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## Preserving the Promise of Higher Education: Ensuring Access to the "American Dream" Through Student Debt Reform

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# ESSAY

## PRESERVING THE PROMISE OF HIGHER EDUCATION: ENSURING ACCESS TO THE “AMERICAN DREAM” THROUGH STUDENT DEBT REFORM

*Bryan D. Watson*\*

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In the pursuit of the “American Dream,” a college education is presumed to open doors to a prosperous post-graduation life. However, that is simply not the case for millions of Americans. Instead, as now-U.S. Senator Elizabeth Warren has proclaimed, “[i]ncreasingly, students must begin their adult lives with debts that outstrip their earning potential, creating a financial vortex from which they may never escape.”<sup>1</sup>

Senator Warren’s observation is from seven years ago—and since then, the situation has gotten significantly worse. Despite the individual and societal benefits gained from higher education, the economic burden created by student borrowing has created a drag on the American economy since the 2008 recession,<sup>2</sup> threatening trouble for the country’s

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\* Colonel, U.S. Air Force JAG Corps. The views expressed in this Essay are those of the author and do not reflect the official policy or position of the Department of Defense or the U.S. Government.

1. Elizabeth Warren et al., *Service Pays: Creating Opportunities by Linking College with Public Service*, 1 HARV. L. & POL’Y REV. 127, 130 (2007).

2. According to the U.S. Department of Commerce’s Bureau of Economic Analysis, the

future well-being. In response, our society must come to grips with policy alternatives to deep student indebtedness, and implement those which can get immediate help to student borrowers and still pave the way for continued access to higher education. The rationale is clear; if large numbers of new job market entrants continue to struggle financially and are unable to fully enter the economic mainstream, we will all suffer.

## I. MAGNITUDE OF THE PROBLEM AND NATIONAL SECURITY IMPLICATIONS

Student loans' outstanding amounts have now topped \$1 trillion.<sup>3</sup> This sum is still growing and has even exceeded the total amount of credit card debt in America.<sup>4</sup> Moreover, 11.5% of the debt is more than 90 days delinquent or in default,<sup>5</sup> with one in ten borrowers defaulting in their first two years of repayment and one in seven defaulting in the first three years.<sup>6</sup> Overall, this is the highest delinquency rate for all forms of American debt and the only form of U.S. consumer debt that has risen consistently since 2003.<sup>7</sup> Because of high levels of indebtedness, many borrowers are delaying or declining to engage in major life and economic

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growth rate of the U.S. Gross Domestic Product (GDP) continues to hover in the low single-digit percentages. The third quarter of 2013 growth rate was 4.1%, and the fourth quarter of 2013 was 2.6%. See U.S. DEPARTMENT OF COMMERCE AND BUREAU OF ECONOMIC ANALYSIS, *U.S. Economy at a Glance: Perspective from the BEA Accounts*, available at <https://www.bea.gov/newsreleases/glance.htm>, (last visited Nov. 24, 2014); see also U.S. DEPARTMENT OF COMMERCE AND BUREAU OF ECONOMIC ANALYSIS, *Gross Domestic Product (GDP) Graph*, available at [http://www.bea.gov/newsreleases/national/gdp/gdp\\_glance.htm](http://www.bea.gov/newsreleases/national/gdp/gdp_glance.htm) (last visited Nov. 24, 2014).

3. Sam Frizell, *Student Loans Are Ruining Your Life. Now They're Ruining the Economy, Too*, TIME, Feb. 26, 2014, available at <http://time.com/10577/student-loans-are-ruining-your-life-now-theyre-ruining-the-economy-too/> (last visited Nov. 17, 2014).

4. Halah Touryalai, *Student Loan Problems: One Third of Millennials Regret Going to College*, FORBES, May 22, 2013, available at <http://www.forbes.com/sites/halahtouryalai/2013/05/22/student-loan-problems-one-third-of-millennials-regret-going-to-college/> (last visited Nov. 17, 2014).

5. See Floyd Norris, *The Hefty Yoke of Student Loan Debt*, N.Y. TIMES, Feb. 20, 2014, available at <http://www.nytimes.com/2014/02/20/business/economy/the-hefty-yoke-of-student-loan-debt.html> (last visited Nov. 17, 2014). Student loan default is defined as the result of failure to make payments on a student loan as scheduled according to the terms of the underlying promissory note, the legal agreement made at the time of the underlying student loan. U.S. DEPARTMENT OF EDUCATION AND FEDERAL STUDENT AID, *Federal Student Aid: Understanding Default*, available at <http://studentaid.ed.gov/repay-loans/default> (last visited Nov. 24, 2014).

6. Shahien Nasirpour & Chris Kirkham, *Student Loan Defaults Surge to Highest Level in Nearly 2 Decades*, HUFFINGTON POST, Sept. 30, 2013, available at [http://www.huffingtonpost.com/2013/09/30/student-loans-default\\_n\\_4019806.html](http://www.huffingtonpost.com/2013/09/30/student-loans-default_n_4019806.html) (last visited Nov. 17, 2014).

