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ARTICLES

RUNNING THE GAUNTLET OF “UNDUE HARDSHIP”—THE DISCHARGE OF STUDENT LOANS IN BANKRUPTCY

Janice E. Kosel*

The National Defense Education Act of 1958 established the National Defense Student Loan Program.¹ National Defense Student Loans (now known as National Direct Student Loans or NDSL's) are funded through annual appropriations by Congress. The funds are distributed to institutions of higher education which agree to match every nine dollars of federal funds with one dollar of their own.² An institution may make loans only to those students who demonstrate financial need.³ A student may borrow up to \$12,000 for undergraduate and graduate school, but no more than \$6,000 may be used for undergraduate studies.⁴ Repayment of NDSL's begins six months after the student ends study at the institution and may take up to ten years.⁵

A second major governmental endeavor, the Federal Insured Student Loan Program, was enacted as part of the Higher Education Act of 1965 and implemented by legislation in 1968 and

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1. 20 U.S.C. §§ 421-429 (1976). Education Amendments of 1972, Pub. L. No. 92-318, § 137(b), 86 Stat. 273, transferred current funding and other key provisions to the Higher Education Act of 1965, Pub. L. No. 89-329, 79 Stat. 1219 (codified in scattered sections of 20 U.S.C.). Recent modifications of relevant NDSL statutes appear at 20 U.S.C.A. §§ 1087cc-1087dd (Supp. 1980).

2. 20 U.S.C.A. 1087cc(a)(2) (Supp. 1980).

3. *Id.* § 1087dd(b).

4. *Id.* § 1087dd(a)(2).

5. *Id.* § 1087dd(c)(1)(A).

1969.⁶ Unlike NDSL's, Federal Insured Student Loans (known as FISL's) are not funded by the federal government. Rather, private lenders are encouraged to make student loans which are guaranteed by the federal government.⁷ Although a borrower need not formally demonstrate financial need, he or she cannot borrow more than the difference between educational costs and other financial aid.⁸ A student may borrow up to \$25,000 for graduate and undergraduate school, but no more than \$12,500 may be for undergraduate studies.⁹ Repayment of FISL's also begins six months after the student ends study at the institution and may take up to ten years.¹⁰

By 1972, Congress had become concerned with the default rates on both NDSL's and FISL's. It perceived an abuse of the programs when students sought to discharge all of their educational debts in bankruptcy shortly after graduation from college. To remedy that supposed abuse, a proposal was made which ultimately was enacted as section 523(a)(8) of the Bankruptcy Reform Act of 1978.¹¹ Henceforth, such student loans would be dis-

6. *Id.* §§ 1071 to 1087-3a.

7. S. REP. NO. 673, 89th Cong., 1st Sess. 43, reprinted in [1965] U.S. CODE CONG. & AD. NEWS 4027, 4061.

8. 20 U.S.C.A. § 1078(a)(2) (Supp. 1980).

9. *Id.* § 1075(a)(2).

10. *Id.* § 1077(a)(2)(B).

11. Section 4-506(a)(8) of the proposed Bankruptcy Act provided that an educational debt could not be discharged in bankruptcy if "the first payment of any installment thereof was due on a date less than five years prior to the date of the petition and if its payment from future income or other wealth will not impose an undue hardship on the debtor and his dependents." COMMUNICATIONS FROM THE EXECUTIVE DIRECTOR, COMM. ON THE BANKRUPTCY LAWS OF THE UNITED STATES TRANSMITTING A REPORT OF THE BANKRUPTCY COMM. ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. DOC. NO. 137, 93d Cong., 1st Sess. Pt. II, at 140 (1973) [hereinafter cited as REPORT ON THE BANKRUPTCY COMMISSION]. While the proposed Bankruptcy Act continued to undergo revision, the essence of that section was enacted as section 439A of the Higher Education Act of 1975, effective Oct. 1, 1977. 20 U.S.C. § 1087-3 (1976).

Section 439A of the Higher Education Act was repealed as of the date of the enactment of the Bankruptcy Reform Act, Nov. 6, 1978. The effective date of the Bankruptcy Reform Act was Oct. 1, 1979. For an eleven-month period between the date of enactment of the Bankruptcy Reform Act on Nov. 6, 1978 and its effective date on Oct. 1, 1979, there would be no federal statute providing for the nondischargeability of student loans. To remedy this inadvertent gap, a new section was added to the Bankruptcy Code by Act of Aug. 14, 1979, providing for the nondischargeability of student loans for a period of five years after they become due absent a showing of undue hardship. Pub. L. No. 96-56, 43 Stat. 387 (codified at 11 U.S.C. § 523(a)(8) (Supp. III 1979)). For a discussion of the dischargeability of student loans between Nov. 6, 1978 and Aug. 1979, see *Georgia Higher Educ. Assistance Corp. v. Broughton*, 6 Bankr. Rep. 1011 (N.D. Ga. 1980).

chargeable in bankruptcy only if "such loan first became due before five years . . . before the date of the filing of the petition; or . . . excepting such debt from discharge . . . will impose an undue hardship on the debtor and the debtor's dependents" ¹²

This Article will first examine the legislative history of that provision and then review the case law implementing and interpreting the undue hardship exception.¹³ It is the author's thesis that the absence of a single coherent legislative theory for the nondischargeability of student loans has inevitably led to a number of disparate judicial interpretations.

Regardless of the underlying rationale, a survey of the case law indicates that the courts have interpreted the undue hardship exception quite stringently. Generally, they have discharged student loans only if the debtor can scarcely maintain a minimal lifestyle after prudent allocation of income and employment effort. Even this hard line approach ignores the undue hardship exception already built into the student loan program—the ability of the administrator to grant unlimited forbearance in the event of financial distress.¹⁴ In light of this second undue hardship exception, it is difficult to envision any circumstances in which a student loan should be discharged. Yet a number of discharges have been granted.

Legislative revision of section 523(a)(8) is essential, not simply to give a consistent meaning to that provision, but to ensure

12. 11 U.S.C. § 523(a)(8) (Supp. III 1979).

13. A number of sanctions have been imposed on the student loan debtor who files bankruptcy that are beyond the scope of this Article. See, e.g., Comment, *Skipping Out on Alma Mater: Some Problems Involving the Collection of Federal Student Loans*, 15 COLUM. J.L. & Soc. PROB. 317 (1980) (denial of transcripts, additional student aid, enrollment at former institution, and admission to the bar); Comment, *A Fresh Start through Bankruptcy: Fact or Frustration for the Student Loan Debtor*, 2 U. PUGET SOUND L. REV. 365 (1979) (denial of transcript); *In re Wave*, 9 Bankr. Rep. 24 (W.D. Mo. 1981) (denial of transcript is an illegal collection effort under section 362(a)(1) of the new Bankruptcy Code); Application of Gahan, 279 N.W.2d 826 (Minn. 1979) (upholding denial of admission to the bar not because of the bankruptcy filing but on the basis of the applicant's moral character as reflected in his lack of financial responsibility and his default on the student loans prior to the filing); *Girardier v. Webster College*, 563 F.2d 1267 (8th Cir. 1977) (private school's refusal to issue a transcript because of failure to pay student loans discharged in bankruptcy is a legal means of inducing debtor to make payment under the Bankruptcy Act).

