The Student Loan Discharge Crisis: How We Got Here and Where Do We Go?

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As overall consumer debt has increased over the years, student loan debt has correspondingly increased to astronomical levels. In 2019, 45 million borrowers collectively owed more than $1.5 trillion in student loan debt.[1] By comparison, in 2005 – the year the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) went into effect – student loan debt was $391 billion with 24.7 million borrowers. The delinquency rate has increased as well. The percentage of loans that are 90+ days delinquent has increased from around 6.5% in 2005 to 11.4% in 2019.[2] These numbers beg the question: how did we get here and what can we do to mitigate the crisis.

A solution may come in the form of legislation as the student loan crisis has become a significant issue in today's politics. However, while debtors wait for legislative action, the courts are left to grapple with this mounting crisis, under the weight of what many believe to be an outdated interpretation of the student loan discharge provisions of the Bankruptcy Code.

This paper explores the history of student loan discharge in bankruptcy courts from pre-*Brunner* days to some recent cases that show some change in the way courts are reacting to the student loan debt crisis. This paper also aims to predict where the courts might be headed and whether debtors can look to other solutions for relief.

[1] U.S. Federal Reserve, G.19: Consumer Credit Release, (last visited July 17, 2020), https://www.federalreserve.gov/releases/g19/current/default.htm
[2] Federal Reserve Bank of New York, Quarterly Report on Household Debt and Credit, (last visited July 17, 2020), https://www.newyorkfed.org/microeconomics/databank.html

I. History of Student Loan Debt Discharge

a. Pre-*Brunner*

A look at the history of the case law governing student loan debt discharge shows that the turning point was the seminal case of *In re Brunner*, 46 B.R. 752 (S.D.N.Y 1985), aff'd, *Brunner v. New York Higher Educ. Servs. Corp.*, 831 F.2d 395 (2d Cir. 1987). Before 1987 – the year *Brunner* was decided – the only restriction to discharging student loan debt was the five-year prohibition on dischargeability enacted by Congress in 1976. Prior to 1976, student loan debt was dischargeable like any other unsecured debt dischargeable in bankruptcy.

In response to concerns that debtors were abusing the dischargeability of their student loans, Congress enacted the Education Amendments Act in 1976 and put a five-year prohibition on student loan debt discharge. The Act prohibited student loan debt from being discharged during the first five years of repayment unless a debtor could show undue hardship. This five-year exception to discharge was later codified in 11 U.S.C. § 523(a)(8) when the Bankruptcy Code was enacted two years later in 1978.

b. *In re Brunner*

After the five-year limitation on student loan discharge took effect, a series of cases culminating in the seminal *Brunner* case, which established a harsh "undue hardship" standard for the discharge of student loans.

Marie Brunner sought to discharge her student loan debts nine months after receiving her master's degree and shortly before the due date of her first payment. She had $9,000 of student loan debt, made no efforts to pay anything on her loans and had been unemployed for only a few months before seeking relief. The facts in *Brunner* were the types of facts in student loan debt discharge cases at that time that had led to an increasing call for reform. The *Brunner* court

aimed to stop this continued "abuse" of the bankruptcy system by narrowly defining the "undue hardship" standard that must be met by debtors who wished to discharge their loans prior to the five-year exception to discharge. The policy's goal was to prevent recent graduates from escaping their student loan obligations prior to entering lucrative careers, a serious concern in the 1970s and 1980s.

To prove undue hardship, the *Brunner* test requires a three-part showing. The debtor must prove by a preponderance of the evidence that: (1) the debtor cannot maintain, based on current income and expenses, a "minimal" standard of living for themselves and their dependents if forced to repay the loans; (2) additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans; and (3) the debtor has made good faith efforts to repay the loans.[3] Each element of the *Brunner* test is a standalone requirement and must be satisfied. This test effectively made student loan discharge almost impossible for the first five years of repayment, giving rise to the now infamous "certainty of hopelessness" phrase used to describe the financial state debtors must find themselves in to have a chance at student loan dischargeability.[4] Nine circuits have adopted the *Brunner* test in deciding the fate of debtors looking to discharge their student loans.

c. Post-*Brunner*

Three years after the *Brunner* decision, Congress amended the Code to extend the five-year exception to seven years. In 1998 the exception became unlimited in time when the Code was amended to provide that federally guaranteed loans could not be discharged *at all* unless the

[3] *In re Brunner*, 46 B.R. 752 (S.D.N.Y 1985), aff'd, *Brunner v. New York Higher Educ. Servs. Corp.*, 831 F.2d 395 (2d Cir. 1987).