7. Halah Touryalai, *\$1 Trillion Student Loan Problem Keeps Getting Worse*, FORBES, Feb. 21, 2014, available at <http://www.forbes.com/sites/halahtouryalai/2014/02/21/1-trillion-student-loan-problem-keeps-getting-worse/>.

decisions such as getting married, having children, purchasing a home,<sup>8</sup> or even starting a small business<sup>9</sup> until they are in a more secure financial situation.

Even more troubling, student loan debt is increasingly wide-spread. A full 42% of American millennials report that they, or someone in their household, has student debt, and 57% feel that student loan debt is a major societal problem.<sup>10</sup> Such opinions are understandable, given that the average student debt of a new college graduate is about \$30,000 today,<sup>11</sup> compared to just \$17,233 in 2005.<sup>12</sup> These sums can be particularly daunting for the increasing numbers of young adults who are encountering difficulties finding productive post-graduation employment.<sup>13</sup> In fact, the number of recent college graduates who are unemployed or underemployed has risen steadily since 2001, and the quality of their jobs has declined as well, with recent graduates increasingly taking low-wage or part-time positions.<sup>14</sup> Student loan debt can be outright devastating for the nearly 50% of college students who drop out of college before earning their degree, because they incur substantial financial obligations without the economic benefit of an additional academic credential.<sup>15</sup>

Even in light of the foregoing, large-scale access to higher education is a national security and economic imperative.<sup>16</sup> In recognition of that

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8. Hadley Malcom, *Millennials' Ball-and-Chain: Student Loan Debt*, USA TODAY, July 1, 2013, available at <http://www.usatoday.com/story/money/personalfinance/2013/06/30/student-loan-debt-economic-effects/2388189>.

9. See generally U.S. SMALL BUSINESS ADMINISTRATION, *STUDENT START-UP PLAN*, available at <http://www.sba.gov/startupamerica/student-startup-plan> (last visited Nov. 24, 2014) (explaining the "Income-Based Repayment Plan," a federally funded program designed to lower loan payments for graduates looking to start their own business).

10. Adam Levin, *Politicians Ignoring Student Loan Crisis Do So at Their Risk*, ABC NEWS, Dec. 15, 2013, available at <http://abcnews.go.com/Business/politicians-ignore-millennial-student-loan-crisis/story?id=21195661>.

11. *Id.*

12. Touryali, *supra* note 7.

13. In November 2012, the unemployment rate for a 2012 graduate was 11.6%; for those in the 16-24 age bracket who are employed, the average annual earnings was \$21,000 for women and approximately \$24,000 for men. Levin, *supra* note 10.

14. Lawrence Mishel & Richard Rothstein, *Unemployment, Schools, Wages, and the Mythical Skills Gap*, ECON. POL'Y INST., Apr. 2, 2014, available at <http://www.epi.org/blog/unemployment-schools-wages-mythical-skills/>.

15. See, e.g., Kelsey Sheehy, *Student Loan Repayment Tips for College Dropouts*, U.S. NEWS & WORLD REP., June 12, 2013, available at <http://www.usnews.com/education/best-colleges/paying-for-college/articles/2013/06/12/student-loan-repayment-tips-for-college-dropouts> (last visited Nov. 24, 2014).

16. For an explanation of the role that higher education will play in the global economy in coming years, see generally *Knowledge and Skills for the Jobs of the Future*, THE WHITE HOUSE, <http://www.whitehouse.gov/issues/education/higher-education> (last visited Nov. 24, 2014):

fact, federal participation in higher education lending stems from the mid-20th century, when the aptly-named National Defense Education Act of 1958<sup>17</sup> authorized loans to higher education students in order “to *strengthen the national defense* and to encourage and assist in the expansion and improvement of educational programs to meet *critical national needs*.”<sup>18</sup> Since then, federally-supported lending has increased steadily, but it surged dramatically in the decade from 2003–2013; during that period, federal lending nearly doubled.<sup>19</sup>

The explanation for this increase reflects how the rise in both federal lending and student borrowing kept pace with the escalating cost of higher education. A primary reason for the latter is that the amount of legislative contributions to public higher education plummeted in the last decade because of serious state budgetary shortfalls. Because 80% of U.S. students enrolled in degree-granting, nonprofit colleges attend publicly-funded institutions, tuition increases in these schools had an immediate effect on a large swath of students; thus, it is no surprise that trend lines between student tuition costs and legislatures’ decisions to redirect public funds elsewhere correspond with the spike in student loan outlays.<sup>20</sup> To illustrate: between 2007 and 2012, tuition at public four-

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Earning a post-secondary degree or credential is no longer just a pathway to opportunity for a talented few; rather, it is a prerequisite for the growing jobs of the new economy. Over this decade, employment in jobs requiring education beyond a high school diploma will grow more rapidly than employment in jobs that do not; of the 30 fastest growing occupations, more than half require postsecondary education. With the average earnings of college graduates at a level that is twice as high as that of workers with only a high school diploma, higher education is now the clearest pathway into the middle class. In higher education, the U.S. has been outpaced internationally. In 1990, the U.S. ranked first in the world in four-year degree attainment among 25-34 year olds; today, the U.S. ranks 12th. We also suffer from a college attainment gap, as high school graduates from the wealthiest families in our nation are almost certain to continue on to higher education, while just over half of our high school graduates in the poorest quarter of families attend college. And while more than half of college students graduate within six years, the completion rate for low-income students is around 25 percent.

