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## Consent to Student Loan Bankruptcy Discharge

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## Consent to Student Loan Bankruptcy Discharge

JOHN PATRICK HUNT\*

*As the Department of Education reconsiders its rules governing consent to discharge of federal student loans in bankruptcy, this Article argues for the first time that the Department should approach the problem specifically as an operator of programs to promote education and benefit students, rather than as an entity interested only in debt collection. This Article shows that the Department's rules to date have treated whether to consent to discharge primarily as a pecuniary issue, without regard to the educational goals of the student loan programs. For example, the Department apparently has never considered whether making it difficult to discharge student loans interferes with borrowers' freedom of career choice or deters students from pursuing higher education in the first place.*

*Discharge should be more predictable for borrowers. The Department's regulations have given ever more nontransparent discretion to student loan holders to decide whether to oppose discharge. This Article joins the scholarly call for the Department to remedy this situation by adopting objectively defined criteria for loan holders' consent to discharge. Creating such "safe harbors" for borrowers would eliminate the uncertainty and formidable procedural barriers that attend seeking relief through an adversarial process in bankruptcy court. These barriers may deter as many as 69,000 eligible borrowers a year from seeking to discharge their student loans in bankruptcy.*

*This Article argues that furthering the educational purposes of the student loan programs calls for the Department to consent to discharge more freely. Currently, the only substantive ground for consent is the presence of "undue hardship," as that term from the Bankruptcy Code has been interpreted by courts. But judicial tests for undue hardship do not take account of discharge-favoring purposes of the student loan programs. To fulfill its mandate, the Department should consent to discharge in cases where failure to do so would thwart the purposes of the student loan programs, even if undue hardship is absent.*

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## INTRODUCTION

“I spoke to two lawyers and they both said the same thing: ‘It’s going to be extremely expensive and you are going to lose . . . .’” That is how Chuck Stewart described to a journalist his investigation of bankruptcy relief for \$60,000 in student loans.<sup>1</sup> The persistent Stewart reportedly was able to eliminate 90% of his debt through bankruptcy.<sup>2</sup> But Chuck Stewarts are decidedly the exception: it is estimated that only 0.187% of the 238,000 student loan debtors who filed bankruptcy in 2007 even tried to discharge their loans.<sup>3</sup> This is true even though the lawyers Stewart consulted may only have been half right: in fact, student loan debtors who do seek discharge enjoy a robust rate of success.<sup>4</sup>

Why, given good odds, do so few student loan borrowers try for bankruptcy relief? Probably because the student loan debtor who seeks a discharge must bring an “adversary proceeding”<sup>5</sup>—essentially a lawsuit within the bankruptcy<sup>6</sup>—against the creditor and must show in that proceeding that repayment would entail “undue hardship.”<sup>7</sup> The adversary proceeding is expensive and unpleasant,<sup>8</sup> and courts’ decisions about undue hardship are unpredictable.<sup>9</sup> As Professor Rafael Pardo has

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1. Araz Hachadourian, *Think Students Can’t Declare Bankruptcy? Think Again*, YES! (Sept. 23, 2015), <https://www.yesmagazine.org/new-economy/think-students-cant-declare-bankruptcy-think-again-20150923> [<https://perma.cc/H96T-GCGH>].

2. *Id.*

3. See Jason Iuliano, *Student Loans and Surmountable Access-to-Justice Barriers*, 68 FLA. L. REV. 377, 381–82 (2016); *infra* notes 118–119 and accompanying text; see also Katy Stech Ferek, *Judges Wouldn’t Consider Forgiving Crippling Student Loans—Until Now*, WALL ST. J. (June 14, 2018, 7:00 AM), <https://www.wsj.com/articles/judges-wouldnt-consider-forgiving-crippling-student-loans-until-now-1528974001> [<https://perma.cc/8CQH-DSKZ>] (reporting that only 473 people sought bankruptcy relief for student loans in 2017).

4. Estimates in published academic papers of rates of success, using different definitions of the term, range from 39% to 57%. See *infra* note 120.