14. 20 U.S.C. § 1080(c) (1976).

the fulfillment of a societal goal greater than the bankruptcy objective of a fresh start for the individual debtor—namely, the maintenance of educational loan programs for future generations of students. In order to facilitate that objective, student loans should be nondischargeable in bankruptcy regardless of the debtor's circumstances.

I. THE LEGISLATIVE HISTORY OF SECTION 523(a)(8) OF THE BANKRUPTCY REFORM ACT

The legislative history of the Bankruptcy Reform Act of 1978 does not clearly refer to the rationale underlying the enactment of section 523(a)(8), but the Senate Report does indicate an intent to follow prior law.¹⁵ Turning then to its predecessor, the purpose of section 439(A) of the Higher Education Act of 1975¹⁶ was explained as follows:

The amendment was adopted in the light of testimony that the bankruptcy rate involving student loans has increased significantly in the last several years and that in some areas of the country students are being counseled on filing for bankruptcy to discharge their obligations to repay guaranteed student loans.

The Committee notes that in most circumstances a student may leave school with several thousand dollars in student loans and no assets, thereby making the student technically eligible to declare bankruptcy. The amendment, by waiting five years, would offer a more realistic view on the student's ability to repay a student loan.¹⁷

Thus, the articulated purpose of this legislation was to prevent a specific abuse, the filing of bankruptcy shortly after graduation for the primary purpose of discharging student loans. Proponents of the legislation produced statistics compiled by the Office of Education showing a rapid and dramatic increase in the incidence of student loan bankruptcies.¹⁸ As one member of Congress noted: "I feel certain that a problem has been identi-

15. "[It] follows generally current law and excerpts [sic] from discharge student loans until such loans have been due and owing for five years." S. REP. No. 989, 95th Cong., 2d Sess. 79, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5787, 5865.

16. 20 U.S.C. § 1087-3 (1976).

17. H.R. REP. No. 1232, 94th Cong., 2d Sess. 13-14 (1976).

18. The statistics demonstrate the rise in student loan bankruptcies.

fied, a problem of serious proportions and consequence, but one which has not yet reached catastrophic or crippling magnitude. Now is the time to act to prevent it from becoming so."¹⁹

The Congressman's fears for the future were based on two factors. Increasing numbers of students had taken out loans over the past decade so that the total dollar impact on the student loan program of even a constant rate of bankruptcy filings would increase dramatically.²⁰ Moreover, in all likelihood the incidence of student loan bankruptcy filing would continue its geometric ascent. The moral stigma attached to bankruptcy was apparently on the decline. And the incidence of bankruptcy in federally administered student loan programs was not yet as high as that in state-run programs "due in large part to the lack of pursuit of defaulters. When the pressure to meet obligations begins to be applied in the Federal programs, I think it is safe to predict a dramatic rise in bankruptcy filings in that program also."²¹

In reference to statistics marshaled by the Office of Education, the Congressman confidently stated that "this is clear evidence of improper use of the Federal bankruptcy law with re-

STUDENT LOAN BANKRUPTCIES

| <i>Fiscal Year</i> | <i>Number of Claims</i> | <i>Dollar Amount</i> |
|--------------------|-------------------------|----------------------|
| 1966-1970 | 348 | .4 million |
| 1972 | 1342 | 1.6 million |
| 1974 | 2914 | 3.8 million |
| 1975 | 4559 | 6.8 million |

| <i>Fiscal Year</i> | <i>Percentage Increase of Personal Bankruptcies</i> | <i>Percentage Increase of Student Loan Bankruptcies</i> |
|--------------------|---|---|
| 1973-1974 | 8.4 | 29.2 |
| 1974-1975 | 32.9 | 59.9 |

*Bankruptcy Act Revision: Hearings on H.R. 31 and H.R. 32 Before the Subcomm. on Civil and Constitutional Rights, 94th Cong., 1st & 2d Sess. 1072-73 (statement of Edward T. York, Jr.) and 1095 (statement of Sheldon Steinbach) (Jan. 29, 1976) [hereinafter cited as *Hearings*].*

19. *Id.* at 1091 (testimony of Representative John N. Erlenborn).

20. *Id.* at 1095 (statement of Sheldon Steinbach). Annual expenditures for NDSL's had increased from 40 million in fiscal year 1960 to 345 million in fiscal year 1975. Annual expenditures for FISL's had increased from 29 million in fiscal year 1968 to 334 million in fiscal year 1975. American Statistical Index, Digest of Education Statistics, 4564-1, at 172 (1979).

21. *Hearings, supra* note 18, at 1088 (statement of Representative John N. Erlenborn).

spect to the discharge of Federally guaranteed student loans."²² Others were not so easily convinced. Indeed, the legislative history is replete with statistics justifying their skepticism. Focusing solely on percentage increases in bankruptcy filings had led to a misconception of the nature and extent of the current problem. Although \$17 million had been paid on guaranteed student loan bankruptcy claims during fiscal years 1969-1975, over \$7 billion had been loaned during that period.²³ Only two-tenths of one percent of the loans made, involving less than three-tenths of one percent of the dollars loaned, had been discharged in bankruptcy.²⁴ As one bankruptcy judge concluded, "bankruptcy losses do not appear to present any great threat to the [student loan] program."²⁵

Indeed, the type of bankruptcy abuse specifically contemplated by Congress was virtually nonexistent. Less than one student borrower in two hundred had declared bankruptcy.²⁶ The specific abuse Congress sought to prevent could be inferred only from that small fraction of these bankruptcy filings where educational loans were the predominant debt.²⁷ In sum, apart from a few well publicized horror stories,²⁸ there was little evidence to suggest that the overwhelming majority of student loan bankruptcies were anything but legitimate.

No data exists describing the situation of those declaring bankruptcy. How many of those former students completed their education and received their degrees? How many were employed when

22. H.R. REP. NO. 595, 95th Cong., 1st Sess. 157 (1977).

23. *Hearings, supra* note 18, at 981 (statement of Clive W. Bare) (Dec. 10, 1975).

24. H.R. REP. NO. 595, 95th Cong., 1st Sess. 161 (1977).

25. *Hearings, supra* note 18, at 981 (statement of Clive W. Bare) (Dec. 10, 1975).

26. H.R. REP. NO. 1232, 94th Cong., 2d Sess. 74 (1976).

27. A survey conducted by the General Accounting Office indicated that in approximately 20% of the bankruptcy cases involving guaranteed student loans, over 80% of the debtor's total indebtedness was attributable to educational loans. H.R. REP. NO. 595, 95th Cong., 1st Sess. 133 (1977). A random sample analyzed by the Comptroller General of student loan borrowers who petitioned for bankruptcy indicated that educational debts averaged only \$4,138 of \$14,115 total unsecured debts—less than 30%. *Id.* at 139. Only 35% of student loan borrowers who petitioned for bankruptcy scheduled educational debts accounting for 60% or more of their nonpriority unsecured debts. *Id.* at 144.

