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# DISCHARGE OF STUDENT LOAN DEBT UNDER 11 U.S.C. § 523(A)(8): REASSESSING "UNDUE HARDSHIP" AFTER THE ELIMINATION OF THE SEVEN-YEAR EXCEPTION

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# DISCHARGE OF STUDENT LOAN DEBT UNDER 11 U.S.C. § 523(A)(8): REASSESSING "UNDUE HARDSHIP" AFTER THE ELIMINATION OF THE SEVEN-YEAR EXCEPTION

## I. INTRODUCTION

In 1998, Congress closed one of only two doors available to debtors seeking discharge of student loan debts in bankruptcy.[1] Prior to October 7, 1998, the Bankruptcy Code made student loan debts non-dischargeable unless: (1) the loans first became due more than seven years before the debtor filed for bankruptcy;[2] or (2) not allowing the student loan debts to be discharged would impose an undue hardship on the debtor and the debtor's dependents.[3] On October 7, President Clinton signed into law the Higher Education Amendments of 1998, which eliminated the seven-year exception, leaving only the undue hardship exception to non-dischargeability.[4]

This Note argues that "undue hardship" must be interpreted more broadly than it has been before, now that debtors are no longer protected by the automatic seven-year exception.[5] Lowering the standards necessary to establish "undue hardship" is consistent with the Bankruptcy Code's underlying policy of providing debtors with a fresh start, free from oppressive debt.[6]

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1. *See* Craig A. Gargotta, *Congress Amends § 523(a)(8) to Eliminate Seven-Year Discharge Provision for Student Loans,* 17-NOV AM. BANKR. INST. J. 8, 8 (1998).

2. *See* Crime Control Act of 1990, Pub. L. No. 101-647, § 3621(1), 104 Stat. 4789, 4964 (codified as amended at 11 U.S.C. § 523(a)(8)(A)) (repealed 1998). Section 523(a)(8)(A) originally required that an education loan be due for a five year period. *See* Bankruptcy Reform Act of 1978, *reprinted in* 1978 U.S.C.C.A.N. 2549, 2591.

3. *See* Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549, 2591 (codified as amended at 11 U.S.C. § 523(a)(8)(B) (1994)).

4. *See* Higher Education Amendments of 1998, Pub. L. No. 105-244, § 971, 112 Stat. 1581, 1837 (1998) (codified as amended at 11 U.S.C. § 523 (a) (8) (1999)). The primary purpose of the 1998 Higher Education Amendments was to provide federal funding for student loans at a reduced interest rate. *See* Gargotta, *supra* note 1, at 8.

5. For an article making the opposite argument, *see* Gargotta, *supra* note 1. To Gargotta, the elimination of the seven-year exception suggests that Congress now views "undue hardship" as creditor protection rather than debtor protection. *See id.* at 9. According to that view, "the circumstances that warrant an undue hardship discharge may have to be more extreme than previously considered." *Id.*

6. *See* Robert F. Salvin, *Student Loans, Bankruptcy, and the Fresh Start Policy: Must Debtors Be Impoverished to Discharge Educational Loans?,* 71 TUL. L. REV. 139 (1996) (arguing prior to the 1998 elimination of the seven-year discharge that undue hardship

Part II presents § 523(a)(8) of the Bankruptcy Code and discusses its legislative history.[7] Part III discusses the major tests used by courts to determine whether "undue hardship" has been established.[8] Part IV explains the critical role the seven-year discharge once played in guiding judicial interpretation of "undue hardship" and how the repeal of the seven-year discharge requires that standard to be reassessed.[9] This note concludes that the often harsh previous interpretations of "undue hardship" were the natural result of a statutory scheme that provided for automatic discharge after seven-years, and that the courts must lower that standard now because debtors no longer have any other way out of oppressive student loan debt.

## II. Section 523(a)(8)

Section 523(a)(8) of the Bankruptcy Code currently provides:

> A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt—for an educational benefit overpayment or loan made, insured or guaranteed by a governmental unit or nonprofit institution, or for an obligation to repay funds received as an educational benefit, scholarship or stipend, unless excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor's dependents.[10]

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should be interpreted more leniently, in a manner more consistent with the fresh start policy).

7. *See infra* notes 10-26.

8. *See infra* notes 27-107.

9. *See infra* notes 108-51.