5. See FED. R. BANKR. P. 7001(6) (“The following are adversary proceedings: . . . (6) a proceeding to determine the dischargeability of a debt.”).

6. See 6A BANKRUPTCY SERVICE LAWYERS’ EDITION § 57:11 (2018) (“[A]n ‘adversary proceeding’ is essentially indistinguishable from a civil action . . .”).

7. See 11 U.S.C. § 523(a)(8) (2018) (excepting student-loan debts from bankruptcy discharge unless denial of discharge “would impose an undue hardship on the debtor and the debtor’s dependents”).

8. See Rafael I. Pardo, *The Undue Hardship Thicket: On Access to Justice, Procedural Noncompliance, and Pollutive Litigation in Bankruptcy*, 66 FLA. L. REV. 2101, 2112 (2014) [hereinafter Pardo, *The Undue Hardship Thicket*] (“[T]he consumer bankruptcy bar has emphasized that many debtors do not have the financial wherewithal to litigate an undue hardship adversary proceeding.”); see also Tim Chen, *Student Loans Have Become Our Modern-Day Debtors Prisons*, USA TODAY (June 5, 2018, 5:00 AM), <https://www.usatoday.com/story/opinion/2018/06/05/student-loans-crisis-allow-bankruptcy-investigate-abuses-column/640460002/> [<https://perma.cc/L9LW-4Z2F>] (“People don’t even try (to get a student loan discharge) because one, they can’t afford the litigation, but two, they’re just fearful of having to face that process.”) (quoting John Rao, National Consumer Law Center).

9. Rafael I. Pardo & Michelle R. Lacey, *Undue Hardship in the Bankruptcy Courts: An Empirical Assessment of the Discharge of Educational Debt*, 74 U. CIN. L. REV. 405, 480–81

argued, together these conditions deter borrowers from seeking relief even if repayment in fact subjects them to undue hardship, creating barriers to access to justice.<sup>10</sup>

The Department of Education (“Department”) can help such borrowers because the large majority of student loans outstanding have been made under federal programs that the Department administers.<sup>11</sup> The Department has issued rules governing when holders of loans made under these programs should consent to discharge.<sup>12</sup> When the holder consents to discharge, it saves the debtor the expense and uncertainty of further litigating an adversary proceeding.<sup>13</sup> The Department’s discharge rules, then, could help the many debtors who should apply for discharge but do not—as many as 69,000 per year, according to one estimate.<sup>14</sup> The Department is currently reconsidering these rules,<sup>15</sup> and this Article advocates that the Department honor Congress’s intent in creating student loan programs by creating more predictable, objective, and generous criteria for consent to discharge.

Despite their importance, the Department’s bankruptcy discharge rules have received little scholarly attention. The work of Professors Matthew Bruckner, Pamela Foohey, Brook Gotberg, Dalié Jiménez, and Chrystin Ondersma (the “BFGJO group”) is an important exception. These authors have published a shorter piece containing the comments they submitted to the Department about its discharge consent rules,<sup>16</sup> and over forty professors have endorsed those comments.<sup>17</sup> Professors Bruckner, Gotberg, Jiménez, and Ondersma have since published a more detailed explanation and defense of their proposal.<sup>18</sup> This Article is the only one to

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(2005) [hereinafter Pardo & Lacey, *Undue Hardship in the Bankruptcy Courts*].

10. See Pardo, *The Undue Hardship Thicket*, *supra* note 8, at 2101.

11. See *Trends in Higher Education*, COLLEGE BOARD, Fig. 6 (2019), <https://trends.collegeboard.org/student-aid/figures-tables/total-federal-and-nonfederal-loans-over-time> [<https://perma.cc/L6C9-KSEB>] (reporting that the percentage of student loans originated under federal programs in the period 1998–2019 has varied from 75% to 93%).

12. As discussed in more detail in Part I, the Department maintains different sets of rules for the different programs it administers. See, e.g., 34 C.F.R. § 674.49(c) (2019) (Perkins program); *id.* § 682.402(i)(1) (Federal Family Education Loan Program).

