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# The “Undue Hardship” Test: The Dangers of a Subjective Test in Determining the Dischargeability of Student Loan Debt in Bankruptcy

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## NOTE

# The “Undue Hardship” Test: The Dangers of a Subjective Test in Determining the Dischargeability of Student Loan Debt in Bankruptcy

*Conway v. National Collegiate Trust (In re Conway)*, 542 B.R. 855 (B.A.P. 8th Cir. 2015)

*Rebekah Keller*\*

### I. INTRODUCTION

In today’s culture of living life on credit, post-secondary education loans have become the most popular method for American students to pay for their college degrees. Further, “[t]he costs for a higher education are among the fastest-rising costs in American culture today. Since 1980, tuition costs at U.S. colleges and universities have risen 757 percent.”<sup>1</sup> With \$1.2 trillion in current outstanding student loan debt,<sup>2</sup> approximately 43 percent of the 22 million Americans with federal student loan debt are not making payments on their loans.<sup>3</sup> In 2014, 69 percent of college seniors at public and nonprofit colleges graduated with some student loan debt.<sup>4</sup> Missouri students alone graduated with an average of \$25,844 in student loan debt in 2014.<sup>5</sup> Coupled with the

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\* B.A., Macalester College, 2014; J.D. Candidate, University of Missouri School of Law, 2017. Associate Managing Editor, *Missouri Law Review*, 2016–2017. I would like to offer a sincere thank you to Professor Michelle Arnpol Cecil for her constant support and guidance throughout law school, particularly through the learning, writing, and editing process of this Note.

1. Cecillia Barr, *Students & Debt*, DEBT.ORG, <https://www.debt.org/students/> (last visited Feb. 7, 2017) (“In comparison, food and electricity costs have risen about 150 percent and gasoline prices have risen more than 400 percent over the same period of time.”).

2. *Id.*

3. John Hayward, *Student Loan Bubble Update: Some 40 Percent of Borrowers Aren’t Making Payments*, BREITBART (Apr. 7, 2016), <http://www.breitbart.com/big-government/2016/04/07/student-loan-bubble-update-some-40-percent-of-borrowers-arent-making-payments/>.

4. Debbie Cochrane & Matthew Reed, *Student Debt and the Class of 2014*, INST. FOR C. ACCESS & SUCCESS (Oct. 2015), [http://ticas.org/sites/default/files/pub\\_files/classof2014.pdf](http://ticas.org/sites/default/files/pub_files/classof2014.pdf).

5. *Id.* at 6–7 tbl.3. In a ten-year study conducted by the Institute for College Access and Success, the changes in student loan debt between 2004 and 2014 were analyzed and compared on a state-by-state basis. *Id.* at 1–35.

high unemployment rates of a recovering economy, student loan debt poses the greatest obstacle for young adults starting out on their own.<sup>6</sup> Such large amounts of debt can have a serious impact on the futures of these student debtors. In a recent policy analysis paper, Mark Kantrowitz, a nationally recognized expert on student loan debt and financial aid, found:

[S]tudents who graduate with excessive debt are about 10% more likely to say that it caused delays in major life events, such as buying a home, getting married, or having children. They are also about 20% more likely to say that their debt influenced their employment plans, causing them to take a job outside their field, to work more than they desired, or to work more than one job.<sup>7</sup>

One unique characteristic of student loan debt, compared with other types of debt that a consumer may take on, is its status as a non-dischargeable debt under the Bankruptcy Code.<sup>8</sup> Thus, student loan debt is not automatically dischargeable when debtors file for bankruptcy and receive a discharge of their other debts in a bankruptcy proceeding.<sup>9</sup> This creates a hardship for debtors who have come out of bankruptcy still saddled with massive student loan debt, leaving them with little hope they will ever rid themselves of their accumulated debt.<sup>10</sup>

Even so, debtors continue to attempt to have their student loan debt discharged in bankruptcy. Because of the difficult standard put in place by Congress, commonly referred to as the “undue hardship” requirement, this requires some creative arguments on the part of these debtors to convince a court that their student loan debt imposes enough of a hardship that it could be categorized as “undue.”<sup>11</sup> In addition to its non-dischargeability, student loan debt can impose different obstacles on borrowers, depending on whether the debt agreement is for federally or privately funded student loans. Even though neither federal nor private student loan debt is dischargeable in bankruptcy, their lasting effects on debtors can be very different. This Note explores the varying

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6. *Data and Statistics*, MO. DEP’T LAB. & INDUS. REL., <http://labor.mo.gov/data> (last visited Feb. 7, 2017).

7. Mark Kantrowitz, *Why the Student Loan Crisis Is Even Worse Than People Think*, TIME (Jan. 11, 2016), <http://time.com/money/4168510/why-student-loan-crisis-is-worse-than-people-think/>.

8. 11 U.S.C. § 523(a)(8) (2012).

9. *Id.*; see also *id.* § 524.

10. Marc S. Stern & Larry B. Feinstein, *Debts That Can Follow You to the Grave: What You Can’t Get Away with in Bankruptcy*, AM. B., [http://www.americanbar.org/newsletter/publications/gp\\_solo\\_magazine\\_home/gp\\_solo\\_magazine\\_index/debts.html](http://www.americanbar.org/newsletter/publications/gp_solo_magazine_home/gp_solo_magazine_index/debts.html) (last visited Feb. 7, 2017) (“Section 523 deals with particular claims. These are the debts that may ‘follow you to the grave.’”).

11. § 523(a)(8). See, e.g., Jason Iuliano, *An Empirical Assessment of Student Loan Discharges and the Undue Hardship Standard*, 86 AM. BANKR. L.J. 495 (2012).

impacts that public and private student loan debt can have on borrowers both before and after a bankruptcy.

## II. FACTS AND HOLDING

Chelsea Ann Conway, a single college graduate, filed for relief under Chapter 7<sup>12</sup> of the Bankruptcy Code in December 2009.<sup>13</sup> Ms. Conway received a discharge in March 2010, and her case was closed.<sup>14</sup> However, in December 2011, Ms. Conway filed a motion to reopen her case, which was granted, in order to determine whether her non-dischargeable student loans could be discharged under the undue hardship exception of the Bankruptcy Code.<sup>15</sup> In August and November 2012, two of the three creditors holding Ms. Conway’s student loan debt filed stipulations to discharge the debt owed to them by Ms. Conway.<sup>16</sup> This left Ms. Conway with fifteen outstanding student loans that survived her Chapter 7 bankruptcy.<sup>17</sup> The fifteen remaining outstanding student loan debts continued to be disputed by the creditor in the case, National Collegiate Trust (“NCT”).<sup>18</sup>

Ms. Conway’s student loans comprised of debt amounts borrowed between 2003 and 2005 while she was enrolled in college at Webster University in St. Louis, Missouri.<sup>19</sup> Ms. Conway borrowed a total of \$37,100 from NCT while attaining her bachelor’s degree at Webster University.<sup>20</sup> She graduated from Webster University in 2005 with a Bachelor of Arts in Media Communications.<sup>21</sup> After attaining her degree, Ms. Conway enrolled at Saint Louis Community College and completed additional coursework.<sup>22</sup> In order to pay

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12. A debtor or debtor organization may also file for bankruptcy under Chapter 11 and Chapter 13; however, this Note focuses on the organization and structure of Chapter 7 bankruptcy proceedings only because that was the subject of the instant case. *See generally* 11 U.S.C. chs. 7, 11, 13.

13. *Conway v. Nat’l Collegiate Tr. (In re Conway)*, 489 B.R. 828, 830 (Bankr. E.D. Mo. 2013) [hereinafter *Conway Bankr. Ct. I*], *rev’d and remanded*, 495 B.R. 416 (B.A.P. 8th Cir. 2013), *reversal aff’d*, 559 F. App’x 610 (8th Cir. 2014) (per curiam).

14. *Id.*

15. *Id.*

16. *See id.* at n.2.

17. *Id.* at 830.

18. *See id.* Ms. Conway also still has approximately \$18,000 in federally guaranteed student loans that were not part of the proceedings and are currently in repayment under an income-contingent repayment plan, and Ms. Conway states there is no similar plan available for private student loans, like the ones at issue in Ms. Conway’s case. *Conway v. Nat’l Collegiate Tr. (In re Conway)*, 495 B.R. 416, 418 n.4 (B.A.P. 8th Cir. 2013) [hereinafter *Conway B.A.P. I*], *aff’d*, 559 F. App’x 610 (8th Cir. 2014) (per curiam).

19. *See Conway Bankr. Ct. I*, 489 B.R. at 830.

20. *See id.* The interest rates on the loans ranged from 3.25 percent to 5.15 percent. *Id.*

21. *Id.*

22. *Id.*

for these courses, Ms. Conway borrowed an additional \$33,000 from NCT from 2005 to 2007.<sup>23</sup> In October 2005, Ms. Conway began a full-time job, but in July 2007, she was laid off.<sup>24</sup> She began working part-time in temporary positions, while also receiving unemployment benefits.<sup>25</sup> Ms. Conway found full-time work again in December 2007 but was again laid off in September 2008 and again began receiving unemployment benefits while working in part-time temporary positions.<sup>26</sup> Since April 2009, Ms. Conway has been waitressing part-time at two restaurants.<sup>27</sup>

Ms. Conway had an adjusted gross income of \$21,115 in 2008; \$16,127 in 2009; \$25,256 in 2010; and \$25,390 in 2011.<sup>28</sup> In her pleadings, Ms. Conway estimated her monthly income as of July 2012 to be \$2461.45.<sup>29</sup> Ms. Conway had also received \$625 in settlement proceeds in relation to a car accident in August 2012.<sup>30</sup> Ms. Conway reported her total monthly income at the time of her hearing to be \$2040.36 and her total monthly expenses to be \$1737.25.<sup>31</sup> This left Ms. Conway with a net monthly income of \$303.11.<sup>32</sup> Since 2005, NCT had granted Ms. Conway part-time deferments, temporary forbearances, and forbearances on all fifteen loans.<sup>33</sup> As of 2012, Ms. Conway had repaid a total of \$5734.48.<sup>34</sup>

Ms. Conway further stated that she suffered from depression, anxiety, Attention-Deficit Disorder (“ADD”), scoliosis, arthritis, and other ailments that

23. *Id.* at 831.