10. 11 U.S.C. § 523(a)(8) (1999). At the conclusion of a bankruptcy case the debtor is normally granted a discharge, an injunction against the enforcement by creditors of the debtor's pre-filing obligations. *See* 11 U.S.C. §§ 524, 727 (1994). In a Chapter Seven case, an individual debtor is granted a discharge in exchange for having surrendered his or her non-exempt property to the bankruptcy trustee, who liquidates that property and distributes the proceeds to the creditors. In a Chapter 13 case, individual debtors may keep all or most of their property, provided the court approves a repayment plan in accordance with the Code. *See id.* at §§ 1321-28. Chapter Nine for municipal bankruptcy, Chapter 11 for corporate reorganization (or sometimes individual reorganization), and Chapter 12 for family-farmer bankruptcy, work in much the same fashion. *See id.* at §§ 941-44, 1121-41, 1321-28. In certain cases it is possible for a debtor to be denied a discharge, such as where the debtor attempts to hide or conceal its assets from creditors. *See id.* at § 727(a).

Before 1990, notwithstanding a debtor's discharge in bankruptcy, § 523(a)(8) specifically restricts the dischargeability of student loans that were insured or guaranteed by a governmental unit, or that were made under any program funded by a governmental unit or nonprofit institution.[11] An amendment to § 523(a)(8) in 1990 added the words "or for an obligation to repay funds received as an educational benefit, scholarship or stipend."[12] "The added words [have] removed any requirement that the loan involve a governmental. . .or nonprofit institution."[13] Thus, "§ 523(a)(8) [now may] be interpreted as applying to a loan made by any lender for an educational purpose."[14]

Supporters of § 523(a)(8) argue that educational loans are not granted on the same basis as other loans.[15] Lenders or guarantors who participate in educational loan programs typically extend credit to students who might not qualify for credit under traditional standards.[16] Interest rates and repayment terms can be very favorable to the student borrower, and no security is usually required.[17] Such lending fosters the government's policy of promoting access to educational opportunities.[18]

In enacting § 523(a)(8), Congress was primarily concerned about abusive student debtors and protecting the solvency of student loan programs.[19] In particular, Congress was concerned by reports of irresponsible students and recent graduates declaring bankruptcy as a way to avoid repayment of student loans on the eve of lucrative careers.[20] Upon graduation, the typical student has little or no non-exempt property that can be distributed to creditors, but may have substantial future earning potential.[21] Section 523(a)(8) was designed to remove the perceived temptation of recent graduates to use the bankruptcy system as a low cost method of unencumbering those future earnings.[22]

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11. *See* 2 COLLIER BANKRUPTCY MANUAL ¶ 523.13[1] (3d ed. 1999).
12. ROBERT L. JORDAN ET AL., BANKRUPTCY 186 (5th ed. 1999).
13. *Id.* at 186-87.
14. *Id.* at 187.
15. *See id.* at 186.
16. *See* 2 COLLIER BANKRUPTCY MANUAL, *supra* note 11, at ¶ 523.13[1].
17. *See* JORDAN, *supra* note 12, at 186.
18. *See* Santa Fe Med. Servs., Inc. v. Segal (*In re* Segal), 57 F.3d 342, 348 (3d Cir. 1995).
19. *See* Andresen v. Nebraska Student Loan Program (*In re* Andresen), Inc., 232 B.R. 127, 137 (B.A.P. 8th Cir. 1999).
20. *See* Thad Collins, *Forging Middle Ground: Revision of Student Loan Debts in Bankruptcy as an Impetus to Amend 11 U.S.C. § 523(a)(8)*, 75 IOWA L. REV. 733, 741-42 (1990).
21. *See* JORDAN, *supra* note 12, at 186.
22. *See id.*

Those who opposed the enactment of § 523(a)(8) addressed the lack of empirical evidence supporting the theory that students and graduates were trying to take advantage of the bankruptcy system, or that such bad actors actually posed a threat to the continued viability of student loan programs.[23] A study by the General Accounting Office made before the enactment of § 523(a)(8) found that only a fraction of one percent of matured student loans had been discharged in bankruptcy, a rate that compared favorably to the consumer credit industry overall.[24] The study also found that most debtors who had obtained discharge of student loans in bankruptcy also had other significant indebtedness, leading to the conclusion that those filings represented a genuine need for bankruptcy relief rather than attempts to find an easy avenue to student debt relief.[25] Finally, the opposition to § 523(a)(8) also argued that the non-dischargeability of student loans was merely a collection device "for lenders who were not being aggressive enough with their collection efforts."[26]

## III. Judicial Interpretation of "Undue Hardship"

Despite all the debate, "undue hardship" remains undefined in the Bankruptcy Code.[27] Additionally, the scope of the legislative history to § 523(a)(8) is limited to Congress's purpose in excepting student loans from discharge.[28] The legislative history only indicates that Congress intended to preserve student loan programs and to bar undeserving student borrowers from abusing the bankruptcy system.[29] The legislative history does little to assist a court in identifying when Congress intended student loans to be discharged for "undue hardship."[30]

To fill in the gap left by Congress, courts have developed a number of tests for determining the existence of "undue hardship" over the last two decades.[31] Although the courts have tried to accurately reflect and enforce Congress's intent in providing an "undue hardship" exception to non-dischargeability, the tests each contain important dif-

23. *See Andresen*, 232 B.R. at 137.