[4] Although *Brunner* never uses the phrase "certainty of hopelessness," courts following the *Brunner* test have quoted the phrase in conjunction with the case, leaving many to mistakenly believe that the language derives directly from the *Brunner* case.

debtor could prove undue hardship. In 2005, Congress extended this exception to private loans with the enactment of BAPCPA.

Despite all the changes in the law, the test has remained the same. The now unlimited-by-time exception and increasing student loan repayment periods result in debtors accruing interest over 30 to 40-year repayment periods. This results in many debtors paying off close to, if not, all the principal amount of their loan but still owing enormous amounts of interest.

Despite the Code amendments and the increasing burden of student debt, bankruptcy courts were reluctant to depart from the *Brunner* test. More recently, however, bankruptcy judges throughout the circuits have begun to whittle down the *Brunner* test. Some have outright rejected the *Brunner* test, giving hope to debtors who are looking for change in the way the law views the dischargeability of student loan debt.

II. How Courts are Fighting Back Against *Brunner*

Recently, courts have been pushing back on *Brunner* and the onerous requirements it imposes on debtors. The pushback ranges from mild criticism of the *Brunner* test to outright rejections of the test. The Second Circuit has yet to overrule *Brunner*. But with criticism from judges across the country, some from courts in the Second Circuit, the *Brunner* test in its present form may soon become a thing of the past.

Judges across jurisdictions have voiced their growing disdain for the "certainty of hopelessness" standard and have begun adopting other tests. A Massachusetts bankruptcy court described the requirement to show "unique" or "extraordinary" circumstances, perpetuated by *Brunner* courts, as overkill.[5] A Maine bankruptcy court stated that to "conclude that the debtor must demonstrate something approaching a 'certainty of hopelessness' or 'total incapacity'

[5] *Hicks v. Educ. Credit Mgmt. Corp.*, 331 B.R. 18, 27 (Bankr. D. Mass 2005) (*Hicks*).

would be to sacrifice the notion of 'fresh start' at the altar of 'undue hardship.'"[6] Along with their criticism, the *Hicks* court and the equally critical *Kopf* court rejected the *Brunner* test and adopted the "totality of the circumstances" test, first articulated in the Eight Circuit by *In re Andrews*.[7]

The debtor in *Hicks* had been paying his student loans for close to 10 years, and the debtor in *Kopf* had been paying for more than 10 years. Both debtors had children; Kopf was a single parent, and Hicks had two children with physical ailments. Hicks also had personal health issues. The totality of the circumstances test allowed both courts to consider all these factors in considering whether the debtors would face undue hardship.

Following decisions such as *Kopf* and *Hicks*, the Bankruptcy Appellate Panel for the First Circuit adopted the "totality of the circumstances" test in 2010.[8] In *Bronsdon*, the debtor was 64 years old at the time of her discharge trial, had received her bachelor's degree at the age of 50 and 11 years later received her law degree. The debtor had failed the bar exam multiple times and, despite her efforts to find employment, she had not succeeded. At the time of trial, her only income was a monthly Social Security payment, and her student loans totaled $82,049.45. The BAP acknowledged that the First Circuit had yet to adopt a test, conducted an analysis of the *Brunner* and "totality of circumstances" tests and stated that "*Brunner* takes the test too far" because of the third prong requiring the debtor to prove "good faith efforts."[9] As a result, the BAP affirmed the bankruptcy's court decision in discharging the debtor's student loan debt.