24. *Id.*

25. *Id.*

26. *Id.*

27. *Id.*

28. *Id.* The bankruptcy court also noted Ms. Conway’s income tax refunds from 2008 through 2011, totaling approximately \$3000. *Id.*

29. *See id.* Ms. Conway reported working approximately twenty hours per week at The Boathouse in Forest Park at \$1665.55 per month and approximately twenty hours per week at P.F. Chang’s China Bistro at \$795.90 per month in July 2012 and \$1379.97 per month at The Boathouse in Forest Park in December 2012. *Id.*

30. *Id.* Ms. Conway reported she would be receiving an additional \$1000 as part of this settlement agreement in the future. *Id.*

31. *Id.* The bankruptcy court broke down Ms. Conway’s monthly expenses to be: \$257.50 in rent; \$98 for electricity and heating; \$158 for cell phone service; \$300 for food; \$50 for clothing; \$25 for laundry and dry cleaning; \$30 for medical and dental care; \$380 for transportation; \$32 for personal care; and \$97 for miscellaneous items. *Id.* The change in Ms. Conway’s monthly income between July 2012 and the time of trial in December 2012 was attributable to fluctuations in her hours at one of her waitressing jobs in the fall and winter. *Id.*

32. *Id.* The bankruptcy court made sure to note that these income amounts had increased since the time of Ms. Conway’s Chapter 7 Petition only three years prior, where Ms. Conway reported a monthly income of \$1397.67 and monthly expenses of \$1350.50, leaving a net monthly income of \$47.17. *Id.*

33. *Id.* at 830.

34. *See id.*

limited her ability to work.<sup>35</sup> Ms. Conway also stated that these ailments would continue to limit her future capabilities to maintain gainful employment.<sup>36</sup> Ms. Conway also asserted that, despite her best efforts, she was unable to find any kind of higher paying, full-time employment in the current job market.<sup>37</sup> Finally, she argued that her bachelor’s degree in media communications was useless to her in finding gainful employment because it provided her with none of the skills, experiences, or expertise necessary for open positions.<sup>38</sup>

In reopening her bankruptcy case, Ms. Conway relied on *Brunner v. New York State Higher Education Services Corp.*,<sup>39</sup> arguing that her outstanding student loan debts should be discharged because they created an “undue hardship” on her and prevented her from receiving a fresh start once her Chapter 7 proceedings were resolved and closed.<sup>40</sup> Ms. Conway argued she was unable to repay over \$118,500 in student loan debt on her current income and that, with her useless degree and ailments, the possibility of finding more gainful employment in the future that would allow her to pay these loans was unlikely.<sup>41</sup>

The U.S. Bankruptcy Court for the Eastern District of Missouri granted Ms. Conway’s petition to reopen her case in order to determine whether her student loan debt did in fact impose an undue hardship on Ms. Conway and should be dischargeable.<sup>42</sup> However, the court rejected Ms. Conway’s argument that the court rely on the test set forth in *Brunner*.<sup>43</sup> Instead, the court’s analysis depended on the Eighth Circuit’s “totality-of-the-circumstances”<sup>44</sup> approach to the undue hardship standard.<sup>45</sup> Based on this totality-of-the-circumstances test, the court found that Ms. Conway’s reasonably reliable future financial resources,<sup>46</sup> combined with her reasonable living expenses, meant that

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35. *Id.* at 832.

36. *See id.*

37. *See id.* Ms. Conway contended that she sent out over 200 resumes and job applications. *Id.*

38. *Id.*

39. 831 F.2d 395 (2d Cir. 1987) (per curiam).

40. *Conway Bankr. Ct. I*, 489 B.R. at 832; 11 U.S.C. § 523(a)(8) (2012).

41. *See Conway Bankr. Ct. I*, 489 B.R. at 832.

42. *Id.* at 830.

43. *Id.* at 833.

44. *See id.* (citing *Long v. Educ. Credit Mgmt. Corp. (In re Long)*, 322 F.3d. 549, 554 (8th Cir. 2003) (rejecting *Brunner* test)).

45. *Id.*

46. The court looks at the debtor’s past, current, and possible future financial resources. *In re Wegfehrt*, 10 B.R. 826, 830 (Bankr. N.D. Ohio 1981) (citing REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. Doc. No. 137, 93d Cong., 1st Sess., Pt. II 140–41 n.17 (1973)). It determines, based on information provided by the debtor, what the debtor’s future resources may look like and determines if those are reasonably reliable. It is a guessing game that depends on the debtor’s ability to prove his or her financial dependence/independence.

Ms. Conway would be able to repay NCT in the future without an undue hardship.<sup>47</sup> Further, the court found that Ms. Conway’s “written submissions to this Court evidence” that she “is articulate, poised, intelligent and quite capable. . . . [S]he undoubtedly has the education and transferable skills that will allow her to obtain a more lucrative career in the future.”<sup>48</sup> The bankruptcy court also found that Ms. Conway’s medical expenses, as part of her monthly living expenses, would likely be reduced by the addition of health insurance if she found a full-time job.<sup>49</sup> The court held that Ms. Conway’s argument failed the totality-of-the-circumstances test, and thus her student loan debt continued to be non-dischargeable.<sup>50</sup>

Ms. Conway appealed the bankruptcy decision to the Bankruptcy Appellate Panel (“BAP”) for the Eighth Circuit.<sup>51</sup> The BAP reviewed Ms. Conway’s case *de novo*<sup>52</sup> and ultimately reversed the bankruptcy court’s holding and remanded the case to the bankruptcy court.<sup>53</sup> First, the BAP reviewed the facts provided to the bankruptcy court regarding Ms. Conway’s income and expenses and concluded that nothing in the record controverted the bankruptcy

47. *Conway Bankr. Ct. I*, 489 B.R. at 836.

48. *Id.* at 834–35. While Ms. Conway’s *pro se* representation in her bankruptcy case led the court to deny her request to discharge her student loans, based, in part, on her competence, intelligence, and future job prospects, other debtors’ *pro se* representations have led courts to reach very different conclusions in the past. *See Rose v. U.S. Dep’t of Educ. (In re Rose)*, 215 B.R. 755, 765 (Bankr. W.D. Mo. 1997) (concluding that the debtor’s student loans should be discharged, in part, because the debtor’s *pro se* representation of herself in the case was so poor that the court highly doubted the debtor’s ability to procure “more lucrative employment in the foreseeable future”).

49. *See Conway Bankr. Ct. I*, 489 B.R. at 835–36.

50. *See id.* at 836.

51. *Conway B.A.P. I*, 495 B.R. 416, 418 (B.A.P. 8th Cir. 2013), *aff’d*, 559 F. App’x 610 (8th Cir. 2014) (per curiam). When appealing a decision from the federal bankruptcy court, the petitioner can appeal to the federal district court or to the Bankruptcy Appellate Panel for the district in which the debtor resides. The Bankruptcy Appellate Panel is a panel of appellate court judges and district court judges who are considered to be specialists in bankruptcy law and hear bankruptcy court appeals. Appealing to the Bankruptcy Appellate Panel requires both parties to agree on venue. *See Samuel R. Maizel, The “Who, What, When, Where, Why, and How” of Appeals in Bankruptcy Proceedings – Generally*, OFFS. U.S. ATT’YS (Mar. 15, 1996), <https://www.justice.gov/usam/civil-resource-manual-96-who-what-when-where-why-and-how-appeals-bankruptcy-proceedings> (last updated Mar. 2007).

52. *Conway B.A.P. I*, 495 B.R. at 419 (“Undue hardship is a question of law which we review *de novo*. Subsidiary findings of fact on which the legal conclusion is based are reviewed for clear error.” (quoting *Educ. Credit Mgmt. Corp. v. Jesperson*, 571 F.3d 775, 779 (8th Cir. 2009))).

53. *Id.* at 418.

court’s finding of fact that Ms. Conway’s current income was stable.<sup>54</sup> However, the BAP did not agree with the bankruptcy court as to Ms. Conway’s “reasonably reliable future financial resources.”<sup>55</sup>

The BAP noted that Ms. Conway had not made much more than \$25,000 per year in the eight years since she graduated from college, which indicated that Ms. Conway’s case was not one where a debtor is intentionally underemployed.<sup>56</sup> The BAP also noted that, even though the bankruptcy court found that Ms. Conway had a net income, after expenses, of approximately \$300 per month, the minimum principal and interest payment due to NCT is \$846.16 per month.<sup>57</sup> The BAP ultimately held that “[w]hile Ms. Conway may have the ‘possibility’ of earning a higher income in the future, there is no evidence to support that possibility. [The court] will not substitute assumptions or speculation for reasonably reliable facts.”<sup>58</sup> Based on this, the BAP found that the bankruptcy court’s finding that Ms. Conway’s possible future financial resources made it likely that she would be able to pay NCT the entire debt was clearly erroneous.<sup>59</sup>

The BAP relied on *Education Credit Management Corp. v. Jesperson*<sup>60</sup> in determining that the bankruptcy court’s conclusion that Ms. Conway’s monthly expenses would be reduced when she received health insurance through a full-time job was erroneous.<sup>61</sup> It reasoned that a court cannot “engage in speculation when determining net income and reasonable and necessary expenses.”<sup>62</sup> The BAP then rejected NCT’s argument that Ms. Conway had sufficient disposable income to repay *part* of her loans, and as such, the loans should not be discharged.<sup>63</sup> The BAP rejected this theory, pointing out that no case law in the Eighth Circuit authorized the court to “partially discharge” a student loan.<sup>64</sup> The BAP was wary of such “subjective application of § 523(a)(8),” referring to concerns about inequities, unpredictability, and a

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54. *Id.* at 420–21.

55. *Id.* at 421.

56. *Id.*

57. *Id.* at 422.

58. *Id.* (quoting *Walker v. Sallie Mae Servicing Corp. (In re Walker)*, 650 F.3d 1227, 1233 (8th Cir. 2011)).

59. *Id.*

60. 571 F.3d 775, 780 (8th Cir. 2009).

61. *Conway B.A.P. I*, 495 B.R. at 422.

62. *Id.* (quoting *Jesperson*, 571 F.3d at 780).

63. *Id.* at 423–24.