24. *See* H.R. Rep. No. 95-595, at 133 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6094. The House report contains the results of the General Accounting Office study, along with the opposing arguments made with respect to nondischargeability.

25. *See id.*

26. *See Andresen*, 232 B.R. at 137.

27. *See id.*

28. *See id.* at 130.

29. *See id.*

30. *See id.*

31. *See id.* at 137.

ferences.[32] Thus, it has been noted that "there are as many tests for undue hardship as there are bankruptcy courts."[33]

### A. *The Brunner Test*

The test that has emerged as the majority view, having been adopted by most bankruptcy courts and several circuit courts,[34] was set forth by the Second Circuit Court of Appeals in *Brunner v. New York State Higher Education Services Corp.*[35] Under the *Brunner* test, the court considers three factors: (1) whether 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;"[36] (2) whether additional circumstances exist indicating that the debtor's state of affairs is "likely to persist for a significant portion of the repayment period;"[37] and (3) whether the debtor has made "good faith efforts" to repay the loans.[38]

The purpose of the good faith inquiry is to ensure that the debtor's inability to repay student loans should not have been caused by the debtor's own willfulness or negligence, but rather by circumstances beyond the debtor's control.[39] Therefore, the good faith prong of the *Brunner* test is met as long as the debtor, through no fault of his or her own, has never had the ability to repay student loans.[40] Application of the *Brunner* test necessarily requires each court to apply its own intuitive sense of what constitutes a "minimal" standard of living and "good faith."[41]

Typical of cases applying the *Brunner* test is *In re Roberson*.[42] After graduating from high school and serving in the United States Army for three years as an equipment repairman and operator the debtor, Jerry

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32. *See id.*

33. *See* Salvin, *supra* note 6, at 149. However, Salvin observes that "[e]ven courts purporting to use the same test will differ in the subtleties with which the test is applied." *See id.* at n.64.

34. *See* Gargotta, *supra* note 1, at 8.

35. 831 F.2d 395 (2d Cir. 1987).

36. *Id.* at 396.

37. *Id.*

38. *Id.*

39. *See* Pennsylvania Higher Educ. Assistance Agency v. Faish (*In re* Faish), 72 F.3d 298, 305 (3d Cir. 1995).

40. *See* 2 COLLIER BANKRUPTCY MANUAL, supra note 11, at ¶ 523.12[2].

41. *See id.*

42. 999 F.2d 1132 (7th Cir. 1993).

Roberson, opted for a career change.[43] Roberson first received an associate of science degree in industry and technology at a community college and later earned a bachelor of science degree in industrial technology from Northern Illinois University.[44] Roberson financed his education with $9,702 in student loans that were guaranteed by the Illinois Student Assistance Commission.[45]

Roberson earned $33,000 in 1988 and another $30,000 in 1989 working as an automobile assembler at Chrysler Corporation, where he had begun working during college and where "his wages as an assembler exceeded those of any job that his degree in industrial technology would enable him to obtain."[46] Then his life began to fall apart in 1990.[47] A second conviction for driving under the influence of alcohol resulted in the loss of Roberson's driving license and his dismissal from Chrysler in February.[48] In April Roberson divorced from his wife.[49] The divorce judgment ordered Roberson to pay $121.60 per week in child support and awarded possession of the marital residence and automobile to his former wife.[50] Without steady employment, Roberson's 1990 income plummeted to only $6,000, leaving him unable to pay his creditors.[51]

Roberson filed for Chapter Seven bankruptcy on September 28, 1990.[52] At that time, Roberson had no income and an estimated $680 per month in expenses, including $40 a week to rent a one room apartment with no kitchen or toilet. In addition, the $34,395 in debts listed in his bankruptcy petition overwhelmed his $18,357 in assets, $11,250 of which represents an illiquid interest in the house that his former wife possessed. Hence, both parties agreed that his financial condition at the time of the petition prevented Mr. Roberson from maintaining a minimal standard of living and making payments on his student loans.[53]

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43. *See Roberson*, 999 F.2d at 1133.
44. *See id.*
45. *See id.*
46. *Id.* at 1133-34.
47. *See In re Roberson*, 999 F.2d at 1134.
48. *See id.*
49. *See id.*
50. *See id.*
51. *See id.*
52. *See id.*
53. *Id.* at 1137.