6 *Kopf v. United States Dep't. of Educ.*, 245 B.R. 731 (Bankr. D. ME 2000) (*Kopf*).
7 *Andrews v. S.D. Student Loan Assistance Corp.*, 661 F.2d. 702 (8th Cir. 1981).
8 *Bronsdon v. Educ. Credit Mgmt. Corp.*, 435 B.R. 791 (1st B.A.P. 2010).
9 *Id.*, at 801.

The Eight Circuit, which created the "totality of the circumstances" test, reaffirmed its use of that test and expressly refused to apply *Brunner* in *Long v. Educational Credit Management Corp*.[10] The debtor in *Long* was a single mother who owed $61,000 in student loan debt that accumulated after she was no longer able to pay due to illness. The debtor had made payments for approximately ten years prior to her illness that eventually led her to default on her loans. The court quickly disposed of the *Brunner* test by stating that 'adhering to such strict parameters diminish[es] the inherent discretion contained in 11 U.S.C. § 523(a)(8)' and that '[the Court] believes that fairness and equity require each undue hardship case to be examined on the unique facts and circumstances that surround the particular bankruptcy.'"[11]

Other Circuits, such as the Ninth and Seventh, have followed suit and have moved towards a more wholistic approach to determining what constitutes "undue hardship." The Ninth Circuit BAP in *Roth v. Education Credit Mgmt. Corp*. discharged the debtor's student loan debts after reviewing her circumstances and stating that her failure to negotiate or accept an alternate payment is not dispositive of the required good faith finding.[12] In *Roth*, the debtor was 64 years old and seeking to discharge $95,000 in student loan debt that she had incurred 15 years earlier. The debtor cited physical and mental ailments as barriers to repayment, and the court noted that even under the alternate payment plan offered by the lender, the debtor would be paying nothing at the moment because of her financial situation, thus further requiring relief.[13]

In his concurrence in *Roth*, Judge Pappas agreed with the majority that the debtor should be granted a discharge, but went on to carefully analyze the changes in student loan lending and

[10] *Long v. Educational Credit Management Corp*., 322 F.3d 549 (8th Cir. 2003).
[11] *Id.* at 554.
[12] *Roth v. Educ. Credit Mgmt. Corp.*, 490 B.R. 908 (B.A.P. 9th Cir.).
[13] *Id.* at 919-20.

the Code, calling the analysis required by *Brunner* "too narrow and no longer [reflective of] reality." Judge Pappas' concurrence called for a revision by the Ninth Circuit of the *Pena/Brunner* standard, stating that "in this era, bankruptcy courts should be free to consider the totality of a debtor's circumstances in deciding whether a discharge of student loan debt for undue hardship is warranted."[14] Judge Pappas continued by comparing the student loan crisis to the "recent mortgage crisis" and reiterating that a hardship test requiring those who cannot pay to continue to pay is hurting us all.[15]

The Seventh Circuit also refused to recognize the concept that an unwillingness to agree to future income-based repayment plans resulted in a failure to meet the "good faith" requirement of the *Brunner* test.[16] The court stated that if good faith entailed commitment to future efforts to repay, as the district judge insisted, no educational loan could ever be discharged because it would "always be possible to pay in the future should prospects improve."[17] The decision, written by Judge Easterbrook, referred to the language in *Brunner* as "judicial gloss" over the text of 11 U.S.C. § 523(a)(8) and cautioned against interpretations that superseded the statute. Judge Easterbrook noted that the statutory language does not forbid discharge as a whole but makes it possible when payment would cause "undue hardship."[18]

Recently, lower courts in the Seventh Circuit have begun using a more relaxed interpretation of the *Brunner* test. In *Bukovics v. Navient*, the Bankruptcy Court for the Northern District of Illinois, Eastern Division discharged $72,674.2 in student loan debt for a debtor who had taken measures to drastically reduce her expenses, had difficulty finding jobs due to her age,

[14] *Id.* at 920.
[15] *Id.* at 923.
[16] *Krieger v. Educ. Credit Mgmt. Corp.*, 713 F.3d 882 (7th Cir. 2013).
[17] *Id*. at 884.
[18] *Id.*

and had a poor work history and had no income at the time of trial.[19] The court compared the debtor in *Krieger* to the debtor in this case, and found that the debtor's circumstances proved that she would face undue hardship if she were forced to repay the loan.