64. *Id.* at 423 (“The court does not have the authority to modify the payment terms of a student loan or to discharge a partial amount of principal or accrued interest.” (quoting *Hawkins v. Buena Vista Coll. (In re Hawkins)*, 187 B.R. 294, 300–01 (Bankr. N.D. Iowa 1995)); see also *Andresen v. Neb. Student Loan Program, Inc. (In re Andresen)*, 232 B.R. 127, 136–37 (B.A.P. 8th Cir. 1999) (criticizing “partial discharge” theory without deciding the issue), *abrogated by Long v. Educ. Credit Mgmt. Corp. (In re Long)*, 322 F.3d 549 (8th Cir. 2003).



lack of uniformity in outcomes under such an approach.<sup>65</sup> Next, the BAP noted that Ms. Conway's debt was actually fifteen individual loans, all held by NCT, and determined that the undue hardship analysis should be applied to each loan separately under § 523(a)(8).<sup>66</sup> The court then remanded Ms. Conway's case back to the bankruptcy court to allow the court to apply § 523(a)(8) on a separate loan-by-loan basis and determine the repayment of which, if any, of Ms. Conway's fifteen student loans imposed an undue hardship on her after bankruptcy.<sup>67</sup>

NCT appealed to the Eighth Circuit the BAP's reversal of the bankruptcy court's determination that Ms. Conway had "reasonably reliable future financial resources with which to pay her entire student loan debt to NTC [sic]."<sup>68</sup> The Eighth Circuit affirmed the BAP's judgment, finding that there was no abuse of discretion in the BAP's decision to remand for further proceedings.<sup>69</sup>

On remand, the Bankruptcy Court for the Eastern District of Missouri was tasked with applying the undue hardship analysis on a loan-by-loan basis to determine the dischargeability of Ms. Conway's fifteen outstanding student loan debts held by NCT.<sup>70</sup> As instructed by the BAP, the court was required to conduct a loan-by-loan analysis based on Ms. Conway's "present disposable income."<sup>71</sup> However, the BAP did not determine the start and end dates from which the bankruptcy court was to determine Ms. Conway's present monthly income.<sup>72</sup> The bankruptcy court based its analysis on Ms. Conway's disposable income for an entire year, starting in November 2013 and ending in October 2014, based on Ms. Conway's submissions of her financial resources to the court for that year.<sup>73</sup> The court then found Ms. Conway's present disposable income to be \$170.30 per month.<sup>74</sup> Based on this amount of disposable income, the court found that Ms. Conway could repay loans 1, 2, 3, and 9 with no undue hardship to her.<sup>75</sup> The court then discharged student loans 4, 5, 6, 7, 8, 10, 11,

65. *Conway B.A.P. I*, 495 B.R. at 423.

66. *Id.*

67. *Id.* at 423–24.

68. *Conway v. Nat'l Collegiate Tr. (In re Conway)*, 559 F. App'x 610, 610 (8th Cir. 2014) (per curiam) [hereinafter *Conway* 8th Cir.].

69. *Id.* at 611.

70. *Conway v. Nat'l Collegiate Tr. (In re Conway)*, Ch. 7 Case No. 09-52394-399, Adv. No. 12-4033-659, slip op. at 1 (Bankr. E.D. Mo. Apr. 20, 2015) [hereinafter *Conway Bankr. Ct. II*], *aff'd*, 542 B.R. 855 (B.A.P. 8th Cir. 2015).

71. *Conway B.A.P. I*, 495 B.R. at 424.

72. *Conway Bankr. Ct. II*, slip op. at 2.

73. *Id.*

74. *Id.* at 5 ("Therefore, Debtor's disposable income which this Court deems to be Debtor's present disposable income is \$170.30 (\$1957-\$1786.70).").

75. *Id.* at 6. The court determined that the combined monthly installment payment of \$167.11 of these four loans fell within Ms. Conway's estimated present monthly disposable income of \$170.30 but did not exceed her present monthly disposable income. *Id.*

12, 13, 14, and 15 because repayment of those loan amounts constituted undue hardship.<sup>76</sup>

Ms. Conway requested that the bankruptcy court amend its judgment due to her increased expenses and decreased income since November 2014, but the court denied the request.<sup>77</sup> Ms. Conway then appealed the bankruptcy court’s decision that some, but not all, of her student loans were dischargeable to the BAP, seeking to have the remaining student loan debts discharged.<sup>78</sup> Ms. Conway argued the bankruptcy court erred in determining that some of her student loans remain non-dischargeable because it did not take into consideration changes in her income and expenses after the court’s cut-off date.<sup>79</sup> Using an abuse of discretion standard of review, the BAP rejected Ms. Conway’s argument, finding that the bankruptcy court did not abuse its discretion in denying Ms. Conway’s motion to amend the judgment and discharge her remaining four student loan debts.<sup>80</sup>

### III. LEGAL BACKGROUND

In order to examine the complicated nature of the BAP’s decision in *In re Conway*, and its implications to individuals in the Eighth Circuit with student loan debt, a thorough analysis of the Bankruptcy Code and current case law on student loan non-dischargeability is necessary. This Part addresses the framework of the federal bankruptcy statutes and the exceptions to the discharge of debt in bankruptcy. Next, it examines the current student loan system and compares federal and private student loan programs. Lastly, this Part examines the current case law regarding the discharge of student loan debt and how the circuits have split regarding which facts-and-circumstances test controls when making determinations of “undue hardship,” as required by statute.

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76. *Id.*

77. *Conway v. Nat’l Collegiate Tr. (In re Conway)*, 542 B.R. 855, 856–57 (B.A.P. 8th Cir. 2015) [hereinafter *Conway B.A.P. II*].

78. *Id.* at 856.

79. *Id.* at 857. Ms. Conway alleged that she was laid off from one of her jobs after November 2014, her federal student loan payments and health insurance expenses increased after November 2014, and that the court erred in reducing her monthly miscellaneous expenses. *Id.*

80. *Id.* at 859. The court noted,

A bankruptcy court’s denial of a motion for new trial, or to alter or amend a judgment, is reviewed with deference and will not be reversed absent a clear abuse of discretion. The bankruptcy court abuses its discretion when it fails to apply the proper legal standard or bases its order on findings of fact that are clearly erroneous.

*Id.* at 857 (citations omitted).

*A. Bankruptcy Statutes and the Exception to Student Loan Discharge*

Title XI of the U.S. Code codifies the federal bankruptcy statutes.<sup>81</sup> Title XI also designates the different types of bankruptcy filings available.<sup>82</sup> Consumer debtors may file for bankruptcy under three different code chapters: Chapter 7, Chapter 11, and Chapter 13.<sup>83</sup> The debtors' first duty under each filing option is to report all income, personal property, and other assets in his or her bankruptcy petitions.<sup>84</sup> Generally, all property in debtors' estates is available to pay creditors; however, debtors can exempt certain portions of their property from their bankruptcy estates.<sup>85</sup> Section 522 of Title XI establishes allowable exemptions.<sup>86</sup> In a Chapter 7 bankruptcy proceeding, non-exempt property and assets must be turned over to a bankruptcy trustee.<sup>87</sup> The assets and property will be distributed and sold to creditors.<sup>88</sup> Once non-exempt assets have been used to pay off creditors, the bankruptcy court will issue a discharge of the remaining outstanding debts.<sup>89</sup> However, not all debts reported in a debtor's Chapter 7 bankruptcy proceeding are dischargeable.<sup>90</sup>

Section 523 of the Bankruptcy Code sets forth the exceptions to discharge.<sup>91</sup> Among those exceptions, the most common debts that are prohibited from discharge in bankruptcy are debts incurred by fraud or false representation,<sup>92</sup> child support obligations,<sup>93</sup> alimony obligations,<sup>94</sup> federal taxes or tax penalties,<sup>95</sup> and federal student loans or other educational loan obligations.<sup>96</sup> Specifically, § 523(a)(8) states that a discharge of student loans available under a Chapter 7 bankruptcy proceeding does not discharge any student loan debt

81. 11 U.S.C. § 101 (2012).

82. *Id.* §§ 701, 1101, 1301.

83. *Id.* §§ 701, 1101, 1301. Additionally, family farmers and fishermen, as defined under the code, can file for bankruptcy protection under Chapter 12. *Id.* § 109(f).

84. *Id.* § 521.

85. *Id.* § 522.

86. *Id.* Some common exemptions include: debtors' interests in real estate – up to a certain value, interest in a motor vehicle – up to a certain value, jewelry used primarily for personal or family reasons, and furniture, appliances, and clothing – up to a certain value. *Id.* §§ 522(d)(1)–(5).

87. *Id.* § 704.

88. Secured creditors are paid back before unsecured creditors. *Id.* § 502. Certain unsecured creditors have priority over other unsecured creditors. *Id.* § 507.

89. *Discharge in Bankruptcy – Bankruptcy Basics*, U.S. CTS., <http://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/discharge-bankruptcy-bankruptcy-basics> (last visited Feb. 7, 2017).

90. *Id.*

91. 11 U.S.C. § 523.

92. *Id.* § 523(a)(2)(A).

93. *Id.* § 523(a)(5).

94. *Id.* § 523(a)(15).

95. *Id.* § 523(a)(1).

96. *Id.* § 523(a)(8). There are nineteen categories of non-dischargeable debts in a Chapter 7 bankruptcy proceeding. *Discharge in Bankruptcy*, *supra* note 89.

“unless excepting such debt from discharge . . . would impose an undue hardship on the debtor . . . for . . . an educational benefit [] or loan made, insured, or guaranteed by a governmental unit, or . . . any other educational loan that is a qualified education loan.”<sup>97</sup> However, the statute does not define “undue hardship.” The bankruptcy courts are thus required to determine the definition of “undue hardship” on a case-by-case basis.