13. See, e.g., *In re McDowell*, 549 B.R. 744, 749 (Bankr. D. Idaho 2016) (indicating that debtor no longer had to litigate adversary proceeding against Department after its consent to discharge); *In re Conway*, 489 B.R. 828, 830 n.2 (Bankr. E.D. Mo. 2013) (indicating that two creditors consented to discharge and therefore dropped out of adversary proceeding).

14. See Ron Lieber, *Last Plea on School Loans: Proving a Hopeless Future*, N.Y. TIMES, (Aug. 31, 2012), <https://www.nytimes.com/2012/09/01/business/shedding-student-loans-in-bankruptcy-is-an-uphill-battle.html> [<https://perma.cc/3H69-K6NW>].

15. See Request for Information on Evaluating Undue Hardship Claims in Adversary Actions Seeking Student Loan Discharge in Bankruptcy Proceedings, 83 Fed. Reg. 7460, 7461 (Feb. 21, 2018).

16. See Dalié Jiménez, Matthew Bruckner, Pamela Foohey, Brook Gotberg & Chrystin Ondersma, *Comments of Bankruptcy Scholars on Evaluating Undue Hardship Claims in Bankruptcy*, 21 J. CONSUMER & COM. L. 114, 114–24 (2018).

17. *Id.* at 114.

18. See Matthew Bruckner, Brook Gotberg, Dalié Jiménez & Chrystin Ondersma, *A No-Contest Discharge for Uncollectable Student Loans*, 91 U. COLO. L. REV. 114 (2020).

date to consider that policy in a context broader than that of the specific proposal advanced by the BFGJO group.

This Article is also unique in grounding its recommendations for liberalizing discharge in the purposes of the student loan programs and in advocating for consent to discharge even where undue hardship is absent. By situating the Department's discharge policy within the context of student loan law, rather than just bankruptcy law, and exploring what the Department can and should do in that framework, this Article offers the fullest account to date of the administrative law of student loan bankruptcy.

This Article starts by giving a brief background on student loan nondischargeability<sup>19</sup> and on the three major federal student loan programs.<sup>20</sup> It then reviews the Department's latest statement on consent to bankruptcy discharge of federal loans.<sup>21</sup> This is a Dear Colleague letter dated July 7, 2015,<sup>22</sup> which requires loan holders to oppose discharge unless doing so would not be cost-effective or the holder decides that repayment would cause the borrower "undue hardship."<sup>23</sup> This Article then presents a brief history of the Department rules reflected in the letter.<sup>24</sup>

This Article makes two sets of recommendations. The first set relates to "trans-substantive" issues,<sup>25</sup> that is, issues other than how readily or stingily the Department consents to discharge.

The first recommendation in this set is that the Department, which has never given a complete explanation of its regulations,<sup>26</sup> explain and defend its bankruptcy discharge policy more thoroughly than it has done so far. Student loan bankruptcy is important enough to command more of the Department's attention than it has to date.<sup>27</sup>

Second, the Department should consider notice-and-comment rulemaking to fix gaps, ambiguities, and nonuniformity in the existing regulations.<sup>28</sup> In so doing, it should weigh the risk of legal attack on the guidance it has issued against the administrative burden of notice-and-comment rulemaking. The Department definitely should amend one particular regulation, a restrictive rule governing the Perkins program that obstructs liberalizing discharge policy.

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19. *See infra* Section I.A.

20. *See infra* Section I.B.

21. *See infra* Section I.C.

22. Letter from Lynn Mahaffie, Deputy Assistant Sec'y for Policy, Planning, and Innovation, Office of Postsecondary Educ., Dep't of Educ. to "Dear Colleague" 1 (July 7, 2015), <https://ifap.ed.gov/sites/default/files/attachments/dpclletters/GEN1513.pdf> [<https://perma.cc/R7D6-2BWY>] [hereinafter 2015 Dear Colleague Letter].

23. *See infra* Section I.C.

24. *See infra* Section I.D.