*Id.*

17. National Defense Education Act, Pub. L. No. 85-864, 72 Stat. 1580.

18. *Id.* (emphasis added).

19. See COLL. BD., TRENDS IN STUDENT AID 2013, tbl. 1, *Total Student Aid and Nonfederal Loans Used to Finance Postsecondary Education Expenses in 2012 Dollars, 2002-2003 to 2012-2013*, available at <http://trends.collegeboard.org/sites/default/files/student-aid-2013-full-report.pdf> (last visited Nov. 24, 2014). During this timeframe, the total amount of annual federal loans grew from \$54.67 billion to \$101.469 billion between 2002–2003 and 2012–2013.

20. See generally BILL ZIMMERMAN, THE STUDENT LOAN SWINDLE: WHY IT HAPPENED – WHO’S TO BLAME – HOW THE VICTIMS CAN BE SAVED (2014).

year institutions increased by more than 15% in 40 states, more than 25% in 18 states, more than 50% in seven states, and, incredibly, public university tuition in California and Arizona during this period grew by more than 70%.<sup>21</sup> Moreover, this phenomenon has not been restricted to public higher education. When tuition began to increase in the public sector, that fact was not lost on private universities; in part because of a desire to maintain prestige and accumulate revenue, private institutions raised their tuition as well.<sup>22</sup> Since many elite private schools turn away huge percentages of their annual applicants,<sup>23</sup> they arguably have “no reason to lower tuition and every reason to continue raising it.”<sup>24</sup>

## II. THE STUDENT LOAN MARKET

As a result, large numbers of students must borrow significant sums in order to fund their higher education goals. To meet this need, student loans generally fall into two broad categories—federal loans and private loans.<sup>25</sup> Prior to 2010, the federal student loan program functioned through private lenders, whereby private banks issued loans to college students, and the underlying debt was guaranteed by the U.S. government.<sup>26</sup> However, in 2010, a cooperative arrangement between the Obama administration and the U.S. Congress changed the applicable rules so that all federal student loans are now made directly by the U.S. Department of Education.<sup>27</sup> Commercial lenders who participate in remaining student loan activity are relegated to the private market, which is only around 8% of the total outstanding student debt.<sup>28</sup>

The sheer volume of both types of student borrowing has caused the entire business cycle of lending, repayment, and debt collection to rapidly

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21. *Id.*

22. *Id.*

23. See *Top 100 – Lowest Acceptance Rates*, U.S. NEWS & WORLD REP., available at <http://colleges.usnews.rankingsandreviews.com/best-colleges/rankings/lowest-acceptance-rate> (last visited Nov. 24, 2014) (ranking the colleges and universities with the lowest acceptance rates).

24. ZIMMERMAN, *supra* note 20.

25. See U.S. DEPARTMENT OF EDUCATION, *Federal Student Aid, Federal Student Loan Programs*, available at <http://studentaid.ed.gov/sites/default/files/federal-loan-programs.pdf> (last visited Nov. 24, 2014).

26. *Id.*; see also Jordan Weissman, *No, the Student Loan Crisis Is Not a Bubble*, ATLANTIC, Sept. 6, 2013, available at <http://www.theatlantic.com/business/archive/2013/09/no-the-student-loan-crisis-is-not-a-bubble/279398/>.

27. *Id.*

28. Or, approximately \$90 billion of the \$1.1 trillion in outstanding student debt. See Allie Bidwell, *Is the Private Student Loan Market As Bad As It Seems?* U.S. NEWS & WORLD REP., Dec. 23, 2013, available at <http://www.usnews.com/news/articles/2013/12/23/is-the-private-student-loan-market-as-bad-as-it-seems> (citing *Private Student Loan Performance Report – 2013, Student Loan Market Data*, MEASUREONE, <http://measureone.com/reports>).

grow into a large-scale financial enterprise. In this regard, it is important to note that the collection process for defaulted student debt can have serious repercussions for borrowers; student loan defaulters enjoy no statute of limitations protections on the underlying debt,<sup>29</sup> and they become subject to special penalties<sup>30</sup> through collectors with unique authorities to seize some borrowers' paychecks, tax refunds, and Social Security benefits without a court order.<sup>31</sup> All of this has caused critics to describe student loan debt collectors as wielding widespread "power that would make a mobster envious."<sup>32</sup>

Tragically, the entire situation is poised to worsen in coming years. This is because the full effects of modern student loan indebtedness are not yet fully realized. Tremendous numbers of students with the largest debt balances have not yet graduated with their degrees and therefore have yet to get their first job or make (or miss) their first student loan payment. These new graduates will have to struggle mightily in order to repay their student debt, and they may not be able to do so at all.