Section 523(a)(8) was amended to include student loan debt as an exception to dischargeability in 1978.<sup>98</sup> Section 523(a)(8) was designed by Congress to “prevent abuse of the bankruptcy system by student borrowers who reap the benefits of access to higher education but seek to escape repayment of their student loan obligations upon graduation.”<sup>99</sup> The amendment protected both federal and private student loans lenders from having their loan agreements discharged in bankruptcy without a showing of undue hardship.<sup>100</sup>

### B. Federal Versus Private Student Loans

Federal student loans are funds set aside by the federal government to supplement post-secondary educational costs for U.S. citizens.<sup>101</sup> Private loans, on the other hand, are funds provided by a private lender like a bank, credit union, or school.<sup>102</sup> Federal student loans have fixed interest rates and income-based repayment plans that are often not available with private student loans.<sup>103</sup> Due to the adjustable interest rates on most private student loans, private student loans tend to be more expensive overall.<sup>104</sup> In addition to the different interest rates, federal and private student loans have different eligibility standards; most private loans require a credit check and/or a cosigner, whereas federal student loan programs are mostly need-based, relying on the student’s income, and do not require credit checks.<sup>105</sup>

97. § 523(a)(8).

98. H.R. REP. NO. 95-595, at 466–75 (1977), as reprinted in 1978 U.S.C.C.A.N. 5963, 6093–94. At first, only federal student loans were made non-dischargeable, but in 2005, private student loans were added to the statute. Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 8-109, § 220, 119 Stat. 23, 59 (codified at 11 U.S.C. 523(a)).

99. Conway Bankr. Ct. I, 489 B.R. 828, 833 (Bankr. E.D. Mo. 2013) (citing Long v. Educ. Credit Mgmt. Corp. (*In re Long*), 322 F.3d 549, 553 (8th Cir. 2003)), reversed and remanded, 495 B.R. 416 (B.A.P. 8th Cir. 2013), reversal *aff’d*, 559 F. App’x 610 (8th Cir. 2014) (per curiam).

100. *Id.*; 11 U.S.C. § 523(a)(8).

101. *Federal Versus Private Loans*, FED. STUDENT AID, U.S. DEP’T EDUC., <https://studentaid.ed.gov/sa/types/loans/federal-vs-private> (last visited Feb. 7, 2017).

102. *Id.*

103. *Id.*

104. *Id.*

105. *Id.*

The major characteristics of federal and private student loans that affect how and who borrows what are the interest rates, repayment plans, and deferment and forbearance options.<sup>106</sup> Federal student loans offer fixed interest rates that are set by Congress and rarely change; the last time the federal Stafford Loan limits were changed was in 2008.<sup>107</sup> Generally, lending exists because of the lender's ability to impose interest rates.<sup>108</sup> Rates have varied from industry to industry and from program to program over the years.<sup>109</sup> Lenders have the ability to adjust interest rates for a variety of reasons.<sup>110</sup> Currently, federal student loan interest rates are between 4.29 percent and 6.84 percent per loan.<sup>111</sup> Most private student loans use an adjustable interest rate, which currently ranges from 0.25 percent to 15.74 percent.<sup>112</sup> In the student lending industry, interest rates also serve another purpose to many private student loan lenders: an insurance policy. The interest rates attached to private student loans act both as an incentive when taking on riskier borrowers and as a bonus because student loans are non-dischargeable – the interest accrues on private student loans until they are paid off in full.<sup>113</sup>

In addition, federal student loans offer many repayment options; in fact, most have been adopted to encourage debtors to make monthly payments on their loans, no matter how low their income.<sup>114</sup> Income-based repayment plans allow borrowers to set up monthly payment amounts they can actually afford based on their monthly income, and in most cases, the remaining unpaid balance of one's federal loans will be forgiven after twenty-five years.<sup>115</sup> Private student loans often do not have income-based repayment options but are limited to a set five-, ten-, fifteen-, or twenty-year period to repay.<sup>116</sup> Federal stu-

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106. *Id.*

107. *Private Student Loans*, FINAID, <http://www.finaid.org/loans/privatestudent-loans.phtml> (last visited Feb. 7, 2017).

108. *See generally* SIDNEY HOMER & RICHARD SYLLA, A HISTORY OF INTEREST RATES (4th ed. 2005).

109. *See id.*

110. STEVE SURANOVIC, POLICY AND THEORY OF INTERNATIONAL ECONOMICS 887 (2012), <http://2012books.lardbucket.org/books/policy-and-theory-of-international-economics/index.html>.

111. *Interest Rates and Fees*, FED. STUDENT AID, U.S. DEP'T EDUC., <https://studentaid.ed.gov/sa/types/loans/interest-rates> (last visited Feb. 7, 2017).

112. *Private Student Loans*, *supra* note 107. Interest rates on adjustable interest rate loans are in part dependent on the borrower's credit score, which means borrowers with lower credit scores will have interest rates closer to the 15.74 percent interest rates instead of the 0.25 percent rates.

113. In theory, this means that, as interest accrues, a debtor in financial hardship will be paying on his or her student loans forever.

114. *Federal Versus Private Loans*, *supra* note 101.

115. *Repayment Plans*, FED. STUDENT AID, U.S. DEP'T EDUC., <https://studentaid.ed.gov/sa/repay-loans/understand/plans> (last visited Feb. 7, 2017).

116. *Private Student Loans*, *supra* note 107.

dent loans also offer deferment and forbearance options that most private student loans do not provide.<sup>117</sup> Deferral allows a borrower to enter a grace period of sorts for various pre-approved situations, like continuing schooling or, in some short-term periods, for hardship.<sup>118</sup> Forbearance is an option for borrowers with federal loans who do not qualify for deferral.<sup>119</sup> Most acceptable reasons for forbearance revolve around financial hardship, illness, and National Guard or teaching service.<sup>120</sup>

### C. Circuit Splits in the Case Law

In determining whether student loan debts impose an undue hardship on a debtor in light of her financial circumstances, federal district courts have essentially established two different tests.<sup>121</sup> The *Brunner* test was officially instituted in 1987 in an appeal from the U.S. District Court for the Southern District of New York, which held that the bankruptcy court erred in discharging the debtor’s student loans based on undue hardship.<sup>122</sup> The U.S. Court of Appeals for the Second Circuit affirmed the district court and adopted a three-part standard for determining undue hardship, requiring:

- (1) that the debtor cannot maintain, based on current income and expenses, a “minimal” standard of living for herself and her dependents if forced to repay the loans;
- (2) that additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans; and
- (3) that the debtor has made good faith efforts to repay the loans.<sup>123</sup>

The court in *Brunner v. New York State Higher Education Services Corp.* based this test on the reasonable interpretation of the legislative history, prior case law, and the original congressional intent behind the adoption of § 523(a)(8) to make discharge of “student loans more difficult than that of other nonexcepted debt.”<sup>124</sup> The court also reasoned that requiring evidence of current inability to pay *and* any exceptional circumstances demonstrating a continuing inability to repay in the future would more reliably justify the hardship as “undue.”<sup>125</sup>

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117. *Federal Versus Private Loans*, *supra* note 101.

118. *Deferment and Forbearance*, FED. STUDENT AID, U.S. DEP’T EDUC., <https://studentaid.ed.gov/sa/repay-loans/deferment-forbearance> (last visited Feb. 7, 2017).

119. *Id.*

120. *Id.*

121. *Compare* *Brunner v. N.Y. State Higher Educ. Servs. Corp.*, 831 F.2d 395, 396 (2d Cir. 1987) (per curiam), *with* *Long v. Educ. Credit Mgmt. Corp. (In re Long)*, 322 F.3d 549, 554–55 (8th Cir. 2003).

122. *Brunner*, 831 F.2d at 396.

123. *Id.*

124. *Id.*

125. *Id.*

Under the *Brunner* test, the debtor has the burden of proving “undue hardship” through evidence of exceptional present and future circumstances demonstrating an inability to repay the debts over an extended period of time.<sup>126</sup>

In *Brunner*, the debtor, Marie Brunner, was a single, able-bodied individual who failed to meet the burden of proving that undue hardship would result if her student loans were not discharged.<sup>127</sup> She failed to produce evidence tending to indicate a lack of job prospects, either currently or in the future.<sup>128</sup> The court also noted that she had graduated from college only ten months prior to the time of the hearing, which did not tend to prove that she was currently, and would continue to be, enduring exceptional circumstances that would make her unable to repay her student loans.<sup>129</sup> Even more telling was the fact that she had been repaying her student loans for only one month at the time she filed for discharge, meaning that she had made no attempt to defer or forebear her payments prior to requesting that the court discharge her debt completely.<sup>130</sup> The court affirmed the district court’s reversal of the discharge of her student loans and concluded “[s]uch conduct does not evidence a good faith attempt to repay her student loans.”<sup>131</sup>

The *Brunner* test has been adopted by the majority of bankruptcy and appellate courts across the country for determining undue hardship imposed by

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126. *Id.*

127. *Id.* at 396–97.

128. *Id.*

129. *Id.* at 397.

130. *Id.*

131. *Id.*

the non-dischargeability of student loans.<sup>132</sup> Not every circuit has been persuaded to adopt the *Brunner* test, however.<sup>133</sup> In 2003, the Eighth Circuit became the first circuit to reject the *Brunner* test for undue hardship determinations.<sup>134</sup> In *Long v. Educational Credit Management Corp.*,<sup>135</sup> the Eighth Circuit instead adopted a “totality-of-the-circumstances” test.<sup>136</sup>

In *Long*, the debtor, Nanci Long, filed for bankruptcy in 2000 after battling numerous health issues that ultimately pushed the debtor to quit her job.<sup>137</sup> Despite dutifully paying down her student loan debt for approximately ten