After conflicting decisions on the discharge of Roberson's student loans by the bankruptcy court and the district court, the Seventh Circuit adopted *Brunner* as the appropriate test and held that Roberson had not established "undue hardship."[54] The court concluded that Roberson's financial situation would only last temporarily rather than over a large portion of the repayment period.[55]

The Seventh Circuit first noted that Roberson's short-term outlook was unquestionably dismal: "[T]he Debtor was unemployed at the time of trial with slight prospects for employment in the near future with his lack of transportation and [his wrist and back injuries]."[56] Nevertheless, the Seventh Circuit agreed with the bankruptcy court that these impediments "would not prohibit gainful employment in the future," that "Mr. Roberson will be eligible for a new driver's license in 1993," and that "his medical condition does not appear 'insurmountable.'"[57] Thus, without deciding whether Roberson's drunk driving convictions precluded a finding of good faith, the court denied Roberson discharge of his student loans for "undue hardship" because he had not "indicated his road to recovery is obstructed by the type of barrier that would lead us to believe he will lack the ability to repay for several years."[58] Fortunately for Roberson, the Seventh Circuit agreed with the bankruptcy court's decision to allow him a "two-year deferment to enable him to get back on his feet."[59] Less fortunate for Roberson was how the Seventh Circuit could fail to conclude that "undue hardship" had been established.

### B. *The Johnson Test*

The *Brunner* test is a popular modification of a test set forth previously by the Bankruptcy Court for the Eastern District of Pennsylvania in *Pennsylvania Higher Education Assistance Agency v. Johnson (In re Johnson)*.[60] Under the *Johnson* test, the court considers: (1) a mechanical analysis of the debtor's past and probable future resources;[61] (2) the debtor's good faith, including the debtor's best efforts to repay the

54. *See Roberson*, 999 F.2d at 1137-38.
55. *See id.* at 1137.
56. *Id.*
57. *Id.*
58. *Id.* at 1137-38.
59. *Id.* at 1137.
60. 5 Bankr. Ct. Dec. (CRR) 532 (Bankr. E.D. Pa. 1979).
61. *See id.* at 544.

loan and minimize expenses;[62] and (3) a policy analysis of the debtor's motives in filing, including whether the debtor derived financial benefits from the education received by virtue of the loans.[63] The student loan is non-dischargeable if the court finds against the debtor on any of the three factors.[64]

Under the *Johnson* test, the debtor's financial circumstances are rigorously scrutinized.[65] First, the mechanical analysis is really an inquiry into whether a debtor can support himself and his dependents at a subsistence or poverty level while continuing to make monthly student loan payments at the same time.[66] Second, the good faith inquiry empowers the court to rule that expenses for necessities are unnecessary where it believes the debtor could have avoided or diminished expense through the exercise of "ordinary prudence."[67]

A court's views of what constitutes "ordinary prudence" can be shockingly harsh.[68] For example, the court might conclude that a debtor's rent and utility expenses were excessive if the debtor had chosen to live alone rather than with a roommate.[69] The court might also conclude that a debtor lacks good faith if he or she does not work at the most economically productive job possible.[70] Therefore, a debtor who is unable to find work in his or her field of study should seriously consider finding work in another field in order to demonstrate good faith.[71] Moreover, a debtor should try to avoid voluntarily working at a job that pays less than he or she is capable of earning.[72] It is easy to see that a debtor's personal choices necessarily become limited by the ongoing requirement of good faith.[73]

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62. *See Johnson*, 5 Bankr. Ct. Dec. at 544.

63. *See id.*

64. *See id.*

65. *See* Salvin, *supra* note 6, at 153-57.

66. *See id.* at 153-54.

67. *See id.* at 155.

68. *See id.* at 155-56. *See also* Wegrzyniak v. United States (*In re* Wegrzyniak), 241 B.R. 689 (Bankr. D. Idaho 1999) (holding that a debtor-teacher failed to satisfy the second and third parts of the Brunner test because she had chosen, after her eighteen year old son had begun using drugs and had attempted suicide, to spend her summers raising her nine year old son rather than seeking additional summer employment).

69. *See Johnson*, 5 Bankr. Ct. Dec. (CCR) at 541.

70. *See id.* at 541-42.

71. *See id.*

72. *See id.*

73. *See* Salvin, *supra* note 6, at 156.

### *C. The Bryant-Poverty Test*

Some courts have declined to follow either the *Johnson* or *Brunner* approaches.[74] In *Bryant v. Pennsylvania Higher Education Assistance Agency (In re Bryant)*,[75] the court expressed dissatisfaction with the "unbridled subjectivity" involved in the good faith analysis of undue hardship cases.[76]

Instead, the court settled for a poverty test under which the debtor's student loans are presumed non-dischargeable if the debtor's income exceeds federal poverty guidelines.[77] That presumption can only be rebutted if the debtor can prove extraordinary circumstances meriting discharge despite the debtor's lack of poverty.[78] Conversely, a debtor's student loans are presumed dischargeable if the debtor's income falls below federal poverty guidelines, unless the creditors can prove extraordinary circumstances why discharge should be denied.[79]