Given this environment, some observers are openly noting similarities between today's student loan climate and the pre-2008 American "housing bubble" that had far-reaching effects across the entire economy. Such a comparison pays particular attention to both systems' arguably lax lending standards, how borrowers and lenders have been specifically incentivized to inject unsustainable amounts of debt into the lending processes, and how the purchased assets (*i.e.*, college degrees and homes) ultimately became economically overvalued.<sup>33</sup> Accordingly, some

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29. See *Lockhart v. United States*, 546 U.S. 142 (2005) (citing 1991 Higher Education Technical Amendments, 20 U.S.C. § 1091a(a)(2)(D), 105 Stat. 123) ("Notwithstanding any other provision of statute . . . no limitation shall terminate the period within which suit may be filed, a judgment may be enforced or an offset, garnishment, or other action initiated or taken . . .").

30. See generally U.S. DEPARTMENT OF EDUCATION, *Student Loans Overview: Fiscal Year 2014 Budget Proposal*, S-32, available at <http://www2.ed.gov/about/overview/budget/budget14/justifications/s-loansoverview.pdf>.

31. See Les Kjos, *Analysis: Student Loan Collections Toughen*, UNITED PRESS INTERNATIONAL, Jan. 6, 2005, available at [http://www.upi.com/Business\\_News/Security-Industry/2005/01/06/Analysis-Student-loan-collections-toughen/UPI-35031105052132/](http://www.upi.com/Business_News/Security-Industry/2005/01/06/Analysis-Student-loan-collections-toughen/UPI-35031105052132/); U.S. DEPARTMENT OF EDUCATION AND FEDERAL STUDENT AID, *supra* note 5.

32. See Peter Zuckerman, *Ending Student Loan Exceptionalism: The Case for Risk-Based Pricing and Dischargeability*, 126 HARV. L. REV. 587, 606 (2012) (citing John Hechinger, *U.S. Gets Tough on Failure to Repay Student Loans*, WALL ST. J., Jan. 6, 2005, available at <http://online.wsj.com/news/articles/SB110497406688418357> (quoting then-Professor (now Senator) Elizabeth Warren)).

33. See, e.g., Dean Baker, *The Housing Crash Recession: How Did We Get Here*, PUB. BROAD. SERV., Mar. 21, 2008, available at <http://www.pbs.org/now/shows/412/housing-recession.html>. When the allegedly lax lending standards resulted in a large-scale failure of borrowers to repay the underlying debt, the entire arrangement suffered. Since that time, the mortgage industry has adopted much more stringent lending practices. *Id.* The comparison between processes for home mortgages and student loans gains a startling amount of traction when one considers the fact that home mortgage loans are secured by real estate collateral which can be

graduates are reasonably contemplating their options, particularly if the prospect of repayment appears less and less feasible for them. Given their amount of student loan debt and their potentially dim employment prospects, many such students, like some pre-2008 mortgage borrowers, undoubtedly feel betrayed by the allure of the “American Dream.” Unfortunately for student borrowers, our society’s primary mechanism for long-term debt relief is simply not a realistic option for them.

### III. BANKRUPTCY AND STUDENT LOANS: THE “UNDUE HARDSHIP” STANDARD

With deep roots in evenhandedness and social justice, bankruptcy occupies a strong tradition in American jurisprudence. The case of *Local Loan Company v. Hunt*, a leading U.S. Supreme Court case from 1934, illustrates the law’s socially-conscious philosophical underpinning: bankruptcy is designed to “relieve the honest debtor from the weight of oppressive indebtedness, and permit him to start afresh . . .” thereby permitting “a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt.”<sup>34</sup> In this way, bankruptcy is about both the debtor and our larger society; by giving a debtor a second chance at a financial future, he or she is rehabilitated to a productive place, instead of being forced to perpetually labor under a crushing amount of debt.

As a procedural matter, American bankruptcy proceedings are initiated in a federal court, per the specific requirements of the U.S. Constitution.<sup>35</sup> Federal statutory law regarding bankruptcy petitioners’

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forfeited and sold in the event of non-payment, but student loans are not. Through such a lens, an outside observer might reasonably question why student borrowers do not have to meet even stronger creditworthiness standards than their mortgage-seeking counterparts; *see also, e.g.*, Michael B. Fishbein, *9 Striking Similarities Between the Housing Bubble and the Higher Education Bubble*, HUFFINGTON POST, Mar. 31, 2014, available at [http://www.huffingtonpost.com/michael-b-fishbein/9-striking-similarities-b\\_b\\_5062840.html](http://www.huffingtonpost.com/michael-b-fishbein/9-striking-similarities-b_b_5062840.html). Today, and especially since the recession of 2008, when a borrower seeks a home mortgage from a lending institution, he or she must satisfy a lender’s extensive list of personal financial questions focused upon the borrower’s projected ability to repay the debt in the future; *see also, e.g.*, UNIFORM RESIDENTIAL LOAN APPLICATION, Freddie Mac Form 65/Fannie Mae Form 1003, available at [https://www.fannie.mae.com/content/guide\\_form/1003rev.pdf](https://www.fannie.mae.com/content/guide_form/1003rev.pdf) (last visited Nov. 24, 2014). One of the popularly-advanced arguments to partially explain the recession of 2008 is found in the housing market’s willingness to extend credit to less-creditworthy borrowers, and in the way in which those loans were subsequently packaged and resold by successive purchasers of the original loans.