28. The classic example was a Stanford University student who secured student loans in order to obtain an undergraduate degree in business, a master's degree in engineering, and a law degree. Two weeks after leaving school he filed a bankruptcy petition listing a total indebtedness of \$17,275—all in student loans. *Hearings, supra* note 18, at 1073-74 (statement of Edward T. York, Jr.).

they filed for bankruptcy, and for how long? How many felt obligated to take out student loans they didn't originally want, or in amounts greater than thoughtful credit counseling would have advised? How many found work, but in occupations far removed in form and earning power from their mortgaged educational careers?²⁹

Opposition to the nondischargeability provision was widespread.³⁰ One critic denounced the proposal to alter the dischargeability of student loans as "a discriminatory remedy for a 'scandal' which exists primarily in the imagination."³¹ Another condemned the proposal as "a serious allegation against a whole generation."³² "Treating students, all students, as though they were suspected frauds and felons is no substitute for improving the administration of the program."³³

The exception to discharge for student loans was viewed by critics as contrary to one of the most basic principles of bankruptcy law—equality of treatment for all debts and creditors.

[I]t treats educational loans precisely as the law now treats loans incurred by fraud, felony, and alimony dodging. *No other legitimately contracted consumer loan, applied to a legitimate undertaking [sic], is subjected to the assumption of criminality which this provision applies to every educational loan.* . . . [I]t is a direct, unmitigated, slap in the face of every single student borrower in the nation. It assumes that borrower's bad intentions, and deprives him of a right that every other citizen has available to him if he

29. H.R. REP. NO. 595, 95th Cong., 1st Sess. 161 (1977).

30. Among the opponents were the House Judiciary Committee, American Bankers Association, Consumer Bankers Association and National Student Lobby. H.R. REP. NO. 595, 95th Cong., 1st Sess. 132-33 (1977).

31. H.R. REP. NO. 1232, 94th Cong., 2d Sess. 73 (1976) (statement of Representative James G. O'Hara).

32. *Hearings*, *supra* note 18, at 1096 (testimony of Sheldon Steinbach, comment by Representative Don Edwards).

33. H.R. REP. NO. 1232, 94th Cong., 2d Sess. 77 (1976) (statement of Representative James G. O'Hara). Debts procured by fraud and criminal penalties are nondischargeable. 11 U.S.C. §§ 523(a)(2)(A), 523(a)(7). Relatively few cases have analyzed educational loans as debts obtained through false pretenses. *See, e.g., Oregon v. Mwongozi*, 4 Bankr. Ct. Dec. 120 (D. Ore. 1978) (decided under former Bankruptcy Act of 1898 § 17(a)(2) [11 U.S.C. § 35(a)(2) (1976)]).

needs it.³⁴

Proponents responded that educational loans are in fact different from most loans, and therefore merit special treatment. Conventional loans typically are made on the basis of a financial analysis of the borrower, his or her assets, and present income. Conventional lenders frequently require security or a cosigner to guarantee repayment of the debt. In contrast, student borrowers rarely have present income or property and their educational loans are neither cosigned nor secured. In a sense, student loans represent a mortgage on the debtor's future because they are based on the supposition that the loan will be paid from future earnings attributable to the debtor's education. Although secured debts are dischargeable in bankruptcy, the debtor must forfeit the collateral; in order to keep the property, the debtor must reaffirm the debt.³⁵ Because student loan debtors cannot surrender an intangible asset like an education, they have no choice; they must commit future earnings to the repayment of student loans.

Moreover, proponents argued, nondischargeability of particular types of debts in bankruptcy was not without precedent. For example, taxes are not dischargeable until three years after they first become due.³⁶ One commentator has written that the philosophical basis for the exception to discharge for taxes is the high moral claim of the government as the representative of the public.³⁷ That policy applied equally well to student loans. "When something is wrong with or threatens the Federally Insured and Guaranteed Student Loan Programs, immediate and thoughtful attention must be given lest we run the risk of losing or impairing the efficiency of key ingredients in our system of financing higher education."³⁸ Later, a court would more clearly articulate the political and practical objectives behind the nondischargeability of student loans—"the preservation of a program that benefits many thousands of borrowers which, if eliminated, would leave students with virtually no institutional

34. H.R. REP. NO. 1232, 94th Cong., 2d Sess. 75 (1976) (emphasis in original).

35. 11 U.S.C. §§ 506, 722 (Supp. II 1978).

36. *Id.* § 523(a)(1).

37. 1 D. COWANS, BANKRUPTCY LAW AND PRACTICE § 242 (2d ed. 1978).

38. *Hearings*, *supra* note 18, at 1087 (statement of Representative John N. Erlenborn).

source of borrowable funds.' ”³⁹

In the end, of course, the proponents of the amendment prevailed. Congress voted to make student loans nondischargeable until five years had elapsed from the date the educational loan first became due. The five year moratorium was apparently selected on the basis of both factual and equitable considerations. Statistics indicated that the average time which elapsed between the last student loan and the bankruptcy filings ranged between thirty months⁴⁰ and forty-one months.⁴¹ Moreover, bankruptcies occurring after the five year period did not have the same indicia of abuse. If payment were not made within that time period, it was more likely that the educational loan had not materially contributed to the increased income stream; because the promise of higher education was unfulfilled, it seemed more appropriate to forgive the debt.

In effect, the moratorium was intended to operate as a presumption that any bankruptcy filed within five years was done with the primary purpose of discharging a student loan. No provision was made for the direct rebuttal of that presumption of abuse. Instead, in order to alleviate the concern that the amendment would unduly impair the traditional goal of bankruptcy—a fresh start for the debtor—provision was made for the dischargeability of student loans if “undue hardship on the debtor and his dependents would otherwise result.”

The undue hardship exception was clearly a compromise measure. It provoked little comment in the legislative history. Reflecting on the diverse concerns expressed by his colleagues, one member of Congress voiced the belief that “this provision . . . will enable referees to distinguish between individuals who have contrived to secure an unjust enrichment through the operation of the bankruptcy law and those who have realistically

39. *In re Payton*, BANKR. L. REP. (CCH) ¶ 67,073 (E.D. Tenn. Nov. 3, 1978). In *Payton*, the court rejected the argument that the provision for nondischargeability of student loans violated the equal protection clause because it was rationally related to the achievement of that legitimate governmental purpose.

40. This figure was derived from a June 1975 random survey of guaranteed student loan bankruptcies under the New Jersey State Guarantee Loan Program. *Hearings*, *supra* note 18, at 1074 (statement of Edward T. York, Jr.).

41. This figure was derived from an analysis of student loan bankruptcies conducted by the Comptroller General. H.R. REP. NO. 595, 95th Cong., 1st Sess. 142 (1977).

fallen on hard times and who deserve the benefits of the general 'fresh start' policy of the act."⁴² Of necessity, that distinction has been made, but in a different manner by each bankruptcy judge who has confronted the issue. For, as the court noted in *Georgia Higher Education Assistance Corporation v. Bell*,⁴³ "the legislative history is . . . of little assistance in determining the underlying rationale of the exception to discharge for the purpose of applying it to facts clearly within its scope."⁴⁴

II. JUDICIAL INTERPRETATION OF "UNDUE HARDSHIP"

A. DISPARATE CRITERIA FOR THE DISCHARGE OF STUDENT LOANS *Extraordinary Hardship*

Focusing on the word "undue," the courts have consistently required a showing of economic difficulty that is not common to all recent graduates.⁴⁵ Repayment of student loans almost always imposes an immediate hardship on the debtor. The debts of recent graduates generally vastly outnumber their assets. Yet a simple comparison of assets and liabilities is misleading, for it ignores a prime factor, earning power. Over time, an increased earning capacity will normally be generated to alleviate that temporary hardship. If the former student has secured employ-

42. *Hearings*, *supra* note 18, at 1095 (statement of Sheldon Steinbach).