*Bryant* has made the Federal Poverty Guidelines an important guide in testing for undue hardship.[80] Many courts now consider the Federal Poverty Guidelines in undue hardship cases, while a few courts have even adopted the guidelines as the sole determinant of undue hardship.[81]

### *D. Miscellaneous Variations*

Other courts have added levels of precision to particular factors of the different tests.[82] Although this practice may clarify an ambiguity within the test applied in a specific jurisdiction, it can also add to the overall confusion.[83]

For example, the Seventh Circuit Court of Appeals has held that under the *Brunner* test, a debtor's student loans may not be discharged unless there is "certain" hopelessness, rather than merely temporary hopelessness, in the analysis of the debtor's future income potential.[84] The court also added that the good faith inquiry requires denial of

74. *See Andresen*, 232 B.R. at 138.
75. *See* 72 B.R. 913 (Bankr. E.D. Pa. 1987).
76. *See id.* at 916-17.
77. *See id.* at 916-19.
78. *See id.*
79. *See id.*
80. *See* Salvin, *supra* note 6, at 162.
81. *See id.*
82. *See Andresen*, 232 B.R. at 138.
83. *See id.*
84. *See Roberson*, 999 F.2d at 1135.

discharge where the debtor's inability to repay student loans is due to negligence or irresponsibility in conducting his or her own financial affairs.[85]

Two courts have modified the undue hardship analysis more drastically.[86] First, the Third Circuit Court of Appeals has gone so far as to redefine undue hardship as "unconscionable" hardship.[87] Second, the Bankruptcy Court for the District of Colorado has stated that it disagrees with the *Brunner* test "to the extent that it looks to the 'repayment period of the loan' to determine whether the debtor's undue hardship situation is likely to persist."[88] The court concluded that § 523(a)(8) "speaks to the 'debt' and not to the repayment period of the loan itself," and that student loan debts should be discharged when there is no hope for the debtor to repay in the future.[89]

### *E. The* Cheesman *and* Pena *Tests*

In some cases courts are simply unable to tell precisely which test has been applied by another court. For example, in *Andresen v. Nebraska Student Loan Program (In re Andresen), Inc.*,[90] the court expressed difficulty in distinguishing between the *Brunner* test and the test adopted by the Sixth Circuit Court of Appeals in *Cheesman v. Tennessee Student Assistance Corp (In re Cheesman)*.[91] But in *United Student Aid Funds, Inc. v. Pena (In re Pena)*, the Bankruptcy Appellate Panel for the Ninth Circuit disagreed.[92]

The *Pena* court seized upon certain wording from *Brunner*, apparently absent from *Cheesman*, as a way of adopting its own totality of the circumstances approach.[93] Specifically, the *Pena* court focused on the Sixth Circuit's apparent omission of the second prong of the *Brunner* test, whether the debtor's state of financial affairs is likely to persist for

85. *See Roberson*, 999 F.2d at 1136.

86. *See Andresen*, 232 B.R. at 138.

87. *See* Pennsylvania Higher Educ. Assistance Agency v. Faish (*In re* Faish), 72 F.3d 298, 306 (3rd Cir. 1995)(quoting Matthews v. Pineo, 19 F.3d 121, 124 (3rd Cir. 1994)).

88. Jones v. Catholic Univ. of Am. (*In re* Jones), 1997 WL 52188, at *1 n. 2 (Bankr. D. Col. 1997).

89. *Id.*

90. *See Andresen*, 232 B.R. 127.

91. *See id.* at 138-39.

92. *See* 207 B.R. 919, 922 (B.A.P. 9th Cir. 1997).

93. *See id.*

a significant portion of the repayment period.[94] The court stated that "rigid adherence. . .to a particular test robs the court of the discretion envisioned by Congress in drafting § 523(a)(8)."[95]

As desirable as a totality of the circumstances test may be, however, the *Pena* court's attempt to distinguish the *Brunner* test from the *Cheesman* test appears flawed.[96] In *Cheesman,* the court explicitly quoted the *Brunner* test in full and proceeded to analyze the debtor's undue hardship claim under all three elements.[97] More accurately, the *Pena* court rejected the *Brunner* test's good-faith limitation because it precludes a debtor from introducing evidence that the education paid for by student loans was of little or no use or benefit to the debtor.[98] Therefore, *Pena's* true holding is that "undue hardship" is flexible enough that the value of a debtor's education can properly be considered in determining the debtor's future ability to pay.[99]