34. *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934) (citing *Williams v. U.S. Fidelity & Guaranty Co.*, 236 U.S. 549, 554–55 (1949), *Stellwagen v. Clum*, 245 U.S. 605, 617 (1918), and *Hanover Nat’l Bank v. Moyses*, 186 U.S. 181, 186 (1902)).

35. U.S. CONST., art. I, § 8, cl. 4.

cases is found within Title 11 of the U.S. Code,<sup>36</sup> requiring commencement of bankruptcy cases to be filed through the U.S. Bankruptcy Court, under affiliation with the local U.S. federal court system.<sup>37</sup> When an individual (*i.e.*, non-corporate) petitioner seeks bankruptcy protection, the outcome is most commonly governed by either Chapter 7<sup>38</sup> or Chapter 13<sup>39</sup> of Title 11 of the Federal Bankruptcy Code, depending on whether the petitioner seeks liquidation/discharge of debts or debt reorganization.

When one reads *Hunt's* plain language, one might easily imagine the situation of a new, deeply-indebted college graduate. However, Title 11 carves out a specific exception, intentionally setting an extremely high bar for the discharge of student loans.<sup>40</sup> In that regard, the statutory language of 11 U.S.C. § 523(a)(8) is explicit: “unless excepting such debt from discharge . . . would impose an *undue hardship* on the debtor and the debtor’s dependents,” a bankruptcy discharge will not relieve a debtor from any debt that originates from “an educational . . . loan made, insured, or guaranteed by a governmental unit” or “any other educational loan that is a qualified educational loan.”<sup>41</sup>

Such unsympathetic treatment for student borrowers has not always been the case. Student loans were fully dischargeable in American bankruptcy until 1976, when Congress only prohibited bankruptcy discharge during the first five years of repayment.<sup>42</sup> In the years that followed, various laws and regulations consistently and increasingly isolated student loans from bankruptcy protections, amid alleged fears that “former students would opportunistically seek discharge and impair the solvency of the student lending program.”<sup>43</sup> These concerns partially culminated with the Higher Education Amendments of 1998, which struck the previous requirement that permitted federal education loans to be discharged after seven years in repayment.<sup>44</sup>

Oddly, these 1998 Amendments passed Congressional muster despite

36. See 11 U.S.C. §§ 101–1532 (2013).

37. See FEDERAL RULES OF BANKRUPTCY PROCEDURE R. 1002, *Commencement of Case*.

38. 11 U.S.C. §§ 701–84 (2013). Chapter Seven is generally the most expeditious for individual petitioners and involves liquidation of assets by a bankruptcy trustee and a subsequent discharge of non-exempt debts.

39. 11 U.S.C. §§ 1301–30 (2013). Chapter 13 focuses upon the legal process and oversight of a petitioner’s debt reorganization, versus liquidation.

40. 11 U.S.C. § 523(a)(8) (2013).

41. *Id.* § 523(a)(8)(A)(i),(a)(8)(B) (emphasis added).

42. Education Amendments of 1976, Pub. L. No. 94-482, § 127(a), 90 Stat. 2081, 2141 (1976).

43. Zuckerman, *supra* note 32, at 595.

44. See Higher Education Amendments of 1998, Pub. L. No. 105-244, § 971(a), 112 Stat. 1581, 1837 (1998).

the fact that in 1997, the National Bankruptcy Review Commission<sup>45</sup> had specifically recommended the complete repeal of the student loan exception.<sup>46</sup> In making that recommendation, the Commission found no indication that the bankruptcy process had been misused during times when bankruptcy was available for student loans, and that the “undue hardship” standard was applied too restrictively in real-world practice.<sup>47</sup> The commission openly questioned the appropriateness of a system in which a borrower with debt stemming from consumer debt incurred to buy a “car, a vacation, or a pizza” can take full advantage of bankruptcy protections, but a student borrower cannot.<sup>48</sup>

Finally, in 2005, the nondischargeability status was extended to the private loan market.<sup>49</sup> Since then, the sole avenue by which a bankruptcy petitioner can seek the application of bankruptcy protection to any student loan debt is to initiate a separate adversarial proceeding within the bankruptcy case, through which he or she has the burden of affirmatively proving that paying the student loan constitutes an “undue hardship.”<sup>50</sup> To complicate matters even further, Congress neglected to define the term “undue hardship,” even though the words appear explicitly in the law. In order to give some level of predictability to this language, most modern bankruptcy courts have chosen to apply a legal and factual test known as the “*Brunner standard*,” named after the Second Circuit Court of Appeals’ decision in *Brunner v. New York State Higher Education Services Corporation*.<sup>51</sup> In *Brunner*, the Court held that in order for a debtor to successfully obtain a discharge of student debt based upon “undue hardship,” that debtor must affirmatively demonstrate three separate criteria: (1) the debtor cannot maintain, based on current income and expenses, a minimal standard of living; (2) that additional