25. The author uses "trans-substantive" to mean that the Department should consider them no matter what it decides about the main substantive aspect of the regulations: how readily to consent to bankruptcy discharge.

26. *See infra* Section II.A.1.

27. *See infra* Section II.A.2.

28. *See infra* Section II.B.

Third, the Department should reverse the historical trend in the regulations toward giving loan holders more and more subjective, nontransparent discretion.<sup>29</sup> It should relieve the uncertainty and procedural barriers facing student loan debtors by announcing specific sets of circumstances under which it will not oppose discharge. That is, the Department should create “safe harbors” for borrowers. This suggestion, advanced by the BFGJO group,<sup>30</sup> addresses the access-to-justice barriers Pardo has identified.

The second set of recommendations is “substantive” in that the recommendations relate to how freely the Department should consent to discharge. This Article contends that the Department should rethink its stance on consent to bankruptcy discharge in light of the overall purposes of the student loan programs, most of which it has not considered to date.<sup>31</sup> Specifically, the Department should consent to discharge more readily in order to further other student loan program goals, which include promoting equal access to education, creating a more educated population, safeguarding freedom of career choice, and benefiting borrowers generally.<sup>32</sup> For example, nondischargeability may deter less privileged students from pursuing higher education or from embarking on lower-paying but valuable careers, thus interfering with equal access and freedom of career choice. Nondischargeable loans can and do harm borrowers, thwarting the programs’ purpose of helping students.<sup>33</sup>

This Article explains that the Department has ample authority to take a more generous position. The Department could add new grounds, beyond cost-ineffectiveness and undue hardship, for consenting to discharge. The Department has broad authority to issue regulations governing the student loan programs and, moreover, is specifically authorized to waive government claims.<sup>34</sup> Nothing in the Higher Education Act or Bankruptcy Code requires the Department to elevate debt collection over the achievement of other statutory goals or to consent to discharge only when undue hardship is present.<sup>35</sup> Other agencies, including the Internal Revenue Service and the Department of Justice, have adopted grounds for debt

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29. See *infra* Section II.C.

30. The BFGJO group presents and defends a specific set of recommendations for what the safe harbors should be. See Jiménez et al., *supra* note 16, at 115. As discussed below, see *infra* Section II.C.2, this author supports their proposal, although this Article is more general in orientation.

31. See *infra* Sections III.A–III.B.

32. See *infra* Section III.B.1. This Article thus recommends a way of addressing the policy tension Professor Abbye Atkinson has identified between encouraging borrowing on the one hand and making bankruptcy discharge difficult on the other. See Abbye Atkinson, *Race, Educational Loans & Bankruptcy*, 16 MICH. J. RACE & L. 1, 22 (2010). Professor Jonathan Glater has made a similar point with regard to debt-financed education generally. See Jonathan D. Glater, *Student Debt and Higher Education Risk*, 103 CALIF. L. REV. 1561, 1563 (2015) (arguing that funding education through loans shifts the risk that education will not be financially successful to students, which “may be counterproductive” to larger goals of federal support of higher education).

33. For a fuller discussion of these points, see John Patrick Hunt, *Tempering Bankruptcy Nondischargeability to Promote the Purposes of Student-Loan Programs*, 72 SMU L. REV. 725, 742–62 (2019).

34. See *infra* Section III.C.1.

35. See *infra* Section III.C.2.

forgiveness or compromise apparently without citing express statutory authorization for the specific grounds they adopted.<sup>36</sup>

With an exception for the small Perkins program, the Department could adopt such rules through issuing guidance, without the delay notice-and-comment rulemaking entails.<sup>37</sup> Notice-and-comment rulemaking does offer borrowers more predictable rules, however.<sup>38</sup> The Department should consider acting through guidance first and then following up with rules issued after notice and comment.<sup>39</sup>

Thus, the Department should engage in a deliberate process leading to the adoption of safe harbors for borrowers, as the BFGJO group has suggested. In crafting its rules, the Department should not focus narrowly on collection, but should be guided by all the purposes of the student loan programs, many of which would be advanced by a more generous discharge consent standard. Nor should the Department see itself as authorized to consent only where courts applying the Bankruptcy Code would find undue hardship. By adopting more objective and generous discharge consent rules, the Department can cast off crabbed and incorrect views of when discharge is warranted, honor Congressional intent, and relieve the suffering of thousands of student loan borrowers.