### *F. The Totality of the Circumstances Test*

Many courts apply a totality of the circumstances test to determine undue hardship.[100] For example, the Bankruptcy Court for the District of South Dakota has rejected the *Brunner* test in lieu of a "case-by-case" and "fact-sensitive" approach that considers a debtor's good faith, financial resources, and necessary expenses as well as any other circumstances.[101] The totality of the circumstances test is a more desirable approach than the others because it "affords a determination that contextually considers both the debtor's situation and the policies underlying § 523(a)(8)."[102] The totality of the circumstances test better "ensures an appropriate, equitable balance [between] concern for cases involving extreme abuse and concern for the overall fresh start policy."[103]

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94. *See id.*
95. *Id.*
96. *See Andresen,* 232 B.R. at 138-39.
97. *See* 25 F.3d 356, 359-60 (6th Cir. 1994).
98. *See Andresen,* 232 B.R. at 139.
99. *See id; see also Pena,* 207 B.R. at 923.
100. *See Andresen,* 232 B.R. at 139-40.
101. *See* Law v. Educ. Res. Inst. Inc. (*In re* Law, SSN: 504-90-2960), 159 B.R. 287, 292-93 (Bankr. D. S.D. 1993).
102. *Id.*
103. *Id.*

The totality of the circumstances test has been adopted by the Eighth Circuit Court of Appeals.[104] The Eighth Circuit's test for undue hardship considers "(1) the debtor's past, present, and reasonably reliable future financial resources; (2) calculation of the debtor's and his dependents' reasonable necessary living expenses, and (3) any other relevant facts and circumstances surrounding the particular bankruptcy case."[105] The Eighth Circuit approach is preferable to *Brunner* and the other tests because it is less restrictive than those tests, yet it maintains the essential considerations found in the other tests.[106] Although a *Brunner* analysis of the debtor's future ability to repay student loans is not ignored under the totality of the circumstances approach, neither does that one factor became dispositive against a finding of undue hardship where the debtor is currently in grave circumstances requiring an immediate fresh start.[107]

## IV. THE ELIMINATION OF THE SEVEN-YEAR DISCHARGE AND THE IRONY OF EQUITABLE RELIEF

Courts have often exercised their equitable powers to cushion the harsh effects imposed by § 523(a)(8).[108] At the same time, however, courts have continued to abide by a narrow interpretation of "undue hardship" even though that interpretation developed in the context of the now repealed seven-year discharge.[109] As one court has stated:

> The rigidity of some of those "tests" almost suggests that the solution to human suffering lies in the application of algebraic equations. . .[W]e cannot commit the court to a policy of mechanical evaluation of comprehensive human problems. "Undue hardship" is a concept so fraught with subjective elements that we must consider the totality of the circumstances to confirm its presence or absence. . . . Our approach is not intended to yield a general rule applicable to a broad class of cases, but remains as flexible and adaptable as the concept of equity itself. We are able to say only that the whole of a debtor's condition, in an

104. *See Andresen*, 232 B.R. at 139-40; *see also* Andrews v. S. Dakota Student Loan Assistance Corp. (*In re* Andrews), 661 F.2d 702, 704 (8th Cir. 1981).

105. *See Andresen*, 232 B.R. at 139.

106. *See id.*

107. *See id.* at 130-31.

108. *See Collins, supra* note 20, at 749-51.

109. *See Andresen*, 232 B.R. at 130 n.7.

> undue hardship case, should be sufficient to strike a chord of pity in the heart of equity.[110]

Thus, many courts have found it necessary to revise loans, partially discharge loans, or defer payments by maintaining or extending the automatic stay.[111] By manipulating § 523(a)(8) courts can uphold the policies behind non-dischargeability while balancing that interest with the fresh start policy.[112] Some courts find the authority to grant partial discharges and other equitable relief implicit in § 523(a)(8),[113] while others rely on the equitable powers of § 105(a).[114] Section 105(a) essentially allows a bankruptcy court to tailor an equitable solution around the facts of a particular case.[115]

Critics of partial discharge of student loans argue that Congress's silence in § 523(a)(8) should foreclose that possibility.[116] If Congress intended for courts to revise or partially discharge student loans, Congress could have expressly provided for those options in § 523(a)(8) or included broader language revealing such equitable solutions as a policy objective.[117] Critics have also argued that § 105(a) of the Bankruptcy Code does not provide authority for partial discharge or revision of student loans; rather, the equitable powers of bankruptcy courts may only be exercised within the enumerations of the Code.[118] The jurisdictional split over whether a court may partially discharge a debtor's student loan or whether courts are confined to an all-or-nothing discharge has grown over the past two decades.[119]

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110. Moorman v. Kentucky Higher Educ. Assistance Auth. (*In re* Moorman), 44 B.R. 135, 137-38 (Bankr. W.D. K. 1984).