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45. The National Bankruptcy Review Commission was established pursuant to the Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, 108 Stat. 4106. The commission was created to investigate and study issues relating to the Bankruptcy Code, solicit divergent views of parties concerned with the operation of the bankruptcy system, evaluate the advisability of proposals with respect to such issues, and prepare a report to be submitted to the President, Congress and the Chief Justice not later than two years after the date of the first meeting. *NBRC Fact Sheet*, NATIONAL BANKRUPTCY REVIEW COMMISSION (Aug. 12, 1997), <http://govinfo.library.unt.edu/nbrcfacts.html> [hereinafter NATIONAL BANKRUPTCY COMMISSION REVIEW FACT SHEET].

46. See *Recommendations to Congress*, NATIONAL BANKRUPTCY REVIEW COMMISSION (Oct. 20, 1997), <http://govinfo.library.unt.edu/nbrcreport/03recomm01title.html>.

47. See *Discharge, Exceptions to Discharge, and Objections to Discharge*, NATIONAL BANKRUPTCY REVIEW COMMISSION (Oct. 20, 1997), <http://govinfo.library.unt.edu/nbrcreport/07consum.html>.

48. *Id.*

49. See Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 220, 119 Stat. 23, 59 (2005).

50. 11 U.S.C. § 523(a)(8) (2013).

51. *Brunner v. N.Y. State Higher Educ. Services Corp.*, 831 F.2d 395, 396 (2d Cir. 1987).

circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the loans; and (3) that the debtor has made good faith efforts to repay the loans.<sup>52</sup> The *Brunner* Court reasoned that Congress's usage of the term "undue" indicated that more than a routine level of hardship was required,<sup>53</sup> resulting in the above inquiry into whether the debtor's purported inability to repay the debt would extend into the future—a question that is very different from a much simpler inquiry into the debtor's present ability to pay an underlying debt. As a result, the process governing student loans stands in stark contrast to other debts discharged in bankruptcy, where unless there is "litigation involving objections to [a] discharge," a discharge will be quickly forthcoming.<sup>54</sup>

The proliferation of *Brunner's* applicability to other federal bankruptcy courts' decisions has caused significant and widespread difficulty for petitioners seeking to discharge student loan debt. In practice, the application of the *Brunner* test to student loan debtors' bankruptcy cases has resulted in a procedural climate where the "undue hardship" standard is one which very few petitioners can successfully meet. An analysis of bankruptcy cases bears this out; for example, a petitioner's likelihood of prevailing in a student loan discharge case is generally considered "slim and worse than in typical civil litigation, with student loan holders and their agents aggressively fighting discharge cases and much less likely to settle a case out of court."<sup>55</sup> Additionally, most bankruptcy petitioners will have to fund the services of an attorney to litigate an adversary proceeding under the "undue hardship" standard—a particularly aggravating fact, given that *pro se* bankruptcy petitioners' cases are much more likely to be dismissed outright than are those who are represented by an attorney.<sup>56</sup> To that end, it is worth noting that before the recent recession (2007), about 29% of consumers filing

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52. *Id.* at 397.

53. *Id.*

54. 11 U.S.C.A. § 727 (2014) ("The court *shall* grant the debtor a discharge, unless . . .") (emphasis added). See also U.S. Courts & *Discharge in Bankruptcy: How Does the Debtor Get a Discharge?*, U.S. COURTS ("Unless there is litigation involving objections to the discharge, the debtor will usually automatically receive a discharge . . .") (Apr. 13, 2014), <http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/DischargeInBankruptcy.aspx>.

55. Specifically, just 36% of debtors' cases in a recent student loan bankruptcy study were settled out of court, whereas about 97% of all cases in state and federal courts reached an out-of-court settlement. See generally *The Truth About Student Loans and the Undue Hardship Discharge*, NATIONAL CONSUMER LAW CENTER <http://www.studentloanborrowerassistance.org/wp-content/uploads/2007/03/iulianoresponse.pdf> (last visited Nov. 24, 2014).