43. 5 Bankr. Rep. 461 (N.D. Ga. 1980).

44. *Id.* at 462. One commentator has attempted to fathom the legislative rationale and thereby provide guidance for the implementation of the undue hardship exception. Ahart, *Discharging Student Loans in Bankruptcy*, 52 AM. BANKR. L.J. 201 (1978).

45. *See, e.g.*, Massachusetts Higher Educ. Assistance Corp. v. Packer, 9 Bankr. Rep. 884 (D. Mass. 1981); Georgia Higher Educ. Assistance Corp. v. Bell, 5 Bankr. Rep. 461, 463 (N.D. Ga. 1980); New York State Higher Educ. Assistance Corp. v. Brock, 4 Bankr. Rep. 491, 494 (S.D.N.Y. 1980); New York State Higher Educ. Assistance Corp. v. Kohn, 5 Bankr. Ct. Dec. 419 (S.D.N.Y. 1979). These cases are consistent with the legislative history. "That which affects the group generally is not considered an undue hardship." *Hearings*, *supra* note 18, at 1092-93 (statement of Representative John N. Erlenborn).

Under § 4-506(a)(8) of the proposed Bankruptcy Act, the burden was on the creditor to show that denial of discharge would not impose an undue hardship on the debtor. REPORT ON THE BANKRUPTCY COMM., *supra* note 11, at 136 (1973). However, the legislative history indicates that the provision as enacted in § 523(a)(8) was intended to be self-executing; that is, the creditor is not required to file a complaint to determine nondischargeability of a student loan. S. REP. NO. 989, 95th Cong., 2d Sess. 79, *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5787, 5865. *But see* University of Alabama v. Wright, 7 Bankr. Rep. 197, 200 (N.D. Ala. 1980) (emphasis in original), suggesting "that the burden is on the creditor to show that the loan first became due before five years before the date of filing the bankruptcy petition. Otherwise the loan is presumed discharged."

ment in the field of endeavor for which he or she is trained and there is a reasonable probability that income will increase in the future, present hardship is neither unique nor unexpected. Confronted by this situation in *Bell*, the court noted that "[w]hile the debtor's budget will undoubtedly be tight for the foreseeable future, that is a common rather than an undue hardship."⁴⁶ If there are no factors which indicate that the bankrupt's plight differs from the great majority of student loan debtors, the undue hardship discharge will be denied.

Self-Imposed Hardship—Maintenance of a Minimal Lifestyle

In other cases, while the debtor's economic straits may be more severe than those of most student loan debtors, that situation is due to circumstances well within the debtor's control. Future repayment difficulties may have been engendered by voluntary reaffirmation of debt,⁴⁷ unwise purchases,⁴⁸ other improvident expenditures,⁴⁹ or even laziness and obesity.⁵⁰ If the

46. *Georgia Higher Educ. Assistance Corp. v. Bell*, 5 Bankr. Rep. 461, 463 (N.D. Ala. 1980).

47. See, e.g., *In re Hayes*, BANKR. L. REP. (CCH) ¶ 67,065 (W.D. Wis. Mar. 2, 1979) (debtor reaffirmed a debt secured by a second car; monthly payments on the car were \$118 while the minimum payment on federally insured student loans would be approximately \$53 per month), and *Vermont Student Assistance Corp. v. Ewell*, 1 Bankr. Rep. 311, 313 (D. Vt. 1979) (debtor reaffirmed a debt of \$3,750 to a credit union holding a security interest in a car worth \$1,000 because his wife was fond of the vehicle and wanted to retain it).

48. See, e.g., *Hayman v. Wilmington Trust Co.*, 4 Bankr. Ct. Dec. 932 (S.D. Fla. 1978) (debtor incurred monthly payments of \$88 on a car purchased after filing bankruptcy).

49. See, e.g., *Price v. United States*, 1 Bankr. Rep. 768, 769 (D. Haw. 1980) (debtor sent her three children to private school at a tuition of \$2,700 per year); *In re De Angelis*, BANKR. L. REP. (CCH) ¶ 67,082 (E.D. Pa. Mar. 20, 1979) (the fact that the debtor's rental expenses absorbed a substantial portion of her monthly income because she preferred "the advantages of a better neighborhood over a more budget-conscious lodging" was not taken into account in determining hardship); *In re Townsend*, BANKR. L. REP. (CCH) ¶ 67,140 (E.D. Pa. Dec. 18, 1978) (debtor made contributions to various churches of \$75-100 monthly while the state would agree to accept monthly payments of only \$10-20 on the student loans).

50. See, e.g., *United States v. Conard*, 6 Bankr. Rep. 151, 152 (W.D. Ky. 1980). Debtor described himself as "overweight" and testified that his physical appearance "turns off a lot of people." The court denied a hardship discharge, noting that corpulence is a condition which may swiftly diminish with continued impecuniosity.

Enlightened self-interest would seem to suggest the virtue of a vigorous and energetic search for a proper workshop in which to use those intellectual tools which have been well

debtor had exercised greater prudence, the money for the repayment of student loans would have been available. When confronted by debtor extravagance, the courts have consistently denied the undue hardship discharge. Their rationale was clearly stated by the court in *Hayman v. Wilmington Trust Company*.⁵¹ "The discretion given this court to permit discharge during those first five years to prevent 'undue hardship on the debtor and his dependents' is not intended to shelter the bankrupt from self-imposed hardship from a reluctance to live within his means."⁵² Or, as the court rather bluntly noted in *Vermont Student Assistance Corporation v. Ewell*,⁵³

[t]he process of rehabilitation entails the exercise of prudence on the part of the debtor. He must not cast caution to the winds. Unfortunately, the bankrupt failed to take heed. . . . [T]he money required to pay off . . . [the car] could have very well been used in the future to pay off part of the student loan. This in itself would tend to deprive him of the protection of "undue hardship".⁵⁴

Although phrased somewhat moralistically, the position adopted by the courts appears to coincide with the legislative intent to discharge student loans only in exceptional circumstances. Modest inconvenience occasioned by personal lifestyle choices is not undue hardship. Discharging student loans in such circumstances would reward extravagance and penalize frugality.

In all other cases of alleged undue hardship, the consensus of the courts has broken down, precisely because of the ambigu-

honed at federal expense. Productivity is preferable to living off the substance of the land.

Id. at 153.

In *Virginia Educ. Loan Auth. v. Archie*, 7 Bankr. Rep. 715 (E.D. Va., 1980), the debtor left school prior to receiving a degree because she was depressed and had a very low self-esteem due to an obesity problem. She had a surplus of income over expenses of \$37.13, even though she had extraordinarily high telephone bills and clothing expenses, and planned to expend funds on a weight reduction program. The court denied the undue hardship discharge, seeing no reason why under careful budgeting the debtor would not be able to repay the student loans. *Id.* at 718-19.

51. 4 Bankr. Ct. Dec. 932 (S.D. Fla. 1978).

52. *Id.* at 933. The debtor had a total indebtedness of \$3,957. Student loans comprise \$2,600 of this total. *Id.* at 932.

53. 1 Bankr. Rep. 311 (D. Vt. 1979).