111. *See Andresen*, 232 B.R. at 130; *see also* Collins, *supra* note 20, at 737 (arguing that Congress should amend § 523(a)(8) explicitly to provide revision as an option for the courts and the parties to student loan discharge proceedings). The automatic stay, found at 11 U.S.C. § 362 (1994), is a mechanism that stops most actions taken against the debtor during the course of a bankruptcy case. *See* KAREN GROSS, FAILURE AND FORGIVENESS: REBALANCING THE BANKRUPTCY SYSTEM 291 (Yale University Press 1997).

112. *See Andresen*, 232 B.R. at 130-31.

113. *See id.* at 131.

114. *See* 11 U.S.C. § 105(a) (1994), which provides, "The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title . . . shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate . . . to prevent an abuse of process."

115. *See Kapinos v. Graduate Loan Ctr. (In re Kapinos)*, 243 BR 271 (W.D. Va. 2000).

116. *See Andresen*, 232 B.R. at 131.

117. *See id.*

118. *See id.*

119. *See id.* at 129.

The most compelling reason for allowing partial discharge or other revision of student loans is fairness.[120] In borderline cases, partial discharge makes it possible for the court to discharge those portions of student loan debt that are causing the debtor's "undue hardship" while requiring the debtor to continue repayment of the remaining student loan debt.[121] Partial discharge promotes fairness by affording some relief to the debtor, while ensuring that the government is not unjustly deprived by a complete discharge of student loans that could be repaid in part without imposing "undue hardship."[122]

Since October 7, 1998, it appears that only one court has recognized the full importance of the repeal of the seven-year discharge as it relates to "undue hardship."[123] In *Andresen*, the debtor, Donna Mae Andresen, obtained three student loans in three consecutive years while attending nursing school.[124] Andresen filed her Chapter Seven bankruptcy petition in 1991.[125] From time to time, Andresen had incurred extraordinary medical expenses as a result of her daughter's medical condition.[126] Andresen's regular expenses included caring for her two children and paying off a second mortgage.[127] During the course of her bankruptcy case, Andresen sustained a severe back injury that made it impossible for her to find work in her home state of Nebraska.[128] After a nationwide job search, Andresen finally found an

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120. *See* Collins, *supra* note 20, at 753.

121. *See id.* The Sixth Circuit Court of Appeals recently held that § 105(a) of the Bankruptcy Code grants the court authority to partially discharge student loans, to institute a repayment schedule modifying the repayment terms of the loan, to defer repayment, to allow the debtor to subsequently re-open the proceedings to argue for "undue hardship" discharge, or to fashion any appropriate remedy. *See* Tennessee Student Assistance Corp. v. Hornsby (In re Hornsby), 144 F.3d 433, 439-40 (6th Cir. 1998). The Sixth Circuit stated that in a case "where undue hardship does not exist, but where facts and circumstances require intervention in the financial burden on the debtor, an all-or-nothing treatment thwarts the purpose of the Bankruptcy Act." *Id.* at 439. Although the court's intentions were honorable, its reasoning leaves an important question unanswered: If the facts and circumstances of a particular case are so grave as to require the court to exercise its equitable powers, why should the court be constrained from concluding that "undue hardship" has been established?

122. *See* Collins, *supra* note 20, at 753-54. *But see* GROSS, *supra* note 111, at 154-55 (arguing that the government's status as a priority creditor should be reconsidered, given the government's better position to recapture bankruptcy losses than other creditors, such as employees).

123. *See Andresen*, 232 B.R. at 130 n. 7.

124. *See id.* at 129.

125. *See id.*

126. *See id.* at 141.

127. *See id.*

128. *See id.* at 129.

employer willing to accommodate her disability in Nevada, where she moved to take that job.[129]

After a trial on Andresen's student loans, the bankruptcy court discharged two of her three loans, concluding that she could repay the third loan without "undue hardship."[130] On appeal, the Nebraska Student Loan Program argued that the bankruptcy court erred by finding that two of Andresen's student loans would impose "undue hardship" if they were not discharged, and that the bankruptcy court had no authority to grant a partial discharge.[131] Without deciding whether a partial discharge is authorized by § 523(a)(8), the Bankruptcy Appellate Panel for the Eighth Circuit held that application of the "undue hardship" test to each student loan separately was not only allowed, but was required.[132] Consequently, the bankruptcy court had not even ordered a partial discharge in the traditional sense.[133] Significantly, the *Andresen* court observed:

> That the original statute contemplated a point at which a debtor could discharge student loans completely and without a showing of undue hardship may explain the apparent all-or-nothing approach to the undue hardship discharge exception. Congress simply wasn't contemplating any situation in which a loan would require revision by a bankruptcy court because either a loan would be fully dischargeable before the five (or seven) years on the basis of undue hardship, or it would be fully dischargeable in any event upon expiration of the applicable number of years. Under the original statute, therefore, a debtor would be unlikely to seek relief in bankruptcy prior to the expiration of the applicable number of years since repayment on a student loan became due, unless the debtor's undue hardship made it imperative.[134]

The critical observation made by the court in *Andresen* is that throughout the cases where courts have granted equitable relief to student

129. *See id.*

130. *See id.*

131. *See id.*

132. *See id.* at 137, 141. One significant reason underlying the Andresen decision was the court's conclusion that the determination of "undue hardship" is a factual determination reversible only for clear error. *See id.* at 128. Other courts have concluded that the determination of "undue hardship" is a question of law subject to de novo review. *See e.g., Cheesman,* 25 F.3d at 359.