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132. See *Easterling v. Collecto, Inc.*, 692 F.3d 229, 235 (2d Cir. 2012) (per curiam) (holding that debtors must satisfy the *Brunner* test in order to prove student loan repayment imposes an undue hardship); *Lepre v. U.S. Dep’t of Educ.* (*In re Lepre*), 530 F. App’x 121, 123 (3d Cir. 2013) (per curiam) (“We, along with the majority of our sister courts, assess whether a debtor faces undue hardship by employing the three-pronged test set forth *Brunner v. New York Higher Education Services Corp.*, 831 F.2d 395 (2d Cir. 1987).”); *Spence v. Educ. Credit Mgmt. Corp.* (*In re Spence*), 541 F.3d 538, 542 (4th Cir. 2008) (adopting the *Brunner* test as it was adopted by the Fourth Circuit in *Educational Credit Management Corp. v. Frushour* (*In re Frushour*), 433 F.3d 393, 400 (4th Cir. 2005)); *Ostrom v. Educ. Credit Mgmt. Corp.* (*In re Ostrom*), 283 F. App’x 283, 285 (5th Cir. 2008) (per curiam) (“As the measure for ‘undue hardship’ in this context, we have adopted the test articulated in the Second Circuit’s decision in *Brunner v. New York State Higher Education Services Corp.*, 831 F.2d 395 (2d Cir. 1987).”); *Fields v. Sallie Mae Servs. Corp.* (*In re Fields*), 286 F. App’x 246, 247 (6th Cir. 2007) (“The Bankruptcy Code does not define ‘undue hardship,’ and, following this circuit’s precedent at the time, the bankruptcy court looked to the test announced in *Brunner v. New York State Higher Education Services Corp.*, 831 F.2d 395 (2d Cir. 1987), for guidance on this issue.”); *Tetzlaff v. Educ. Credit Mgmt. Corp.*, 794 F.3d 756, 758 (7th Cir. 2015) (“To determine which situations constitute an ‘undue hardship,’ we have adopted the *Brunner* test for student loan discharge proceedings . . . .”); *Hedlund v. Educ. Res. Inst. Inc.*, 718 F.3d 848, 851 (9th Cir. 2013) (“To determine if a debtor has shown undue hardship, we follow the three-part test from *Brunner*.”); *Roe v. Coll. Access Network* (*In re Roe*), 295 F. App’x 927, 929 (10th Cir. 2008) (“To evaluate whether an undue hardship exists, we adopted the three-part test articulated in *Brunner* . . . .”); *Wieckiewicz v. Educ. Credit Mgmt. Corp.*, 443 F. App’x 449, 451 (11th Cir. 2011) (per curiam) (“The Bankruptcy Code does not define ‘undue hardship,’ but we have adopted the standard set forth in *Brunner*, 831 F.2d at 396.”).

133. See *Long v. Educ. Credit Mgmt. Corp.* (*In re Long*), 322 F.3d 549, 553 (8th Cir. 2003); *Educ. Credit Mgmt. Corp. v. Jespersion*, 571 F.3d 775, 779 (8th Cir. 2009); *Nash v. Conn. Student Loan Found.* (*In re Nash*), 446 F.3d 188, 190 (1st Cir. 2006); *Bronsdon v. Educ. Credit Mgmt. Corp.* (*In re Bronsdon*), 435 B.R. 791, 798 (B.A.P. 1st Cir. 2010).

134. *In re Long*, 322 F.3d at 553.

135. *Id.* at 549.

136. *Id.* at 553 (citing *Andrews v. S.D. Student Loan Assistance Corp.* (*In re Andrews*), 661 F.2d 702, 704 (8th Cir. 1981)).

137. *Id.* at 551–52.



years, Ms. Long still owed \$76,000.<sup>138</sup> Based on these facts – as well as additional circumstances and Ms. Long’s financial information – the bankruptcy court discharged the debtor’s student loan debt owed to the Educational Credit Management Corporation (“ECMC”), finding that the debt would impose an undue hardship on the debtor, and the BAP affirmed the bankruptcy court’s determination.<sup>139</sup>

On appeal, the Eighth Circuit reviewed the BAP’s decision and rejected ECMC’s request that the court adopt the *Brunner* test for determining whether student loan debt imposed an undue hardship on a debtor requesting relief.<sup>140</sup> The court reaffirmed the analysis to be used in the Eighth Circuit to determine undue hardship as the totality-of-the-circumstances test set forth in *Andrews v. South Dakota Student Loan Assistance Corp.*<sup>141</sup> The Eighth Circuit, in adopting the totality-of-the-circumstances test, openly utilized a less restrictive test to determine undue hardship.<sup>142</sup> The court reasoned that any particular test would undermine the inherent discretion provided for in § 523(a)(8)(B) of the Bankruptcy Code.<sup>143</sup> In relying on the more flexible totality-of-the-circumstances test, the Eighth Circuit stressed the importance of examining the particular facts and circumstances that surround each bankruptcy situation.<sup>144</sup> In order to facilitate such an examination of facts and circumstances, the totality-of-the-circumstances test requires the bankruptcy court to consider: “(1) the debtor’s past, present, and reasonably reliable future financial resources; (2) a calculation of the debtor’s and her dependent’s reasonable necessary living expenses; and (3) any other relevant facts and circumstances surrounding each particular bankruptcy case.”<sup>145</sup>

More recently, the totality-of-the-circumstances test was favored in *Educational Credit Management Corp. v. Jesperson*.<sup>146</sup> In *Jesperson*, the debtor, Mark Jesperson, filed for bankruptcy, seeking a discharge of his student loan debt because it imposed an undue hardship on him.<sup>147</sup> The bankruptcy court concluded that Mr. Jesperson’s student loan debt imposed an undue hardship on him and discharged his debt.<sup>148</sup> The district court affirmed the bankruptcy court’s conclusion.<sup>149</sup> ECMC appealed the district court’s decision to the Eighth Circuit.<sup>150</sup>

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138. *Id.* at 552. Over \$61,000 of the debt was held by Educational Credit Management Corporation and was the sole debt in question on appeal. *Id.*

139. *Id.* at 551.

140. *Id.* at 553.

141. *Id.* at 554 (citing *In re Andrews*, 661 F.2d at 704).

142. *Id.* (citing *In re Andrews*, 661 F.2d at 704).

143. *Id.* (citing *In re Andrews*, 661 F.2d at 704).

144. *Id.* (citing *In re Andrews*, 661 F.2d at 704).

145. *Id.* (citing *In re Andrews*, 661 F.2d at 704).

146. 571 F.3d 775, 778 (8th Cir. 2009).

147. *Id.*

148. *Id.*

149. *Id.*

150. *Id.*

The Eighth Circuit cited *Long* in reaffirming its use of the totality-of-the-circumstances analysis; the court also acknowledged that while a majority of circuits have adopted the *Brunner* test, only the Eighth Circuit or the Supreme Court of the United States can resolve the conflicting approaches to undue hardship determinations.<sup>151</sup> The court of appeals reversed the district court and the bankruptcy court.<sup>152</sup> The court concluded that the bankruptcy court’s determination of undue hardship was based on clearly erroneous factual conclusions in Mr. Jesperson’s case.<sup>153</sup> The court found that Mr. Jesperson’s “young age, good health, number of degrees, marketable skills, and lack of substantial obligations to dependents or mental or physical impairments” established that his student loan debt did not impose an undue hardship.<sup>154</sup> The court also emphasized Mr. Jesperson’s failure to attempt to repay any of his \$304,463.62 student loan debt owed to ECMC, as well as his failure to even attempt to enroll in an Income Contingent Repayment Plan (“ICRP”), which would have limited his monthly installment payments on his debt in proportion with his monthly income and allowed for discharge of any debt still remaining after twenty-five years of regular payments.<sup>155</sup>

In addition to the Eighth Circuit’s departure from the *Brunner* test, the U.S. Court of Appeals for the First Circuit also distanced itself from the *Brunner* test in *Nash v. Connecticut Student Loan Foundation*.<sup>156</sup> In *Nash*, the debtor, Noreen Nash, sought the discharge of over \$140,000 in student loans.<sup>157</sup> The bankruptcy court concluded that the debtor failed to carry her burden of proof for a showing of undue hardship.<sup>158</sup> The bankruptcy court judge used a totality-of-the-circumstances approach but concluded that both this test and the *Brunner* test essentially required analyses of the same factors.<sup>159</sup> The U.S. District Court for the District of Massachusetts affirmed the bankruptcy court’s determination but elaborated further that the statutory language supported a totality-of-the-circumstances test as “the default standard for all judging.”<sup>160</sup> Ms. Nash appealed the district court’s decision to the First Circuit.<sup>161</sup>

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151. *Id.* at 779 n.1.

152. *Id.* at 778.

153. *Id.* at 779–83.

154. *Id.* at 780.

155. *Id.* at 781. The court also rejected the bankruptcy court’s conclusion that Mr. Jesperson’s failure to enroll in the ICRP option was not a factor to be considered in determining undue hardship because the ICRP failed to provide Mr. Jesperson with the “fresh start” that bankruptcy discharge is supposed to provide to debtors. *Id.* at 780.

156. 446 F.3d 188, 190 (1st Cir. 2006).

157. *Id.* at 189.

158. *Id.* at 190.

159. *Id.*

160. *Id.* (quoting *Nash v. Conn. Student Loan Found.*, 330 B.R. 323, 326–27 (D. Mass. 2005), *aff’d*, 446 F.3d 188).

161. *Id.* at 189.

On appeal, the First Circuit declined to make a determination on which undue hardship test it should adopt.<sup>162</sup> Instead, the court noted that “[u]nder any test assessing eligibility for discharge of student loan debt, [the debtor] must show that her current inability to maintain a minimal standard of living if forced to repay the debt will continue into the future.”<sup>163</sup> Based on Ms. Nash’s lack of evidence demonstrating the long-term prognosis of her disability, the court of appeals concurred with the bankruptcy court that she failed to meet her burden of proof of undue hardship.<sup>164</sup> The First Circuit concluded that based on either the *Brunner* test or the totality-of-the-circumstances test, Ms. Nash failed to prove by a preponderance of the evidence that the repayment of her loans would cause her undue hardship.<sup>165</sup>

More recently, in *Bronsdon v. Educational Credit Management Corp.*, the BAP for the First Circuit addressed the different undue hardship tests.<sup>166</sup> In *Bronsdon*, the debtor, Denise Bronsdon, sought to have her student loan debt discharged in her Chapter 7 bankruptcy proceeding because repayment imposed an undue hardship on her.<sup>167</sup> Analyzing Ms. Bronsdon’s claim under the totality-of-the-circumstances approach, the bankruptcy court determined that Ms. Bronsdon’s student loan debt imposed an undue hardship on her and discharged her loans.<sup>168</sup> The creditor, ECMC, appealed the bankruptcy court’s decision to the U.S. District Court for the District of Massachusetts.<sup>169</sup> The district court vacated the bankruptcy court’s decision and remanded the case to the bankruptcy court to consider “the impact that participation in the William D. Ford Federal Direct Loan Program . . . would have on the undue hardship analysis.”<sup>170</sup> The bankruptcy court concluded that her failure to participate in that program was not sufficient to overcome a finding of undue hardship and discharged Ms. Bronsdon’s student loans again.<sup>171</sup> ECMC again appealed, this time to the BAP for the First Circuit, arguing for the adoption of the *Brunner* test, which the bankruptcy court refused to endorse either time it reviewed Ms. Bronsdon’s case.<sup>172</sup>

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162. *Id.* at 190 (finding “no need in this case to pronounce [its] views of a preferred method of identifying a case of ‘undue hardship’”).