This Article proceeds as follows. Part I provides background on student loan bankruptcy, the student loan programs, the Department's current rules on consent to bankruptcy discharge, and the history of those rules. Part II makes the three recommendations described above that do not relate to how readily the Department consents to discharge. Part III argues that the Department should look to the overall purpose of the student loan programs and consider expanding the circumstances under which it will consent to discharge, and that it has authority to do so.

#### I. THE EDUCATION DEPARTMENT'S BANKRUPTCY DISCHARGE RULES

This Part surveys the content and history of the Department's rules<sup>40</sup> on consent to discharge in borrower bankruptcy. Section I.A provides background on the nondischargeability of student loans in bankruptcy. Section I.B supplies an overview of the major federal student loan programs. Section I.C reviews the Department's 2015 Dear Colleague Letter, which sets forth the Department's current policy on consent to bankruptcy discharge. Section I.D gives a brief summary of the history of the Department's student loan bankruptcy discharge consent rules.

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36. See *infra* Section III.C.3.

37. See *infra* Section III.C.4.

38. In particular, rules that are contained only in guidance documents such as the 2015 Dear Colleague Letter can be changed without going through notice-and-comment rulemaking. See *infra* Section III.C.4.

39. See *infra* Section III.C.5.

40. This Article refers to the Department's discharge consent regulations, its interpretations of those provisions in the 2015 Dear Colleague Letter, and its statements in the letter about how it handles consent to discharge under the Ford program collectively as "rules," recognizing that the Dear Colleague Letter may not set forth "rules" under the Administrative Procedure Act. For discussion of the status of the 2015 Dear Colleague Letter under the Administrative Procedure Act, see *infra* Section III.C.4.



*A. Student Loan Bankruptcy Nondischargeability*

U.S. law provides that a debtor can get a “discharge” of debt by going through a bankruptcy proceeding.<sup>41</sup> After an unsecured loan such as a federal student loan is discharged, a creditor generally may not attempt to collect it.<sup>42</sup> The most common type of bankruptcy is a Chapter 7 proceeding,<sup>43</sup> in which the debtor’s property (except for certain property specified as exempt) is liquidated and the proceeds paid to creditors, after which unpaid debts are discharged.<sup>44</sup> Not all loans are dischargeable in bankruptcy, however. For example, a debtor cannot discharge obligations to pay child support,<sup>45</sup> debts arising from the debtor’s willful and malicious infliction of injury,<sup>46</sup> or most fraudulently incurred debts.<sup>47</sup>

Under section 523(a)(8) of the Bankruptcy Code, student loans are among these nondischargeable debts.<sup>48</sup> The Bankruptcy Code’s treatment of student loans is more complex than its treatment of most other nondischargeable debts in that the bar to relief is not absolute. Student loans can be discharged if the debtor can show that denial of discharge would “impose an undue hardship on the debtor and the debtor’s dependents.”<sup>49</sup> A party opposing discharge in an undue-hardship proceeding can settle by agreeing that the debtor is entitled to discharge.<sup>50</sup> The federal government’s policies on consent to student loan bankruptcy discharge are particularly important because most outstanding student loans have been issued under the government’s student loan programs.<sup>51</sup>

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41. See 11 U.S.C. §§ 727, 944(b), 1141, 1228(a), 1328(b) (2018) (providing for discharge of debts under Chapters 7, 9, 11, 12, and 13 of the Bankruptcy Code, respectively).

42. See *id.* § 524(a).

43. The American Bankruptcy Institute reports that there were 755,182 bankruptcy filings in 2018, of which 462,681 were Chapter 7 filings. *Newsroom: Statistics from Epiq Systems, December 2018 Bankruptcy Statistics – State and District*, AM. BANKR. INST., <https://www.abi.org/newsroom/bankruptcy-statistics?page=3%2C2> [<https://perma.cc/R9DN-WLNJ>].