54. *Id.* at 313. The debtor scheduled student loans of \$8,400 and other debts of \$4,650, including an obligation of \$3,750 which he reaffirmed. *Id.* at 312-13.

ity of the legislative history. As one judge noted:

It is regrettable that Congress shed so inadequate a spotlight on the exculpating phrase "undue hardship". What can be gleaned is that the hardship is to be found in the exceptional case and must be based on something more than inability to pay. It is also regrettable that so much is therefore left to the individual view of each judge who, after all, brings the sum of who and what he was, who he has become, and what he sees through his own eyes to this basically disagreeable task.⁵⁵

A majority of courts generally have been sympathetic in finding undue hardship to exist where unexpected difficulties triggered the debtor's financial problems. In so doing, they have relied to a great extent on the absence of the specific abuse highlighted in the legislative history. Moreover, as one member of Congress pointedly observed: "This requirement recognizes that in some circumstances the debtor, because of factors beyond his reasonable control, may be unable to earn an income adequate both to meet the living costs of himself and his dependents and to make the educational debt payments."⁵⁶

The present and potential hardship, however, must be of exceptional degree to conform to the guidelines articulated in a communique from the Bankruptcy Commission.

In order to determine whether nondischargeability of the debt will impose an undue hardship on the debtor, the rate and amount of his future resources should be estimated reasonably in terms of ability to obtain, retain, and continue employment and the rate of pay that can be expected. Any unearned income or other wealth which the debtor can be expected to receive should be taken into account. The total amount of income, its reliability, and the periodicity of its receipt should be adequate to maintain the debtor and his dependents, *at a minimal standard of living* within their management capability as well as

55. *New York Higher Educ. Serv. v. White*, 6 Bankr. Rep. 26, 29 (S.D.N.Y. 1980) (citation omitted).

56. REPORT ON THE BANKRUPTCY COMM., *supra* note 11, at 140.

to pay the educational debt.⁵⁷

Unforeseen Circumstances

Most courts have applied the standard of the Bankruptcy Commission quite stringently, focusing on the nature of the scheduled debts and the circumstances that led to the filing of the petition, as well as the debtor's prospective ability to maintain a "minimal" standard of living following the discharge of other debts in bankruptcy. Thus, an undue hardship discharge was granted to student loan debtors in the following rather classical hardship circumstances:

—The debtor's wife had contracted a rare disease which had generated major medical bills and had made impossible her present, and perhaps future, employment. The debtor's take home pay was less than the family needed for living expenses. He had no real or personal property of any consequence. The court determined that the existence of medical problems coupled with the lack of income constituted grounds for a finding of undue hardship, noting that there was no apparent abuse of the bankruptcy system and that the debtor had clear need for a fresh start.⁵⁸

—The debtor was diabetic and had no equity in his household furnishings or his auto. He was paying child support for the child of his first marriage and was in the midst of a divorce from his second wife. Although there was no evidence of extravagant living, the debtor was unable to keep current with his bills on his present income and had little prospect of increased income in the future. Educational loans constituted only fifteen to twenty percent of his total indebtedness. Under these circumstances, the court concluded that requiring the debtor to repay the student loans would impose upon him an undue hardship.⁵⁹

—The debtor and her husband maintained a standard of living near the welfare level. She had recently terminated her employment due to pregnancy. She and her husband were unable to pay monthly expenses, much less the ex-

57. *Hearings*, *supra* note 18, at 1097 (testimony of Sheldon Steinbach quoting the Bankruptcy Commission Report) (emphasis added).

58. *In re Valentine*, BANKR. L. REP. (CCH) ¶ 67,042 (E.D. Tenn. Jan. 3, 1979).

59. *In re Bonnington*, BANKR. L. REP. (CCH) ¶ 67,009 (E.D. Tenn. Sept. 26, 1978).

isting medical bills they were obligated to pay as post-petition debts, and the future medical bills they would likely incur for their child who suffered from a respiratory problem. The court discharged a student loan of approximately \$2,200.⁶⁰

—The debtor was the divorced, forty-five-year-old mother of four children, two of whom lived at home. She did not receive a college degree. She had suffered a series of illnesses, including heart trouble and alcoholism, and needed surgery. When the debtor was employed, she could work only half a day because of her health problems. She was spending more per week than her income. Characterizing the situation as a “classic hardship case,” the court discharged the student loan.⁶¹

—The debtor was a third generation depressive. At the time of the hearing, she was living on unemployment insurance which was scheduled to run out in a month or two. Although her future was bleak, the court chose to focus on the present. “Not being clairvoyant, the Court can only base its decision upon what has happened in the past and what was happening at or about the time of the hearing. Certainly, at this point in time, it would work an undue hardship on the bankrupt to pay the plaintiff.”⁶²

—The debtor completed only one semester of college and had not worked in the three years since she dropped out of school. She was a welfare recipient, pregnant, and in the midst of a divorce. She lived at home with her parents and planned to move out. She was partially disabled for an uncertain duration from an automobile accident. The court discharged her \$1,500 student loan. It represented less than thirty percent of her total unsecured debts.⁶³

60. *Connecticut Student Loan Foundation, Inc. v. Bagley*, 4 Bankr. Rep. 248 (D. Ariz. 1980).

61. *Diaz v. New York Higher Educ. Serv. Corp.*, 5 Bank. Rep. 253, 253-54 (W.D.N.Y. 1980).

62. *New York State Higher Educ. Serv. Corp. v. Barrington*, 7 Bankr. Rep. 267, 268 (W.D.N.Y. 1980).

63. *Pennsylvania Higher Educ. Assistance Agency v. Johnson*, 5 Bankr. Ct. Dec. 532 (E.D. Pa. 1979).

Failure of the Promise of Education—Increased Earning Capacity

Although they might not have disagreed with the results in each of the classic cases above, other courts have cautioned that honest debtors who suffer extreme misfortune due to circumstances beyond their control do not automatically present cases of undue hardship. In so doing, they have followed the admonition of one member of Congress who noted that in such circumstances further inquiry should be undertaken.⁶⁴

If, after graduating from school, an individual becomes a paraplegic and earning capacity was impaired, there might be a finding of hardship. If the individual has had his or her earning capacity improved by virtue of the loan and other factors are not present, I don't think a hardship would exist.⁶⁵

The Congressman's comment reiterates the argument that student loans represent a claim of the government on the future earnings of the debtor, somewhat in the nature of a security interest. The implicit promise of education is an increased earning capacity. If that promise is unfulfilled, the "collateral" is economically valueless and the student loan debtor should be free to discharge the debt. But if the debtor is employed in a job related to his or her educational training, on a quantum meruit theory discharge should be denied regardless of the presence of unforeseen circumstances or the absence of any indicia of abuse.

The court accepted this view in *In re Garcia*⁶⁶ where the debtor had recently lost a child and the resulting medical expenses were the primary reason for his bankruptcy filing. Debtor's assets consisted of household furniture and a car. His monthly living expenses consumed all but twenty-five dollars of his net income. Nonetheless, the court was unwilling to grant a hardship discharge, noting that the debtor was employed as an internal revenue agent and was "young, intelligent, and healthy."⁶⁷ Unforeseen circumstances had not impaired his abil-

64. *Hearings*, *supra* note 18, at 1092-93 (testimony of Representative John N. Erlenborn).

65. *Id.*

66. 1 Bankr. Rep. 253 (S.D. Fla. 1979).

67. *Id.* at 254.

ity to repay the student loan because they had not negated his earning capacity.