163. *Id.* at 192.

164. *Id.*

165. *Id.*

166. 435 B.R. 791, 797–800 (B.A.P. 1st Cir. 2010).

167. *Id.* at 793.

168. *Id.*

169. *Id.*

170. *Id.* at 793–94.

171. *Id.* at 794. The bankruptcy court found that even under the William D. Ford Federal Direct Loan Program, Ms. Bronsdon would not be required to make any monthly payments because her income is too low. *Id.* at 795. In addition, at the end of the repayment period, the forgiveness of her student loan debt would cause tremendous tax liability to Ms. Bronsdon, who is currently only surviving on Social Security. *Id.*

172. *Id.* at 797.

The BAP affirmed the bankruptcy court’s discharge of Ms. Bronsdon’s student loan debts based on the totality-of-the-circumstances test.<sup>173</sup> The court acknowledged that not only had the First Circuit previously declined to adopt either of the undue hardship tests in *Nash*, but the BAP for the First Circuit declined to adopt either test in several prior cases.<sup>174</sup> The court then went on to analyze the two tests and determine the differences between them.<sup>175</sup> The court concluded that, while the tests converge in many areas, “the *Brunner* test imposes two additional requirements on the debtor that *must* be met if the student loans are to be discharged.”<sup>176</sup> The court reasoned the *Brunner* test places too much weight on a demonstration of “extraordinary circumstances” in order to demonstrate the present and future undue hardship imposed by the debtor’s student loans.<sup>177</sup> In sum, the court concluded that “*Brunner* takes the test too far.”<sup>178</sup> Thus, following the totality-of-the-circumstances analysis, the BAP found that the bankruptcy court properly considered Ms. Bronsdon’s eligibility for the William D. Ford Federal Direct Loan Program as part of its totality-of-the-circumstances analysis and affirmed the discharge of Ms. Bronsdon’s student loan debt.<sup>179</sup>

These cases have begun to draw a line in the sand between these undue hardship tests. Even so, debtors continue to try to persuade the courts to change their analyses and their standards to help improve their chances of receiving a discharge of their student loan debt. Ms. Conway is one such debtor who attempted to persuade the Eighth Circuit to depart from the totality-of-the-circumstances test.

#### IV. INSTANT DECISION

The instant decision is based on almost six years’ worth of adversarial proceedings in the bankruptcy court regarding Ms. Conway’s outstanding student loan debts.<sup>180</sup> Ms. Conway received her Chapter 7 bankruptcy discharge in 2010, but the discharge did not include any of her outstanding student loan debt.<sup>181</sup> The bankruptcy court granted Ms. Conway’s motion to reopen her

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173. *Id.*

174. *Id.* at 797–98 n.9.

175. *Id.* at 798–99.

176. *Id.* at 799 (quoting *Hicks v. Educ. Credit Mgmt. Corp.* (*In re Hicks*), 331 B.R. 18, 26 (Bankr. D. Mass. 2005)).

177. *Id.*

178. *Id.* at 800. Specifically, the court found that the “good faith” requirement of the *Brunner* test is “without textual foundation.” *Id.* (quoting *In re Hicks*, 331 B.R. at 28).

179. *Id.* at 804.

180. *See Conway Bankr. Ct. I*, 489 B.R. 828, 830–33. (Bankr. E.D. Mo. 2013), *reversed and remanded*, 495 B.R. 416 (B.A.P. 8th Cir. 2013), *reversal aff’d*, 559 F. App’x 610 (8th Cir. 2014) (per curiam).

181. *Id.* at 830.

case to address the dischargeability of her student loans.<sup>182</sup> However, in its analysis, the court determined that Ms. Conway's student loans did not impose an undue hardship and therefore did not meet the requirements under the Bankruptcy Code to be dischargeable.<sup>183</sup> On appeal, the BAP reversed the bankruptcy court's ruling and found that the undue hardship analysis should be conducted on a loan-by-loan basis.<sup>184</sup>

NCT appealed the BAP decision to the Eighth Circuit, which affirmed the BAP and remanded the case to the bankruptcy court for an analysis of undue hardship on a loan-by-loan basis.<sup>185</sup> The bankruptcy court determined that eleven of Ms. Conway's fifteen student loans held by NCT imposed an undue hardship and discharged those eleven loans but found that the remaining four did not impose an undue hardship and denied the request to make them dischargeable as well.<sup>186</sup> Ms. Conway then appealed that decision to the BAP, arguing that the bankruptcy court attempted to inflate her income in order to impose undue hardship on her by disallowing the discharge of the remaining four student loans she had outstanding.<sup>187</sup>

In this appeal, the BAP reviewed the bankruptcy court's denial of a motion to amend the judgment with deference to the lower court, noting that such decisions will never be reversed absent a clear abuse of discretion.<sup>188</sup> The BAP found no such abuse of discretion in this case.<sup>189</sup> The BAP also addressed the issue of dischargeability of Ms. Conway's student loan debt, which is a question of law to be reviewed by the appellate court *de novo*.<sup>190</sup> Factual findings, however, are only to be reviewed by the appellate court for clear error.<sup>191</sup>

Ms. Conway's arguments on appeal in the instant decision revolved around the allegedly arbitrary timeline the bankruptcy court created to determine which, if any, of Ms. Conway's student loans imposed an undue hardship on her.<sup>192</sup> The bankruptcy court created a timeframe from which to determine

182. *Id.*

183. *Id.* at 836.

184. Conway B.A.P. I, 495 B.R. 416, 423–24 (B.A.P. 8th Cir. 2013), *aff'd*, 559 F. App'x 610 (8th Cir. 2014) (per curiam).

185. Conway 8th Cir., 559 F. App'x 610, 610 (8th Cir. 2014) (per curiam).

186. Conway Bankr. Ct. II, Ch. 7 Case No. 09-52394-399, Adv. No. 12-4033-659, slip op. at 6. (Bankr. E.D. Mo. Apr. 20, 2014), *aff'd*, 542 B.R. 855 (B.A.P. 8th Cir. 2015).

187. Conway B.A.P. II, 542 B.R. 855, 857 (B.A.P. 8th Cir. 2015).

188. *Id.* (first citing *Suggs v. Regency Fin. Corp.* (*In re Suggs*), 377 B.R. 198, 203 (B.A.P. 8th Cir. 2007); and then citing *Guy v. Danzig* (*In re Danzig*), 233 B.R. 85, 93 (B.A.P. 8th Cir. 1999)).

189. *Id.* at 859.

190. *Id.* at 857 (“The issue of dischargeability of student loans is a question of law, which we review *de novo*.”).

191. *Id.* (“A finding is clearly erroneous if, after examining the entire record, we are left with a definite and firm conviction that the bankruptcy court has made a mistake.”).

192. *Id.*

Ms. Conway’s monthly disposable income, using the most recent twelve-month period for which Ms. Conway had provided financial information, November 2013 through October 2014.<sup>193</sup> Ms. Conway argued that the court failed to consider additional pertinent events that affected the calculation of her disposable income, namely that she was laid off from one of her jobs two months after the court’s cut-off point.<sup>194</sup>

The BAP rejected Ms. Conway’s arguments regarding changes in her income, because in making post-discharge undue hardship determinations, the court relied on facts existing at trial that supported a finding of “reasonably reliable future financial resources.”<sup>195</sup> In making such determinations of fact, the court is required to examine the totality of the circumstances; however, the court is not authorized to base factual findings on speculation or estimates.<sup>196</sup> The BAP noted, “A decision on the dischargeability of student loan debt will nearly always be akin to a judicial version of ‘Whack-A-Mole’ because a debtor’s income and expenses are seldom static. Life is like that.”<sup>197</sup> The BAP pointed out that it had recognized Ms. Conway’s fluctuating income and expenses when viewed on a month-to-month basis but reasoned that her financial resources appeared more stable when viewed on a yearly basis.<sup>198</sup> It was for that reason, the court pointed out, that the BAP requested the bankruptcy court base its findings on Ms. Conway’s ability to repay individual loans over the course of an entire year.<sup>199</sup>

The court also emphasized the inherently subjective nature of dischargeability determinations and recognized that “[t]he courts are not equipped to revisit a nondischargeability determination every time a debtor’s circumstances change; to do so would wreak havoc with the concept of the finality of a court order.”<sup>200</sup> Ultimately, the court found that the bankruptcy court had properly reviewed a full year of Ms. Conway’s income and expenses and made a factual determination based on the most complete set of information provided by the parties.<sup>201</sup> Therefore, even though Ms. Conway felt that the remaining four student loans imposed a financial hardship on her, the bankruptcy court’s conclusion was not clearly erroneous, and thus it did not abuse its discretion.

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193. *Id.* at 856.

194. *Id.*

195. *Id.* at 858.

196. Walker v. Sallie Mae Servicing Corp. (*In re Walker*), 650 F.3d 1227, 1233 (8th Cir. 2011) (“[A] court may not engage in speculation when determining net income and reasonable and necessary living expenses.” (quoting Educ. Credit Mgmt. Corp. v. Jespersen (*In re Jespersen*), 571 F.3d 775, 780 (8th Cir. 2009))).

197. *Conway B.A.P. II*, 542 B.R. at 858.

198. *Id.*

199. *Id.*

200. *Id.*

201. *Id.* at 858–59.

## V. COMMENT

Ms. Conway's case provides an example of the complicated and often ambiguous analysis of student loan debt discharge under the Bankruptcy Code. Based on the vague statutory language and varying interpretations of both the statute and the tests created to address the statute, debtors across the United States are left entirely unsure and unprepared for what might happen to their outstanding student loan debt in bankruptcy. This Part examines further the two currently accepted tests used by courts across the country and ultimately concludes that, due to the inherently subjective nature of these types of facts-and-circumstances tests, they should be altogether rejected in favor of a bright-line rule in which only federal student loan debt remains non-dischargeable and private student loans become dischargeable in bankruptcy. Next, this Part looks to the characterization of student loans as non-dischargeable debts. This Part then presents a possible solution to the current circuit split and ambiguities of Congress's "undue hardship" analysis requirement. Finally, this Part looks forward to the implications involved in the creation of a bright-line rule for discharging student loan debt in bankruptcy.