44. See 11 U.S.C. § 704(a)(1) (2018) (Chapter 7 trustee “shall . . . collect and reduce to money the property of the estate for which such trustee serves”); *id.* § 727(a) (“[t]he court shall grant the debtor a discharge” in a Chapter 7 proceeding, with certain exceptions).

45. See *id.* § 523(a)(5) (providing a debt for a “domestic support obligation” is nondischargeable); *id.* § 101(14A) (defining “domestic support obligation” to include child support).

46. See *id.* § 523(a)(6).

47. See *id.* § 523(a)(2).

48. *Id.* § 523(a)(8). The Code provides for nondischargeability of three distinct categories of education-related obligations. See *id.* For simplicity, this Article refers to such obligations as “student loans.”

49. *Id.*

50. See Rafael I. Pardo & Michelle R. Lacey, *The Real Student-Loan Scandal: Undue Hardship Discharge Litigation*, 83 AM. BANKR. L.J. 179, 210 (2009) [hereinafter Pardo & Lacey, *The Real Student-Loan Scandal*] (discussing resolution of student-loan bankruptcies by settlement, that is, agreement about whether the debtor “should be granted an undue hardship discharge”).

51. According to the College Board, student loans originated under federal programs in the period 1997–2018 have accounted for from 75% (in 2006–07 and 2007–08) to 93% (in

### B. Overview of Major Federal Student Loan Programs

This Article discusses three major federal student loan programs, the Federal Perkins Loan Program (“Perkins program”), the Federal Family Education Loan Program (“FFEL program” or FFELP), and the William D. Ford Federal Direct Loan Program (“Ford program”). These are the major programs administered by the Department of Education: both the 2015 Dear Colleague Letter setting forth the Department’s bankruptcy discharge policy<sup>52</sup> and the Department’s *Federal Student Aid Portfolio Summary*<sup>53</sup> refer to these, and only these, three programs.<sup>54</sup>

The Perkins program was the oldest federal student loan program, tracing its history to the 1958 National Defense Education Act.<sup>55</sup> The program expired in September 2017.<sup>56</sup> Perkins loans were made from funds contributed in part by the government and in part by the student’s institution.<sup>57</sup> The higher education institution is (present tense because Perkins loans are still outstanding although new loans are not being made) the lender and is usually the party that decides whether to oppose a borrower’s petition for discharge.<sup>58</sup> Perkins loans outstanding at the end of the first

1997–98, 2009–10, 2010–11, and 2011–12) of the dollar value of all student loans. COLLEGE BOARD, *supra* note 11.

52. 2015 Dear Colleague Letter, *supra* note 22, at 1.

53. U.S. Dep’t of Educ., *Federal Student Aid Portfolio Summary*, FED. STUDENT AID, <https://studentaid.ed.gov/sa/about/data-center/student/portfolio> [<https://perma.cc/LE4A-AFRA>].

54. Other federal student-loan programs have existed. For example, the HEAL program provided health-education loans until 1998. U.S. Dep’t of Educ., *Health Education Assistance Loan (HEAL) Information*, FED. STUDENT AID, <https://ifap.ed.gov/health-education-assistance-loan-information> [<https://perma.cc/H3PP-Y6P5>] (reporting that last HEAL loans were made in 1998). In addition, the TEACH program, which provides grants to people studying to become teachers, might be considered a student-loan program because TEACH Grants convert to loans in some circumstances. See U.S. Dep’t of Educ., *TEACH Grants*, FED. STUDENT AID, <https://studentaid.ed.gov/sa/types/grants-scholarships/teach> [<https://perma.cc/3UUN-35EY>].

55. National Defense Education Act of 1958, Pub. L. No. 85-864, 72 Stat. 1580 (codified as amended in scattered sections of 20 U.S.C.).