133. *See Andresen,* 232 B.R. at 141.

134. *Id.*

loan debtors, those courts lacked any compelling reason to alter the standard for "undue hardship."[135] First, courts did not even arrive at the question of equitable relief until they had already determined that the debtor did not qualify for the "undue hardship" exception.[136] Second, courts did not view the issue as whether the standard for establishing "undue hardship" was too high; rather, the issue was whether the policies behind non-dischargeability could be promoted while giving some deference to the fresh start policy at the same time.[137]

Courts were satisfied that the tests for proving "undue hardship" could not be too restrictive because that was just one of two ways for debtors to have their loans discharged.[138] In any case where a debtor could not prove "undue hardship" before the expiration of the five or seven year period, the loan would be automatically discharged absent that showing as soon as the applicable time period expired.[139]

That logic breaks down now that the seven-year discharge exception has been repealed.[140] Without a seven-year automatic discharge to protect debtors, it is now incumbent on the courts to reconsider whether "undue hardship" can continue to be interpreted as restrictively as in the past.[141]

The National Bankruptcy Review Commission[142] has gone even further by recommending the total repeal of § 523(a)(8).[143] In its report the commission first traced the history of § 523, noting that originally there was only a short list of exceptions to discharge for certain kinds of wrongdoing.[144] These types of wrongdoing included fraud, defalcation, and intentional torts.[145] Over time, the list of exceptions

135. *See Andersen*, 232 B.R. at 141.

136. *See* Collins, *supra* note 20, at 753.

137. *See Andresen*, 232 B.R. at 130-31.

138. *See id.* at 130 n. 7.

139. *See id.*

140. *See id.*

141. *See id.*

142. The National Bankruptcy Review Commission is an independent commission established pursuant to the Bankruptcy Reform Act of 1994. It was created to investigate and study issues relating to the Bankruptcy Code, to solicit divergent views concerning the operation of the bankruptcy system, to evaluate proposals with respect to bankruptcy issues, and to prepare a report that was submitted to the President, Congress, and the Chief Justice on October 27, 1997. *See* National Bankruptcy Review Commission at, http://www.nbrc.gov(last modified Nov. 26, 1997). The Commission ceased to exist on November 19, 1997. *See id.*

143. *See* NATIONAL BANKRUPTCY REVIEW COMMISSION FINAL REPORT, BANKRUPTCY: THE NEXT TWENTY YEARS (1997), *reprinted in* [Vol. G] COLLIER ON BANKRUPTCY 44-219-229 (15th ed. revised 1999).

144. *See id.* at 44-193.

145. *See id.*

has grown to nearly twenty, mostly as a result of special interest amendments.[146]

The commission then suggested a number of specific reasons why § 523(a)(8) should be repealed. First, the commission found it unfair that a debtor overloaded with consumer debts incurred to by "a car, a vacation, or a pizza" can resort to bankruptcy but a debtor who borrows to pay for tuition and books cannot.[147] Thus, the repeal of § 523(a)(8) would make the treatment of most student loans similar to the treatment of all other unsecured debts.[148] Repeal of § 523(a)(8) would also be consistent with federal policy to encourage educational endeavors.[149] Additionally, Chapter Thirteen debtors who had made diligent efforts to repay their loans would no longer be penalized after the completion of a bankruptcy plan with thousands of dollars of compound interest.[150] Finally, litigation over "undue hardship" would finally be eliminated, and discharge of student loans would no longer be denied to those who need it most.[151]

## V. Conclusion

The existing tests for "undue hardship" under § 523(a)(8) of the Bankruptcy Code were developed in the context of an automatic discharge for seven-year old student loans that could not be repaid. Now that "undue hardship" is the only way for debtors to seek discharge of student loans, courts should reassess and lower that standard. Although it may have sufficed in the past for courts to use their equitable powers to lessen the impact of § 523(a)(8), the repeal of the seven-year discharge means that debtors need to have a realistic chance of proving "undue hardship." Otherwise, they will have no way out.

*Scott Pashman*

146. *See id.*
147. *See id.* at 44-220.
148. *See id.* at 44-229.
149. *See id.*
150. *See id.*
151. *See id.*