A. *Facts-and-Circumstances Tests*

As written, § 523(a)(8) requires courts to create and adopt a facts-and-circumstances test in order to make undue hardship determinations. Facts-and-circumstances tests necessarily require the courts to factor in specific individual facts and circumstances of each debtor's case before them. This inherently creates inconsistent rulings across bankruptcy courts and jurisdictions.<sup>202</sup> Although individual facts and circumstances are never evaluated in a vacuum, the use of such inherently subjective tests leads to disparate results.<sup>203</sup>

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202. See Quixada Moore-Vissing, U. of N.H. Dep't of Educ., *Inconsistency in Judicial Interpretations of Undue Hardship: The Complications of Student Loan Discharge Through Bankruptcy* 10 (from the 29th Ann. Student Fin. Aid Res. Network Conf., June 15, 2012), [http://www.pellinstitute.org/downloads/sfarn\\_2012-Moore-Vissing\\_061512.pdf](http://www.pellinstitute.org/downloads/sfarn_2012-Moore-Vissing_061512.pdf); Ryan Freeman, Comment, *Student-Loan Discharge – An Empirical Study of the Undue Hardship Provision of § 523(a)(8) Under Appellate Review*, 30 EMORY BANKR. DEV. J. 147 (2013); Aaron N. Taylor, *Undo Undue Hardship: An Objective Approach to Discharging Federal Student Loans in Bankruptcy*, 38 J. LEGIS. 185 (2012).

203. See Rafael I. Pardo & Michelle R. Lacey, *Undue Hardship in the Bankruptcy Courts: An Empirical Assessment of the Discharge of Educational Debt*, 74 U. CIN. L. REV. 405, 487 (2005) ("Debtors whose claim of undue hardship was analyzed pursuant to the Brunner test received a discharge approximately 49% of the time, whereas debtors whose claim of undue hardship was analyzed pursuant to the totality test received a discharge approximately 46% of the time."); *but see* Jason Iuliano, *supra* note 11, at 497 (finding no statistically significant differences between outcomes in *Brunner* circuits and the Eighth Circuit).

Even within the limitations of judicial tests, like the *Brunner* test or the totality-of-the-circumstances test, the results that follow from facts-and-circumstance tests begin to look incongruent. For example, where one court may determine that a debtor with bipolar disorder faces an undue hardship in repayment of her student loans, another court may find that a second debtor with bipolar disorder who possesses other distinct facts and circumstances revolving around her life will be capable of repaying her student loans without undue hardship. No two bankruptcies are identical, and the courts are left weighing one debtor against another. The court in *Brunner* attempted to limit the inconsistencies in undue hardship analyses by creating a tripartite test for courts to apply to each demand for a discharge of student loans.<sup>204</sup> The court in *Long* also attempted to limit inconsistencies in its creation of the totality-of-the-circumstances test.<sup>205</sup> These two prevailing undue hardship tests have been adopted by all eleven circuits, nine following the *Brunner* test and two currently following the totality-of-the-circumstances test.<sup>206</sup>

The result is cases like *In re Conway*, where the bankruptcy court initially determined that, because Ms. Conway capably and intelligently represented herself, and therefore had the potential for more gainful employment, her student loan repayment would not impose an undue hardship on her.<sup>207</sup> Such a finding would seem to highlight the inconsistent effects these tests have when compared with a case like *Rose v. Department of Education*, where the bankruptcy court found that a licensed *pro se* attorney should have her student loan debt discharged in part due to her poor representation of herself in her own bankruptcy proceedings, which indicated to the court that gainful employment was not likely in the future.<sup>208</sup> In either case, many other factors were considered by the court, but it seems that courts also take into account the debtors’ presentations of themselves in court, which can be affected by personal perceptions and interactions with debtors and can cloud courts’ analyses of debtors’ other arguments and circumstances. Should our system really fall prey to such subjective notions and interpretations of intelligence, instead of limiting the analysis to factors like work history, accommodations, family circumstances, or disability?

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204. *Brunner v. N.Y. State Higher Educ. Servs. Corp.*, 831 F.2d 395, 396 (2d Cir. 1987) (per curiam).

205. *Long v. Educ. Credit Mgmt. Corp. (In re Long)*, 322 F.3d 549, 553 (8th Cir. 2003).

206. See *supra* note 132 and accompanying text for cases following the *Brunner* test. See *supra* note 133 and accompanying text for cases following the totality-of-the-circumstances test.

207. *Conway Bankr. Ct. I*, 489 B.R. 828, 836 (Bankr. E.D. Mo. 2013), *reversed and remanded*, 495 B.R. 416 (B.A.P. 8th Cir. 2013), *reversal aff’d*, 559 F. App’x 610 (8th Cir. 2014) (per curiam).

208. 215 B.R. 755, 765 (Bankr. W.D. Mo. 1997) (concluding that the debtor’s student loans should be discharged, in part, because the debtor’s *pro se* representation of herself in the case was so poor that the court highly doubted the debtor’s ability to procure “more lucrative employment in the foreseeable future”).



If facts-and-circumstances tests revolve around subjective analyses in order to make undue hardship determinations, why has Congress created this subjective system instead of creating a bright-line rule for student loan discharges? Clearly, the creation and passage of this section of the Bankruptcy Code was a reaction to a perceived injustice or loophole in the law.<sup>209</sup> But does such a subjective analysis, like the *Brunner* test and the totality-of-the-circumstances test that stemmed from the creation of § 523(a)(8), resolve the issues that Congress identified prior to the creation of the non-dischargeability of student loans? Is there a better place to draw the line?

Based on the analysis provided above, neither test adopted currently by the circuit courts provides a clear answer to the growing problem student loan debt has created in the United States. Rather than allowing courts across the country to continue to parse out the minor differences between two equally insufficient facts-and-circumstances tests, Congress should altogether reject a subjective facts-and-circumstances analysis and create a bright-line rule. In order to find a different standard for discharging student loans in bankruptcy, we must discuss the two major ways students can get student loans: federal student loan programs and private bank student loan programs.<sup>210</sup> Additionally, in order to determine if there exists a more consistent standard by which courts or Congress can determine the dischargeability of student loans, we must address the current statutory scheme and the social and economic implications of this system.

### B. Non-Dischargeable Debts

Debts excepted from discharge in bankruptcy are primarily based on some sort of wrongdoing on the part of the debtor.<sup>211</sup> As discussed in Part III, these include debts incurred by fraud or false representation, embezzlement, criminal restitution,<sup>212</sup> punitive damages,<sup>213</sup> and wrongful death damages where the debtor was intoxicated.<sup>214</sup> The other main category of non-dischargeable debts are those that implicate government resources, such as taxes, fines, and penalties,<sup>215</sup> and alimony and child support obligations,<sup>216</sup> which debtors' spouses and children often rely on for basic necessities.<sup>217</sup> In the mix with all these non-dischargeable debts are student loan debts – debts incurred for the lofty goal of continuing education and self-improvement.

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209. See *supra* Part III on the legislative history of § 523(a)(8).

210. *Private Student Loans*, *supra* note 107.

211. 11 U.S.C. § 523(a) (2012).

212. *Id.* §§ 523(a)(2)(A), 523(a)(4).

213. *Id.* § 523(a)(6).

214. *Id.* § 523(a)(9).

215. *Id.* §§ 523(a)(1), (14).

216. *Id.* §§ 523(a)(15), (5).

217. *Discharge, Exceptions to Discharge, and Objections to Discharge*, NAT'L BANKR. REV. COMM'N, <http://govinfo.library.unt.edu/nbrcreport/07consum.html> (last visited Feb. 7, 2017).

### C. *The Solution*

Federal student loans should remain non-dischargeable in bankruptcy because of their status as public debts, because they fall within the category of government resources, and because the U.S. Department of Education has created many alternative ways for borrowers to repay their loans. As previously discussed,<sup>218</sup> there are several federal student loan repayment plans and deferral options that allow the government to work with each individual borrower and provide a plan or system of repayment that they can actually afford each month. Additionally, while federal student loan caps have remained consistent since 2008 and were not amended prior to that since 1992,<sup>219</sup> private student loan interest rates have skyrocketed, in part because tuition costs across the country have substantially increased.<sup>220</sup> Additionally, most borrowers do not ever attempt to discharge their student loan debt, meaning that only a small portion of borrowers would attempt to get their federal loans discharged under an undue hardship analysis.<sup>221</sup>

Private student loans present a different problem. Private lenders set their own limits on how much to lend to any given student, and with so many possible options, it is possible for students to accumulate debt from multiple private lenders to finance their educations.<sup>222</sup> This can also lead to larger amounts of debt per student.<sup>223</sup> Take Ms. Conway, for example. At the time when she filed for Chapter 7 bankruptcy, she had approximately \$118,500 in private student loans and \$18,000 in federal student loans.<sup>224</sup> Her federal student loans were not even brought into her adversary proceeding when she requested discharge of her student loan debt.<sup>225</sup> Ms. Conway was enrolled in an income-based repayment plan for her federal loans that lowered her monthly payments

218. *See supra* Part III.

219. *Historical Loan Limits*, FINAID, <http://www.finaid.org/loans/historicallimits.phtml> (last visited Feb. 7, 2017).

220. *See* Kantrowitz, *supra* note 7 (“Student loan debt is increasing because government grants and support for postsecondary education have failed to keep pace with increases in college costs. This has shifted much of the burden of paying for college from the federal and state governments to families. The government no longer carries its fair share of college costs, even though it gets a big increase in income tax revenue from college graduates.”).

221. Jennifer Grant & Lindsay Anglin, Note, *Student Loan Debt: The Next Bubble?*, 32-DEC AM. BANKR. INST. J. 44, 87 (2013) (“[A] 2007 study found that of the 169,774 debtors in bankruptcy with student loan debt, only 217 filed an adversary proceeding in an effort to discharge their loans.”).