56. See Jack O’Brien, *Congress Fails to Reauthorize Federal Perkins Loan Program—Here’s How It Could Impact Students*, NH J. (Oct. 3, 2017), <https://www.insidesources.com/congress-fails-reauthorize-federal-perkins-loan-program-heres-impact-students/> [<https://perma.cc/NUA2-FK94>].

57. See Nat’l Ass’n of College & Univ. Bus. Officers, *NACUBO Advisory Guidance 18-03: Perkins Loan Program Close-Out*, NACUBO 3 (August 2018), <https://www.nacubo.org/-/media/Nacubo/Documents/AdvisoryGuidance182PerkinsLoanProgramwinddown81618.aspx?la=en&hash=6090553A8E2D44FBCAC24FD0CF50A25E62743847> [<https://perma.cc/46X4-B3VL>] [hereinafter NACUBO Guidance].

58. See 2015 Dear Colleague Letter, *supra* note 22, at 1–2 (institution as holder decides whether to oppose discharge). Although the Dear Colleague letter treats the institution’s holding the loan in borrower bankruptcy as the typical case, it appears that the Department may become the loan holder if the institution is unable to collect. See 34 C.F.R. § 674.50(a)(1) (2019) (providing for assignment of defaulted note to United States); *id.* § 674.50(f)(1) (providing that United States acquires all “rights, title, and interest in” the loan upon assignment); *id.* § 674.50(c)(12) (providing that assigning institution must cooperate with

quarter of 2020 totaled \$5.9 billion, making Perkins the smallest of the three federal student loan programs discussed here.<sup>59</sup>

The FFEL program originated in the Higher Education Act of 1965 as the Guaranteed Student Loan (GSL) program<sup>60</sup> and received its current name in 1992.<sup>61</sup> Congress terminated the program in 2010 and no new loans have been made under it since June 30, 2010.<sup>62</sup> Under the FFELP, private lenders made loans to students. Most, if not all, FFELP loans still outstanding are guaranteed by “guaranty agencies,”<sup>63</sup> which can be state government or nonprofit organizations.<sup>64</sup> The guaranty agency reimburses the lender for losses arising from default and other events.<sup>65</sup> The Department in turn reimburses the guaranty agency for its payments to the private lender, provided certain conditions are met.<sup>66</sup> The guaranty agency typically holds the loan in borrower bankruptcy and decides whether to consent to discharge.<sup>67</sup> At the end of the first quarter of 2020, a total balance of \$257.2 billion was outstanding under the FFELP program.<sup>68</sup>

Under the Ford program, the federal government makes loans to students<sup>69</sup> and decides on consent to discharge itself.<sup>70</sup> After termination of the Perkins and FFELP

Secretary to “enforce the loan or loans”).

59. See U.S. Dep’t of Educ., *supra* note 53.

60. See U.S. Dep’t of Educ., *Federal Student Loan Programs Data Book, FY 1997–FY 2000*, ED.GOV, <https://www2.ed.gov/finaid/prof/resources/data/fslpdata97-01/edlite-intro.html> [<https://perma.cc/AKA9-Q5CC>].

61. See *id.*

62. See Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, §§ 2201–2208, 124 Stat. 1029, 1074–1077.

63. See 34 C.F.R. § 682.401(b)(5) (2019) (specifying what percentage of loan balance the guaranty agency is to guarantee).

64. See *id.* § 682.200 (defining “Guaranty Agency”). Guaranty agencies did not guarantee all GSL program and FFELP loans. The Department has guaranteed some student loans directly, without the involvement of a guaranty agency. See, e.g., Guaranteed Student Loan Program, 44 Fed. Reg. 53,866, 53,884 (Sept. 17, 1979) [hereinafter 1979 GSL Final Rule] (codified at 45 C.F.R. § 177.503(a)(2) (2019)) (describing basic structure of federally insured student loan program contract). The Department withdrew regulations governing such arrangements in 2013. See Student Assistance General Provisions, Federal Perkins Loan Program, Federal Family Education Loan Program, and William D. Ford Federal Direct Loan Program, 78 Fed. Reg. 65,768, 65,820 (Nov. 1, 2013) (removing and reserving subpart E of 34 C.F.R. pt. 682, which had governed guaranteed loans guaranteed directly by the federal government without the involvement of a guaranty agency). The 2015 Dear Colleague Letter does not mention federally insured loans. See 2015 Dear Colleague Letter, *supra* note 22.

