public policy.

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555. Margaret Howard, *A Theory of Discharge in Consumer Bankruptcy*, 48 OHIO ST. L.J. 1047, 1087 (1987) ("[T]he [educational loan] provision is a perfect example of legislation based on pathological cases, in which a result appropriate for a small minority of cases is imposed on substantially all."); Smith, *supra* note 448, at 337 (2013)(also finding no evidence of abuse). *See also* Sarah E. Smith, *Should the Eighth Circuit Continue To Be the Loan Ranger? A Look at the Totality of the Circumstances Test for Discharging Student Loans Under the Undue Hardship Exception in Bankruptcy*, 29 HAMLINE L. REV. 601, 615–19 (2006) (examining four tests for "undue hardship" developed by federal courts).

556. Austin, *supra* note 532, at 417 ("Discharge of education loan debt is not likely in the foreseeable future, and as yet, the marketplace has not come up with a solution to student debt that matches the demand for education loans.").