Even in the absence of actual employment in a field related to one's education, a *potential* for such employment, however remote, may negate the finding of undue hardship. For example, the court in *New York State Higher Education Services Corporation v. Henry* denied the discharge of \$4,500 in student loans to a debtor who had received a masters degree in social work.⁶⁸ She was unemployed and lived with her brother and his family. The debtor was unsuccessful in obtaining a job, even though she had applied for fifty positions in the social work area. The court pointedly observed that "her potential for future gainful employment is far from bleak . . . [T]here are hundreds of organizations in New York City which have positions in her field to which she has not applied, and she apparently has made no effort to seek employment outside her chosen field."⁶⁹

In many instances, however, the promise of education has not been fulfilled. Increased earnings in the chosen field were not forthcoming. In such circumstances, most courts will grant a hardship discharge, provided the debtor maintains the minimal lifestyle envisioned in the report of the Bankruptcy Commission.⁷⁰ For example:

—Although the debtor had a degree in social work, she was unable to hold a regular job. What she could hope to earn would be minimal at best. She had no property. Noting the lifestyle standard suggested in the report of the Bankruptcy Commission, the court found the requisite undue hardship and discharged the student loan.⁷¹

—The debtor had spent five years in college but had received no degree. He had no assets and his net income as a part-time truck driver was expended as soon as it came in. Noting that the debtor's "education was valueless in ap-

68. 4 Bankr. Rep. 495 (S.D.N.Y. 1980).

69. *Id.* at 497-98. In part, the harshness of the opinion may be explained by the timing of the bankruptcy petition—two months after the student loan became due. See the discussion of *Littel* in the text accompanying notes 84-87 *infra* for a more sympathetic approach when employment in the chosen field is unrealistic.

70. See text accompanying note 57 *supra*.

71. *In re Matthews*, BANKR. L. REP. (CCH) ¶ 67,049 (D. Conn. Feb. 6, 1979).

praising his future income," the court discharged the student loan.⁷²

—The debtor enrolled in a number of accounting courses, but his education did not improve his position in his employment as a policeman. It did not appear that his earning capacity in the foreseeable future would be enhanced to any extent because of the educational value of the courses. After bankruptcy, the debtor's financial resources were insufficient to support him and his dependents at a break-even level. Again, the student loan was discharged.⁷³

—The debtor was a CETA employee who had never completed college. She and her children resided with her family. In dictum, the court stated that the debtor had no present ability to make payments and noted that "[o]nly by divining a rosy future unsupported by known facts could the plaintiff argue any ability to repay this loan in the future."⁷⁴ Because the loan was a direct loan rather than a federally insured or guaranteed loan, it was unnecessary to make a hardship determination. If it were necessary, the outcome is clear.⁷⁵

—The debtor was a certified teacher but her efforts to obtain a job in her field had been futile. Since receiving her certification, she had held a number of dead-end jobs, ultimately working as a substitute teacher. The court took into account her efforts to obtain work, the job obtained, her present level of employment, and her current level of income, which was unable to sustain her above the poverty level. The court determined that she had little chance in the near future of obtaining a full-time teaching job which would significantly alter her present circumstances. "[I]f the past is any guide to the future, the bankrupt's prospects are far from rosy."⁷⁶ The court clearly articulated its interpretation of the legislative purpose behind the nondis-

72. *In re Gangloff*, BANKR. L. REP. (CCH) ¶ 67,007 (E.D. Pa. Oct. 13, 1978).

73. *In re Fonzo*, 1 Bankr. Rep. 722 (S.D.N.Y. 1979).

74. *Daemen College v. Thomas*, 4 Bankr. Ct. Dec. 796, 796 (W.D.N.Y. 1978).

75. *Id.* at 796, 797.

76. *New York Higher Educ. Serv. Corp. v. Moore*, 4 Bankr. Ct. Dec. 791, 792 (W.D.N.Y. 1978). Even though the debtor had a \$30 miscellaneous item in her budget, "[s]he [had] stretched her budget by not eating, not replacing clothes and doing without many of the necessities of life"; therefore, the student loan was discharged. *Id.*

chargeability of student loans.

In essence, Congress is saying to the Bankruptcy Courts that they are Courts of Equity and if they are satisfied that the repayment of student loans within the purview of the statute would work an inappropriate, inequitable burden upon the bankrupt or their [sic] dependents then a discharge should be granted.⁷⁷

In each of these cases, the debtor maintained a very minimal lifestyle. If the debtor had been able to maintain a more moderate lifestyle, albeit unenhanced by the mortgaged education, the student loans may not have been discharged.

The Government's High Moral Claim

The legislative history indicates that the government is a special creditor with a high moral claim to repayment.⁷⁸ Thus, even in the absence of benefit, courts may deny the discharge of student loans if there is a capacity for repayment. For example:

—The debtor was dismissed from school after four years of college work in marketing and sales for failure to meet minimum academic requirements. At the time of trial, he was employed in a factory job. Although he had no wealth, the court noted that the debtor was “able bodied with no medical problems, no dependents and no excessive living expenses.”⁷⁹ The court denied the hardship discharge because the debtor maintained more than a minimal lifestyle, even though his job was unrelated to his education.

—The debtor was employed as a spot welder on an assembly line. Her former husband had left the country and refused to support the children, one of whom had a brain tumor which required an elaborate operation. There was a substantial possibility that if additional treatment were required for her son, the debtor would be unable to continue her full-time employment. The court noted that she had proposed “an extremely tight but not unreasonable budget

77. *Id.*

78. See text accompanying notes 36-39 *supra*.

79. *Ohio v. Kirch*, 4 Bankr. Ct. Dec. 680, 682 (S.D. Ohio 1978). The debtor budgeted only \$205—\$85 for rent and \$120 for food.

which appears to account for most normal expenditures."⁸⁰ Nonetheless, the court denied the discharge, finding that payment by deferred installments of twenty-five dollars per month, almost one-half of the unbudgeted income, "might be within the debtor's future economic abilities."⁸¹

—The debtor was educated in the area of urban studies. She was thirty years old, healthy, and working part-time. The court noted that she "could keep life and limb together for herself and her daughter while not living opulently."⁸² The court denied the hardship discharge, observing that "[i]t is no answer that the bankrupt is not presently employed in her chosen area."⁸³ The rationale of the court is abundantly clear, for in a footnote, it quoted from the statement of a Congressman in the legislative history: "[W]hile I sympathize with . . . the many students who are unable to find employment which they believe to be commensurate with their level of education, I do not believe that this gives them a license to steal."⁸⁴

B. THE MULTIFACETED TEST—"RUNNING THE GAUNTLET"

The cases reflect four primary considerations in a decision to discharge a student loan: [1] a minimal lifestyle, [2] unforeseen circumstances, [3] a job unrelated to the debtor's studies, and [4] the special status of the government as creditor. The legislative history lends support to each theory of dischargeability, but it fails to rank them in order of priority. As a result, bankruptcy courts generally have been unable to agree on the relative importance of each of these factors. For the most part, the courts have adopted an ad hoc approach, applying whatever test seemed to be appropriate to the circumstances. From the cases, only the following generalizations can be gleaned:

- [1] The undue hardship discharge will be denied if the debtor can make the scheduled repayments and still maintain a minimal lifestyle—regardless of the source

80. *Wisconsin Higher Educ. Aids Bd. v. MacPherson*, 4 Bankr. Ct. Dec. 950, 951 (W.D. Wis. 1978).