In *Bukovics*, Judge Schmetterer included statistics on the current student loan market and the changes in the law since *Brunner*. The opening line of the decision calls student loan debt a "crushing burden" and a "financial obstacle" for many people in the United States.[20] Judge Schmetterer discussed the average amount of student loan debt debtors carry today and compared it to the average student loan debt from 1992-1993. Judge Schmetterer, similar to Judge Pappas' concurrence, put into perspective the massive burden debtors carry into courts when trying to discharge their student loans.

Roth, *Krieger* and *Bukovics* show a shift towards judicial activism and a relaxation of application of the *Brunner* standards in light of the pervasive burden of student loan debt. All three courts reinterpreted *Brunner* by shifting the narrative from the "certainty of hopelessness" standard to a more reasonable statutory reading of 11 U.S.C. § 523(a)(8) without the harsh "judicial gloss" of the *Brunner* test developed under substantially different circumstances. The fact that Judge Pappas and Judge Schmetterer allude to the student loan debt crisis in their opinions show that courts are aware of the current situation.

Even courts in the Second Circuit have criticized the *Brunner* decision. In *Kraft v. New York State Higher Educ. Servs. Corp.*, 161 B.R. 82 (Bank. W.D. N.Y. 1993), the bankruptcy court called the "certainty of hopelessness" standard "excessive," claiming that it would be hard to believe persons with a "certainty of hopelessness" are not afflicted with too much despair to

[19] *Bukovics v. Navient*, 2020 Bankr. LEXIS 540 (Bankr. N.D. Ill. 2020).
[20] *Id.*, at 177.

file a bankruptcy petition.[21] The debtor was a 38 year old divorced female who had three children who did not live or depend on her, was employed as a school bus driver and making $6.36 per hour. Despite criticizing the "certainty of hopelessness" standard, the court found that the debtor had applied for discharge "too soon" and without considering all her options for employment outside of a specific field.[22]

More recently, in January of 2020, Chief Judge Morris of the Bankruptcy Court of the Southern District of New York used *Brunner* to discharge $221,385.49 of student loans while criticizing the interpretations of *Brunner* throughout the years that have made the case synonymous with hopelessness. Judge Morris states that "retributive dicta were applied and reapplied so frequently in the context of *Brunner* that they have subsumed the actual language of the *Brunner* test…and this Court will not participate in perpetuating those myths [that discharge of student loans is impossible]."[23] *Rosenberg* is now on appeal to the district court. Although the Second Circuit has not overruled *Brunner*, with opinions such as Judge Pappas' concurrence in *Roth* and Judge Schmetterer's decision in *Bukovics*, it seems only a matter of time before *Brunner* is revisited.

III. What Can Debtors Expect for the Future?

Recently, two courts have applied the notion of a "partial discharge" to ease the amount that debtors would have to repay. The court in *In re Modeen* found that the debtor had failed to demonstrate an undue hardship for a full discharge under *Brunner* but because a reduction in her expenses would still make it difficult for her to make full payments on her loan, the debtor was

[21] *Kraft v. New York State Higher Educ. Servs. Corp.*, 161 B.R. 82, fn. 2 (Bankr. W.D.N.Y. 1993).
[22] *Id.*, at 86-87.
[23] *Rosenberg v. N.Y. State Higher Educ. Servs. Corp.*, 610 B.R. 454, 459 (Bankr. S.D.N.Y. 2020), on appeal.

granted a partial discharge.[24] The debtor in *Modeen* had refinanced her student loans with loans from her employer, and the parties agreed that the new loans would still retain their character as education loans after the refinancing. The court conducted a *Brunner* analysis and determined that the debtor could not meet a minimal standard of living but considering her age (mid-30s) and her earning potential, the debtor could reasonably repay some portion of the loan. Thus, the court chose the "partial discharge" option giving the debtor the opportunity to satisfy the portion of the loan that she would pay.