222. *Private Student Loan Lenders for 2017*, LENDEDU, <https://lendedu.com/blog/private-student-loans/> (last updated Feb. 1, 2017).

223. *A Look at the Shocking Student Loan Debt Statistics for 2017*, STUDENT LOAN HERO, <https://studentloanhero.com/student-loan-debt-statistics/> (last visited Feb. 7, 2017).

224. Conway B.A.P. I, 495 B.R. 416, 418 (B.A.P. 8th Cir. 2013), *aff’d*, 559 F. App’x 610 (8th Cir. 2014) (per curiam).

225. *Id.*

based on her annual income.<sup>226</sup> In contrast, Ms. Conway argued in her request for discharge of her private student loan debt that there was not any kind of income-contingent repayment option available to her on her private student loans.<sup>227</sup> Without any alternative repayment plans, Ms. Conway would probably be indebted to ECMC for the rest of her life, all for wanting to get an education.

Total student loan debt in the United States is estimated to be around \$1.2 trillion, with 95 percent of it being backed by the federal government.<sup>228</sup> If § 523(a)(8) were to be amended to make only private student loans dischargeable, it would thus only affect 5 percent of the current student loan debt nationally. In addition, making private student loan debt dischargeable in bankruptcy would take away the incentive for private lenders to use adjustable interest rates that are often more than double the federal interest rates.<sup>229</sup> Alternatively, making private student loan debt dischargeable would incentivize private lenders to be more stringent in their eligibility requirements, knowing that the loans are dischargeable, and may cause fewer people to qualify for loans with higher adjustable interest rates that end up costing the borrowers far more money in the long run. Non-dischargeable federal student loans also pose less of a hardship for borrowers because four out of the seven available repayment plans for federal loans provide for forgiveness of outstanding debt after a twenty- or twenty-five-year repayment period, meaning that the debt does not follow borrowers around for their entire lives if they can prove that they are unable to repay the full loan amount in fewer than twenty-five years.<sup>230</sup>

Economically, this makes sense: private lenders have no accountability for their high interest rates – currently, they are taking advantage of the system by charging interest rates to borrowers who really should not be taking out loans because the lenders know the loans they give out cannot be discharged in bankruptcy. Making private loans dischargeable would incentivize private lenders to be more stringent with their eligibility requirements and should greatly reduce the amount of loans private lenders would approve, knowing that their loans are now dischargeable.

#### D. Implications

There are important financial implications for debtors in drawing a line between federal student loan debt and private student loan debt. Particularly, differentiating between federal and private student loans superficially creates a

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226. *Id.* at 416 n.4.

227. *Id.*

228. John T. Harvey, *Student Loan Debt Crisis?*, FORBES (Apr. 28, 2014), <http://www.forbes.com/sites/johntharvey/2014/04/28/student-loan-debt-crisis/#771efea614d>.

229. For a comparison chart of available private student loans, see *Private Student Loans*, *supra* note 107.

230. *Interest Rates and Fees*, *supra* note 111.

disparity for debtors. For example, a single debtor with only private student loans who falls on hard times would have the option of discharging all of her student loan debt in her bankruptcy pleading. Whereas, a similarly situated debtor with only federal student loans would not have the option of discharging her student loan debt in a bankruptcy proceeding – instead, she would have to make payments and allow the debt to follow her around for twenty-five years before it could be forgiven. On its face, this seems to give preferential treatment to borrowers of private student loans. However, in many cases where a debtor is facing bankruptcy and where a debtor’s income is not sufficient to pay his or her debts, the same limited income would allow the debtor to take part in the alternative repayment plans offered for federal student loan debt, like income-based repayment or income-contingent repayment plans.<sup>231</sup>

Beyond the direct implications of discharging debt in bankruptcy, there are less obvious aspects of the discharge of debts that should be seriously considered when creating a standard for student loan debt discharge. Allowing student loan debt to be dischargeable in bankruptcy provides a very real benefit in its tax consequences. Generally speaking, when a debt is discharged or forgiven, it is ordinary income to the debtor at the time of the discharge.<sup>232</sup> If – as with most student loan debt – the amount of the debt that is discharged is fairly large, this treatment of debt forgiven as ordinary income can impose an enormous, unexpected tax burden on debtors. For example, currently, the average student loan debt for a Missouri resident is \$27,480 plus interest. Including this amount of money in income can create a tax burden for the debtor.<sup>233</sup> However, where a debtor is in need of having her student loan debts discharged, there is an exception to the inclusion of the discharged debt amount in income.

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231. *Id.* In many cases where a debtor’s income is so low that she is unable to repay all of her debts, her monthly installment payment on her federal student loans would be insignificant, if not zero dollars. In such cases, the debtor would be paying little to nothing on her debt for twenty-five years before the debt would be discharged. This would end up affecting borrowers of federal student loans in a similar fashion as borrowers of private student loans who declare bankruptcy and have their student loans discharged.

232. I.R.C. § 61(a)(12) (2012).

233. For example, suppose a single Missouri college graduate had \$27,480 in student loan debt and had an annual household income of \$48,173 (the median household income for a Missouri resident as of the 2010 U.S. Census in 2015 dollars). *Project on Student Debt: State by State Data*, INST. FOR C. ACCESS & SUCCESS, [http://ticas.org/posd/map-state-data#overlay=posd/state\\_data/2016/mo](http://ticas.org/posd/map-state-data#overlay=posd/state_data/2016/mo) (last visited Feb. 14, 2017); *Quick Facts: Missouri*, U.S. CENSUS BUREAU, <http://www.census.gov/quick-facts/table/INC110215/29> (last visited Feb. 14, 2017). In the taxable year that this debtor’s student loans were discharged, her taxable income would increase from \$44,000 to \$69,844 (\$44,000 + \$25,844). This would mean this debtor’s tax liability would increase from \$7235 to \$13,696. Our debtor would be liable for almost twice as much tax, even though she did not actually receive any additional income or money during that year.

Under § 108(a)(1)(B), if the debtor is insolvent<sup>234</sup> at the time the debt is discharged, the debtor does not have to include the discharged amount in income.<sup>235</sup>

Economists and politicians have been debating the causes and impacts of the rising student loan rates and outstanding debt for years.<sup>236</sup> Part of this debate has been a discussion of whether this “student loan crisis” will eventually resemble the housing bubble and its burst between 2007 and 2009.<sup>237</sup> An argument can be made that this proposal would make it harder to get out from under these student loan debts, and that this could accelerate the arrival of this looming issue. While this is a serious concern for our economy and the future of student loan accessibility, this proposal would not have that effect. There are three vital considerations to keep in mind supporting this proposal. First, while the amount of outstanding student loan debt has been dramatically increasing in recent years, the true “problem” many debtors face in trying to repay their student loan debt is the accruing of interest at high rates. Second, private lenders of student loans hold only approximately 5 percent of the outstanding student loan debt, however, they also appear more frequently in requests for discharge in bankruptcy proceedings.<sup>238</sup> This proposal only seeks to allow private loans to be dischargeable, which would not affect the majority of outstanding student loan debt. Third, the creation of a bright-line rule would reduce the cost of litigation in bankruptcy filings and proceedings; this would

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234. I.R.C. § 108(d)(3).

235. *Id.* § 108(a)(1)(B). Instead, there is a toll charge exacted from the debtor requiring her to reduce her basis in her tax attributes by the amount of the debt discharged that was excluded from income. *Id.* § 108(b). Under the code, the debtor’s tax attributes shall be reduced in the following order: net operating losses, general business credits, minimum tax credits, capital loss carryovers, the basis of the taxpayer’s property, passive activity loss and credit carryovers, and foreign tax credit carryovers. *Id.*

236. See Hayward, *supra* note 3; Mohamed A. El-Erian, Opinion, *The U.S. Education Bubble Is Now Upon Us*, MKT. WATCH (Nov. 9, 2015, 9:26 AM), <http://www.marketwatch.com/story/the-us-education-bubble-is-now-upon-us-2015-11-09>.

237. See William S. Howard, *The Student Loan Crisis and the Race to Princeton Law School*, 7 J. L. ECON. & POL’Y 485, 488 (2011) (“An eerie conceptual analogy to the student loan crises can be found in the American housing market in the first decade of the new millennium. The paradigms are: (1) specific identifiable market forces cause both the housing market and the higher education market to inflate faster than the ‘normal’ rate of inflation; (2) politicians respond by creating short-sighted programs that loan money to consumers who can then buy these “goods” at the inflated prices instead of identifying the inflation’s root causes; and (3) these programs inject excessive leverage into the markets and exacerbate the problem by turning the market’s homeostasis regulation mechanism into a vicious inflationary cycle.”).

238. In a cursory study of the eleven bankruptcy cases from across the country addressing student loan debt discharge examined in this Note, disputes over privately held student loan debt consisted of 81 percent of cases, or nine of the eleven, where disputes over federally funded student loans appeared in only 18 percent of these cases. See cases cited *supra* notes 132–33.

save debtors thousands of dollars spent disputing whether or not they can afford to pay these debts.

## VI. CONCLUSION

The use of subjective facts-and-circumstances tests in determining undue hardship leads to disparate results across the country for debtors attempting to escape their burdensome debts in bankruptcy. Congress’s inclusion of student loan debt as a non-dischargeable debt seems to imply a distrust of students as a whole, likening student loan debts to fraud, judgments for punitive damages, and back child support and alimony. When teens and young adults are strongly encouraged to pursue college degrees, whether by family, educators, or the present job market, penalizing attempts by students to fund their post-secondary education is an undue burden in and of itself. Rather than penalizing students for taking on loans to better themselves, especially using subjective tests for determining the undue hardship of such debt, Congress should provide a more transparent and objective standard by which debtors entering into the twists and turns of bankruptcy filings can expect some form of consistency in terms of discharge and treatment. One such way to provide a more transparent determination for treatment of student loan debt in bankruptcy discharge is by repealing the undue hardship requirement and creating a bright-line rule for the courts that distinguishes federal student loan debt from private student loan debt for courts to follow. While Congress should still work to reform the federal student loan programs, the creation of this bright-line rule will begin to furnish debtors with the fresh start the bankruptcy statutes were originally enacted to provide.