81. *Id.*

82. *New York Higher Educ. Serv. Corp. v. White*, 6 Bankr. Rep. 26, 28 (S.D.N.Y. 1980).

83. *Id.*

84. *Id.* at 28 n.5.

of income.

- [2] The undue hardship discharge will be denied if the debtor could make the scheduled repayments and still maintain a minimal lifestyle with a more prudent allocation of income or effort to seek employment.
- [3] The undue hardship discharge will be granted if the debtor can maintain only a minimal lifestyle and there is no indicia of bankruptcy abuse—that is, if the financial problems are due to circumstances beyond the debtor's control and/or the debtor plainly received no economic benefit from his or her education.

In *Pennsylvania Higher Education Assistance Agency v. Johnson*,⁸⁵ the court attempted to bring a semblance of order to the diverse interpretations of the undue hardship exception by formulating a multifaceted test that reflected the concerns expressed in the legislative history. The *Johnson* court's standards are remarkably in line with the above generalizations. In order to obtain an undue hardship discharge, the student loan debtor must run a gauntlet by passing [1] a "mechanical" test (minimal lifestyle), [2] a "good faith" test (prudent allocation of income and bona fide effort to secure employment), and [3] a "policy" test (absence of bankruptcy abuse and benefit of education).⁸⁶ The *Johnson* court concluded:

[A] debtor should be denied discharge of his student loan within the five year period after the debt matures, if either:

(a) his future financial resources are most likely sufficient to finance repayment of the student loan, and to support the debtor and his dependents at or above the poverty level, or

(b) but for the debtor's negligence or irresponsibility he would be able to repay the loan without lowering his standard of living below the poverty level.

....

A court should grant discharge of a student loan within five years after it becomes due, based on a finding that repayment of the loan would cause the debtor "undue hardship," where:

(a) The debtor's future income and wealth, in

85. 5 Bankr. Ct. Dec. 532 (E.D. Pa. 1979).

86. *Id.* at 544-45.

the maximum foreseeable period allowed for repayment of the student loan, are likely to be insufficient to fund the loan's repayment and to support the debtor and his dependents at a subsistence level of living, and

(b) either such hardship is due to circumstances beyond the debtor's control; or,

(c) the circumstances clearly indicate that discharge of the student loan was not a dominant reason for filing bankruptcy, and that the debtor's earning prospects have not appreciably benefited from his education.⁸⁷

Whichever test is applied, in the vast majority of cases, the undue hardship discharge will be denied. As one administrator of the student loan program noted: "In practically all cases, student loan borrowers are young, healthy, have few obligations beyond the student loan, and have a lifetime of earning ability ahead of them."⁸⁸

III. PARTIAL DISCHARGEABILITY AND UNLIMITED FORBEARANCE

A number of additional considerations impinge upon the problem yet are rarely articulated in the decisions. For example, in many situations, the student and the educational institution are *in pari delicto*. The student's education did not enhance his or her earning capacity, but there was little reason to expect that it would. The court in *Littel v. Oregon*⁸⁹ clearly took note of this abuse in the administration of the student loan program when it observed that the debtors may have been "inveigled into obtaining the loan and taking particular courses in college when the college authorities should have known that upon graduation from college the student had little chance of obtaining employment in that field."⁹⁰

In *Littel*, both husband and wife had majored in Education and English with the thought of becoming teachers. Both had been unable to find teaching jobs which would utilize their col-

87. *Id.*

88. *Hearings*, *supra* note 18, at 1099 (statement of John N. Erlenborn quoting the Director of the Virginia Loan Program).

89. 6 Bankr. Rep. 85 (D. Ore. 1980).

90. *Id.* at 88.

lege educations. The husband worked as a service station attendant while his wife was employed as a CETA worker in a half-time position as a counselor at a community college. For these students, the promise of education was hollow. Only one of the four theories of nondischargeability would require them to repay the loan—the special status of the government as creditor. The court in *Littel* apparently considered that theory to be sufficient. It was not persuaded that repayment was altogether impossible. Indeed, “by a reasonable additional effort, some payment could be made.”⁹¹ Accordingly, the court directed each spouse to make payments of ten dollars a month on the student loans over a thirty-three and forty-eight month time period for a total repayment of approximately eleven percent of the principal.⁹² Thus, a theory of partial dischargeability was born.⁹³

In *United States v. Hemmen*,⁹⁴ the court fashioned a more unique formula for partial dischargeability. There the debtor was recently divorced, living with his parents, and receiving unemployment benefits. His educational debts of approximately \$4,000 amounted to less than one-fourth of his total unsecured debts. Although his present circumstances were modest, the court observed that “[t]his is a temporary lack of income rather than permanent.”⁹⁵ Therefore, the court was willing to supervise its judgment for a short term of years and discharge the student loans only if the debtor used his best efforts to find suitable employment and paid the student loan creditors all funds in excess of \$3,600 per annum for a period of five years from the date of maturity of the last loan.⁹⁶

The creative solutions employed by the courts in *Littel* and *Hemmen* are commendable because they mesh nicely with the existing statutory scheme for the repayment of student loans. Under the student loan program, the lender has the option of unlimited forbearance to assist the borrower during a period of financial difficulty; payments may be reduced or deferred indefi-

91. *Id.*

92. *Id.*

93. Earlier, in *Wisconsin Higher Educ. Aids Bd. v. MacPherson*, 4 Bankr. Ct. Dec. 950, 951 (W.D. Wis. 1978), the court had required the debtor to repay the principal amount of the student loan but forgave the interest.

94. 7 Bankr. Rep. 63 (N.D. Ala. 1980).

95. *Id.* at 67.

96. *Id.*

nately.⁹⁷ In effect, an undue hardship provision was already built into the student loan program before the enactment of the bankruptcy exception to discharge.

In light of that second undue hardship provision, a few courts have found it nearly impossible for a debtor to discharge a student loan.⁹⁸ While it may be possible to show an inability to meet the normal repayment schedule, it is inordinately difficult to demonstrate an inability to pay even a nominal amount until circumstances improve. Most courts, however, have simply ignored the possibility of unlimited forbearance.⁹⁹ Both views render one of the undue hardship provisions devoid of meaning. It would seem that an accommodation of the dual statutory scheme could best be served through a rule of partial dischargeability, requiring whatever repayment is feasible under the circumstances during the five year period following the maturity of the student loan.

IV. DISCHARGE OF STUDENT LOANS THROUGH CHAPTER 13 OF THE BANKRUPTCY REFORM ACT¹⁰⁰

Perhaps the greatest paradox in the dischargeability of student loans is revealed in a contrast between the provisions of Chapter 7, straight bankruptcy, and Chapter 13, the repayment plan. Chapter 13 contains a super discharge provision—section 1328(a). While a number of debts such as student loans, traffic tickets,¹⁰¹ and debts procured by fraud¹⁰² are nondischargeable in straight bankruptcy, all debts except taxes and family support obligations are dischargeable in Chapter 13. The intent of Congress in providing for greater dischargeability under Chapter 13 than Chapter 7 was apparently to encourage debtors to attempt a repayment plan.¹⁰³ But, once again, the legislative intent has been distorted by judicial interpretation.

97. 20 U.S.C. § 1080(c) (1976).

98. *See, e.g., Warren v. University of Illinois*, 6 Bankr. Rep. 233 (S.D. Fla. 1980) and *Georgia Higher Educ. Assistance Corp. v. Densmore*, 8 Bankr. Rep. 308 (N.D. Ga. 1979).