56. *Id.* (citing Katherine Porter, *The Do-It Yourself Mirage: Complexity in the Bankruptcy System*, in *BROKE: HOW DEBT BANKRUPTS THE MIDDLE CLASS*, 157 (2012)).

for bankruptcy held student loans, which totaled about \$4.8 billion.<sup>57</sup> Today, a conservative estimate of total student debt not discharged in bankruptcy proceedings is estimated to be about double that, or even higher.<sup>58</sup> Overall, the population that even attempts to pursue a discharge of student loans under the “undue hardship” standard is estimated to be between a mere 0.1% and 0.3% of bankruptcy petitioners.<sup>59</sup>

#### IV. A CHANGE IN THE LAW: EXPANDING STUDENT LOAN DISCHARGEABILITY THROUGH AN AMENDMENT TO 11 U.S.C. § 523(A)(8)

Extension of bankruptcy protections to student loan debt could take several forms. Noting the disparities between federal and private loan mechanisms, various lawmakers have proposed legislation such as the “Fairness for Struggling Students Act,”<sup>60</sup> which would restore federal bankruptcy law to its pre-2005 status, when privately-issued student loans were still eligible for discharge. Although these legislative attempts have been unsuccessful, there are excellent policy rationales for such action; after all, the obvious differences between federal and private loans prompts a logical question as to why the two types of loans should ever have been treated on equal footing in the first place. Federally-issued student loans have fixed interest rates, income-based repayment options, and multiple avenues for payment forgiveness or deferment, whereas private loans have interest rates that can vary widely, with very few deferment options and extremely unlikely prospects of debt forgiveness.<sup>61</sup> Of course, a repeal of § 523(a)(8)’s applicability to only private loans would certainly be opposed strongly by the private loan-issuing community.

Another alternative is the repeal of § 523(a)(8), returning student loans’ treatment in the federal bankruptcy structure to its pre-1976 footing. This would be a dramatic policy change, but it deserves serious consideration as a mechanism to offer a viable future to the most desperate class of student loan borrowers and as a powerful injection into America’s economic engine. In accordance with the National Bankruptcy

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57. See Zuckerman, *supra* note 32, at 604.

58. *Id.* at 605.

59. *Id.* at 609.

60. See S.114, 113TH CONGRESS (2013–2014): *A Bill to Amend Title 11, United States Code, with Respect to Certain Exceptions to Discharge in Bankruptcy*, <http://beta.congress.gov/bill/113th-congress/senate-bill/114/text> (last visited Nov. 24, 2014).

61. See generally “What are the Differences Between Federal and Private Student Loans?,” FEDERAL STUDENT AID <http://studentaid.ed.gov/types/loans/federal-vs-private>, (last visited Nov. 24, 2014).

Review Commission's recommendation in 1997,<sup>62</sup> such a step would not necessarily result in a radical and widespread purposeful avoidance of student debt across American society. Instead, returning the law to 1970s' levels would merely allow student loans to be treated the same as other personal debts.

## V. ALL STUDENT BORROWERS ARE NOT THE SAME

During the acceleration of student loan balances in recent years, one particular aspect of the cause has been largely overlooked from a policy perspective: student loans are made without regard to the borrower's future creditworthiness.<sup>63</sup> Advocates of this policy argue that a creditworthiness-blind system permits access to higher education for those members of society who need it the most, especially when young borrowers have little or no personal credit history.

However, given the current magnitude of the student debt problem in America, this policy begs an obvious question: should individual student borrowers be evaluated on some basis of their *future* ability to pay? After all, *Brunner* requires bankruptcy judges to evaluate a petitioner's future ability to pay before making a bankruptcy discharge decision under the "undue hardship" standard. Despite that, future creditworthiness is ignored when a student loan is made at the outset. At best, such a system is inconsistent. At worst, it is outright deceptive. By relying upon a lending scheme that ignores differences in borrowers' future debt repayment abilities, our current student loan system undoubtedly leads many individual borrowers to take on far too much debt when compared to the amount of real financial value on return.

At first blush, it may seem harsh to treat one student's creditworthiness and future earnings differently from another student's. However, the facts are clear; student borrowers with certain degrees and academic majors will have an exceedingly difficult time repaying high-balance loans. It is a simple reality that some college graduates earn much more than others soon after graduation,<sup>64</sup> while some graduates struggle to find any employment at all.<sup>65</sup> In fact, the difference in earning power

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62. See National Bankruptcy Review Commission Fact Sheet, *supra* note 45.

63. For a discussion of the value of considering future creditworthiness as a precondition for higher education loans, see, e.g., Hardeep Walia, *The Unspoken Cause of the Student Loan Crisis*, FORBES, Sept. 26, 2013, <http://www.forbes.com/sites/hardeepwalia/2013/09/26/the-unspoken-cause-of-the-student-loan-crisis/>.

64. See Anthony P. Carnevale et al., *Hard Times, College Majors, Unemployment, and Earnings: Not All College Degrees are Created Equal*, GEORGETOWN UNIVERSITY CENTER ON EDUCATION AND THE WORKFORCE 4–6 (2012), <https://georgetown.app.box.com/s/og6p8y9x1yeacejk1ci0>.

65. See *id.*

between one undergraduate major and another can be more than 300%.<sup>66</sup> This fact was not lost on President Obama when he jokingly questioned the amount of future earning power a student might receive from an art history degree.<sup>67</sup> Even though his comment was quickly criticized and he subsequently apologized,<sup>68</sup> the President's observation reflected a good amount of current reality. As a financial matter, it should be no surprise to any student that a choice of college major can be just as important as the decision of whether to attend college at all. It simply follows that lending decisions for the pursuit of higher education should, at some level, be made with a candid financial assessment in mind.