In *In re Clavell,* Judge Wiles ordered a partial discharge for a debtor eliminating all the accrued interest and a portion of the outstanding principal of the student loan debt so that the debtor would only pay a $250 monthly payment under a standard 25-year repayment plan.[25] The debtor owed more than $96,000 in student loan debt, was 35 years old at the time of trial, employed and receiving a stable income. However, the court specifically pointed to the "certainty of hopelessness" standard and acknowledged that it did not arise from *Brunner* itself, and reiterated that the second prong of *Brunner* only requires the presence of "any circumstances, beyond the mere current inability to pay, that show that the inability to pay is likely to persist for a significant portion of the repayment period."[26] The court found that the debtor's evidence showed that he would not be able to repay his student loans and that his budget would in fact get tighter over time, requiring some sort of relief.

It is important to point out that both debtors in the partial discharge cases were in their 30s, employed and able to make some sort of payment towards their loans if partial discharge were provided. Thus, debtors in similar situations might find partial relief in bankruptcy courts if

[24] *Manion v. Modeen (In re Modeen)*, 586 B.R. 298, 308 (Bankr. W. D. Wis. 2018).
[25] *Clavell v. United States Dep't of Educ. (In re Clavell)*, 611 B.R. 504 (Bankr. S.D.N.Y 2020).
[26] *Id.*, at 529.

they can prove that despite their employment and steady income, other circumstances exist that make meeting a minimum standard of living difficult, and that their current situation is likely to persist.

The growing willingness of courts to find a way to provide relief from student loan debt in appropriate cases provides a sliver of hope for those carrying astronomical amounts of debt into the future. But does this trend also mean that *Brunner* will be overruled? And, what can borrowers currently in repayment, students currently amassing student loan debt, and students who are finding ways to finance their education, expect for the future?

From the way courts are pushing back on *Brunner*, it may be that *Brunner* will soon meet a head-on challenge that will force the Second Circuit to revisit the *Brunner* test. In that case, the courts may shift to the "totality of the circumstances" test as a better measure of actual need for relief from student loan debt.

Moreover, in advancing their own interests, financial institutions may support efforts to alleviate student loan debt. A national survey conducted by Apartment List in 2019, showed that 12% of 10,000 millennials surveyed across the country stated that they planned on renting housing for the rest of their lives.[27] Of the 12% who stated they were planning on renting for life, 69% cited affordability as the major barrier to home ownership. Economists at the Federal Reserve have also asserted that low homeownership numbers are likely due to the increase in student loan debt.[28] Such studies and surveys may push banks and other financial instiutions to

[27] Apartment List, 2019 Millennial Homeownership Report, (last visited July 17, 2020) https://www.apartmentlist.com/rentonomics/2019-millennial-homeownership-report/

[28] Consumer and Community Context, Can Student Loan Debt Explain Low Homeownership Rates for Young Adults?, Federal Reserve, January 2019. https://www.federalreserve.gov/publications/files/consumer-community-context-201901.pdf?mod=article_inline

lobby for some sort of legislation for relief of student loan debt to stimulate housing and other parts of the economy that are likely to experience a decline if the student loan crisis constinues to persist and grow at its current pace.

IV. Conclusion

Although *Brunner* still stands as binding precedent in most circuits, the trend of courts to depart from a strict interpretation of *Brunner* seems to be growing. As the student loan crisis becomes even more burdensome on the economy, it is likely that courts will continue moving away from *Brunner* and make it easier for debtors to discharge their student loan debt. Even if *Brunner* is not overruled, debtors can seek alternative ways to discharge their student loan debt, such as partial discharges or participating in student loan mediation programs such as the one announced in the Second Circuit after Judge Morris' *Rosenberg* decision.

Until *Brunner* is overruled, it is up to debtors to convince judges that their mounting student loan debts and the circumstances surrounding their failure to repay those loans are an "undue hardship" that would require relief under a modern test for "undue hardship." In the meantime, debtors and bankruptcy professionals can advocate for relief by seeking to convincing politicians and financial institutions that the burden of student loans is hurting the economy as much as it is hurting the students who amass these loans.