99. *See Pennsylvania Higher Educ. Assistance Agency v. Johnson*, 5 Bankr. Ct. Dec. 532, 536 (E.D. Pa. 1979).

100. 11 U.S.C. §§ 1301-1330 (Supp. II 1978).

101. *Id.* § 523(a)(7).

102. *Id.* § 523(a)(2).

103. *See, e.g., In re Seman*, 4 Bankr. Rep. 568, 569-70 (S.D.N.Y. 1980).

Under Chapter 13, a debtor's repayment plan need not provide for payment of all debts in full; unsecured creditors must simply receive more than they would in straight bankruptcy proceedings.¹⁰⁴ In many consumer bankruptcies, all of the debtor's assets are exempt; unsecured creditors receive nothing. As a result, a number of courts have applied the statutory test quite literally and have approved Chapter 13 repayment plans calling for nominal payments to unsecured creditors.¹⁰⁵

Thus, while student loans may be generally nondischargeable in straight bankruptcy, in a number of jurisdictions they are freely dischargeable in Chapter 13 proceedings, regardless of hardship. The disparity in treatment between the student loan debtor who files under Chapter 7 and the student loan debtor who files under Chapter 13 renders the legislature's and the court's rather stringent view of the undue hardship discharge—on whatever theory—remarkably anomalous.

CONCLUSION

It is readily apparent that the courts are in hopeless disarray with respect to the dischargeability of student loans in bankruptcy. Their confusion is a function of the apparent dichotomy between the focus of the legislative history on bankruptcy abuse and Congress' articulated grounds for discharge, "undue hardship." Until the legislative compromise that led to the introduction of the undue hardship exception, Congress' intent to deny discharge to those engaged in bankruptcy abuse was manifest. Deeming it impractical for the courts to independently ascertain the requisite fraud under section 523(a)(2) in each case, such fraud was to be conclusively presumed if a bankruptcy were filed within five years of graduation. Yet the factual basis for such a wholesale presumption of fraud was nonexistent. Rather than abandoning that premise altogether, Congress reached an unhappy compromise with the undue hardship exception. It chose inappropriate language and then failed to furnish clear guide-

104. 11 U.S.C. § 1325(a)(4) (Supp. II 1978).

105. Compare *United States v. Eichelberger*, 6 Bankr. Rep. 705 (S.D. Miss. 1980) with *In re Yee*, 7 Bankr. Rep. 747 (E.D.N.Y. 1980). The immediate dividend to the creditor may well be greater in a repayment plan than in straight bankruptcy proceedings. But the Chapter 7 student loan creditor is free to pursue its claim to repayment in full after bankruptcy because its debt is nondischargeable. The Chapter 13 student loan creditor is barred from further collection effort because its debt is discharged.

lines for judicial application.

Not surprisingly, the absence of a single coherent theory for the discharge of student loans has led to a variety of judicial interpretations. Until the statutory language is clarified to more accurately reflect the legislative intent, student loan debtors will continue to be dependent on the unlimited, and generally unreviewable,¹⁰⁶ discretion of individual bankruptcy judges.

The medley of concerns expressed in the legislative history suggest a number of possible revisions:

- [1] If the legislative concern is truly bankruptcy abuse, reliance might be placed on section 523(a)(2). However, given the difficulty of establishing fraudulent intent at the time the loan is made, a *conclusive* presumption of abuse should arise if bankruptcy is filed within a given period of time and student loans comprise a given percentage of total indebtedness. In addition, either the super discharge provision of Chapter 13 should be amended to conform to this intent, or Chapter 13 should be revised to require a repayment plan premised on the debtor's best efforts.¹⁰⁷
- [2] If the legislative concern is the inequity inherent in the debtor retaining a valuable asset—education—without paying for it, student loans should be nondischargeable unless the debtor, after bona fide effort, is unable to secure employment in a field related to his or her education. Again, either the super discharge provision of Chapter 13 should be amended to conform to this intent, or Chapter 13 should be revised to require a repayment plan premised on the debtor's best efforts.
- [3] If the legislative concern is the high moral claim of the government as a creditor and the maintenance of an ongoing program of educational assistance, student loans should be nondischargeable altogether. Again, either the super discharge provision of Chapter 13 should

106. Findings of fact cannot be set aside unless clearly erroneous. FED. R. CIV. P. 52(a).

107. A good faith effort was required of the Chapter 13 debtor by the technical amendments bill, S. 658, 96th Cong., 1st Sess., § 191(a) (1979).

be amended to conform to this intent, or Chapter 13 should be revised to require a repayment plan premised on the debtor's best efforts.

- [4] If the legislative concern is *in fact* true hardship, student loans should be nondischargeable in the absence of unforeseen circumstances that will not be alleviated by the discharge of other debts. Despite the student loan creditor's option of unlimited forbearance in the event of hardship, a separate provision in the bankruptcy act to facilitate a fresh start for the debtor would be desirable. In addition, the possibility of a middle ground, partial dischargeability, should be clearly set forth in the legislation. Again, either the super discharge provision of Chapter 13 should be amended to conform to this intent, or Chapter 13 should be revised to require a repayment plan premised on the debtor's best efforts.

A survey of the case law indicates that the majority of courts purport to apply the fourth standard—the present statutory standard—albeit somewhat harshly. The tenor of the opinions and the overwhelming result, nondischargeability, belie that theory. In fact, the third standard generally prevails. Bankruptcy judges have been swayed by an opinion shared by lenders, a number of members of Congress, and the public at large: bankruptcy is inherently unfair to unsecured creditors. In the end, the controversy surrounding student loans in bankruptcy may be characterized by one dominant theme: hostility to the basic premise of bankruptcy—forgiveness of debt.

Depicting the legislative and judicial approaches as retaliatory or vindictive is, perhaps, overly harsh. It is necessary to separate the result—nondischargeability—from the rhetoric and the theory. The result is sound for it comports with a fundamental governmental interest—the maintenance of ongoing assistance to students of higher education. The purpose of the federal student loan program is twofold: [1] ensuring a sufficient supply of well trained, competent professional and technical personnel, and [2] allowing every person the fullest possible educational opportunity by making loans available to those who would not otherwise obtain a loan because of their age, lack of collat-

eral, or borrowing history.¹⁰⁸ These are worthy objectives that are clearly subverted by the discharge of student loans in bankruptcy. Even though the statistics do not indicate that bankruptcy filings were ever a great problem in terms of absolute dollars, they clearly remain a problem in a political sense. As the legislative history indicates, even an ill-perceived abuse may be as significant as actual abuse in terms of its impact on congressional willingness to fund a student loan program. In sum, Congress did not go far enough in its treatment of student loans in bankruptcy. Student loans should be nondischargeable altogether—regardless of hardship and the period of time elapsed.¹⁰⁹ The debtor is already adequately protected from the spectre of debtor's prison or involuntary servitude through a program of forbearance built into the administration of the student loan program. The interests of future generations of students demand that their predecessors' promises be kept.

108. S. REP. NO. 673, 89th Cong., 1st Sess. 35-36, *reprinted in* [1965] U.S. CODE CONG. & AD. NEWS 4027, 4053.

109. Because student loans are repaid over a ten year period, a student now may discharge one-half of the obligation at the end of five years.