Obviously, money is not everything. Our entire society benefits tremendously from valuable contributions made by lower-earning graduates. For many in the higher education community, it is a well-accepted proposition that there is more to picking a college or a major than the salary to be earned after graduation; job satisfaction and the ability to make meaningful contributions to society are tremendously important, too. Individual borrowers and the entire lending industry, however, should both remember that an important corollary is also true: there is much more to debt repayment than the borrower's mere possession of an academic degree. If a student wants to pursue a program of study that has a relatively low future-earning potential, that student is well-advised to conduct a realistic evaluation of his/her personal situation and plan his/her academic future accordingly.

It is here that a change to § 523(a)(8) can play its most important role. If lenders, whether private lenders or the federal government, begin to realize that some students might be unable to sustain future repayment and perhaps obtain a lawful discharge through bankruptcy, those lenders will become more prudent in their lending habits. For example, lenders might decide to increase interest rates in order to account for additional risk inherent in some underlying loans. In any event, if students are unable to secure high amounts of student loans at a low interest rate in order to pay high tuition amounts to universities, those students will have to decide whether to opt in favor of lower-cost educational options, or to pursue an educational goal which a lending agency will fund on acceptable terms. In either event, the end result would put welcome

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66. See Press Release, Georgetown University Center on Education and the Workforce, *New Report on the Economic Value of 171 College Majors Links College Majors to Earnings* (May 24, 2011), <https://georgetown.app.box.com/s/omooxnult5yvuctf0ftl>.

67. *Is College Worth It?*, *ECONOMIST*, Apr. 5, 2014, <http://www.economist.com/news/united-states/21600131-too-many-degrees-are-waste-money-return-higher-education-would-be-much-better> (last visited Nov. 24, 2014).

68. See Juliet Eilperin, *Obama Apologizes to Art Historian for Public Quip*, *WASH. POST*, Feb. 18, 2014, <http://www.washingtonpost.com/blogs/post-politics/wp/2014/02/18/obama-apologizes-to-art-historian-for-public-quip/> (last visited Nov. 24, 2014).

pressure on universities in favor of reduced student costs.

Implementation of a system that evaluates individuals' future creditworthiness will necessitate administrative mechanisms for equitably risk-assessing students' academic performance and income prospects throughout the life of the loan. As daunting as that may sound, it is certainly possible to accomplish and, it may be the best way to ensure the longevity of our student loan industry. After all, the modern lending industry already utilizes such a process when it requires prospective borrowers to make their case for a small business loan<sup>69</sup> or for the purchase of a home.<sup>70</sup> Given the dollar amounts at stake for individual higher education students today, it is not at all unreasonable to require student borrowers to prove—with clarity—how their future educational plans and academic performance will likely translate into solid employment and debt repayment.

## VI. CONCLUSION

When student loans become essentially zero-risk for the lender because they are exempt from bankruptcy discharge and subject to “mobster”-style recoupment tactics,<sup>71</sup> lenders are incentivized to make loans with relatively few restrictions. When one adds this arrangement to a system where loans are extended to students irrespective of their future ability to pay, economic disincentives for borrowers begin to disappear in a similar fashion. These two phenomena can then feed into an ideal environment for institutions of higher learning to increase tuition costs dramatically—especially when public funding is being redirected elsewhere because of more pressing social needs. The ensuing spiral is a predictable one, where rising tuition costs are fed by an increasing supply of personal student debt.

Yet, even this economic spiral has limits, and our society may be reaching that point now. The result will likely leave legions of college graduates in the jaws of a dual threat: without the economic means to repay their loans and similarly without the legal mechanisms to avoid repaying them. Because students cannot realistically seek the protection of personal bankruptcy, these borrowers' personal economic situation will likely continue to deteriorate, with predictable consequences for an already-anemic job market and an American economy that continues to

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69. For a detailed explanation of the value of requiring students to create and modify a business plan for their higher education goals, see Brett Nelson, *How to Deal with the \$1 Trillion Student Loan Crisis*, FORBES, Jan. 20, 2014, <http://www.forbes.com/sites/brettnelson/2014/01/20/how-to-deal-with-the-1-trillion-student-loan-crisis/>.

70. See, e.g., UNIFORM RESIDENTIAL LOAN APPLICATION, *supra* note 33.

71. See Hechinger, *supra* note 32.

sputter. Additionally, the simultaneous growth of aggregate loan balances and accompanying default rates places the entire current student loan system in jeopardy for future generations of borrowers.

Simply put, the student loan status quo is unacceptable, if access to the higher education portion of the “American Dream” is to remain viable. To that end, breaking the destructive cycle of mounting higher education-related debt will require clarifying, understanding, and leveraging the involved economic incentives. Repealing § 523(a)(8) is the perfect place to start.