65. See 34 C.F.R. § 682.100(b)(1) (establishing an exception for loans guaranteed directly by government, but stating generally that “a guaranty agency guarantees a lender against losses due to default by the borrower on a FFEL loan”).

66. See *id.* § 682.404(a) (specifying that government will pay guaranty agency 95 to 100% of the agency’s default claim losses on FFEL loans, depending on when loan was made).

67. See *id.* § 682.402(i).

68. See U.S. Dep’t of Educ., *supra* note 53.

69. See 34 C.F.R. § 685.100(a) (“Under the William D. Ford Direct Loan Program . . . , the Secretary makes loans to enable a student or parent to pay the costs of the student’s attendance at a postsecondary school.”).

70. See 2015 Dear Colleague Letter, *supra* note 22, at 1 (noting that Department follows

programs, the Ford program is the only one of the three still making loans. A total balance of \$1.251 trillion was outstanding under the Ford program at the end of the first quarter of 2020,<sup>71</sup> making it the largest federal student loan program.

### C. The 2015 Dear Colleague Letter

A Dear Colleague letter from the Department dated July 7, 2015 (“2015 Dear Colleague Letter”) sets out the Department’s current policies governing what loan holders are to do in deciding whether to object to discharge of student loans in bankruptcy.<sup>72</sup> The letter covers three federally supported loan programs: the Ford program, the FFELP, and the Perkins program.<sup>73</sup> The 2015 Dear Colleague Letter is based on regulations governing the FFEL and Perkins programs;<sup>74</sup> the Ford program does not have its own regulations governing the Department’s response to bankruptcy.

The identity of the loan holder varies depending on the loan program. The holder is the Department itself for direct loans.<sup>75</sup> The holder is usually a guaranty agency for FFEL program loans<sup>76</sup> and is usually a higher education institution for Perkins loans.<sup>77</sup> However, the substance of the analysis the letter prescribes is the same for all three programs.<sup>78</sup> A uniform approach seems sensible because a borrower may have loans of more than one type, although different entities will be responsible for making decisions for the different programs in that case.

The letter describes a two-step analysis. In the first step, the holder must determine whether it believes that the borrower will suffer “undue hardship” if the loan is not discharged.<sup>79</sup> The letter is arguably ambiguous about what the holder is to do if it reaches the “clear conclusion”<sup>80</sup> that discharge is necessary to avert undue hardship.

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the same discharge consent analysis for Ford program loans as it prescribes for holders of FFELP and Perkins loans).

71. U.S. Dep’t of Educ., *supra* note 53.

72. 2015 Dear Colleague Letter, *supra* note 22, at 1 (citing regulations governing treatment of FFEL and Perkins, but not Direct Loan Program, loans in bankruptcy).

73. The letter does not cover some older loan programs, such as the federally insured GSL program discussed below and the HEAL Program. The HEAL program regulations do not discuss consent to discharge. *See* 34 C.F.R. § 681.1 (2019). New loans under the HEAL program stopped in 1998, the program loan balance outstanding dropped to \$187 million by 2014, and the HEAL regulations apparently are not historically linked to the Ford regulations as the FFEL and Perkins regulations are. *See* Health Education Assistance Loan Program, 82 Fed. Reg. 53,374, 53,374–75 (Nov. 15, 2017) (to be codified at 34 C.F.R. pt. 681). Thus, this Article does not further discuss the HEAL program.

74. 2015 Dear Colleague Letter, *supra* note 22, at 1.

75. *See id.*

76. *See id.*

77. *See id.*

78. *See id.* (“While this letter addresses the holders of FFELP and Perkins loans, the Department follows the same two-step analysis when evaluating whether to consent or not object to a borrower’s claim of undue hardship for the William D. Ford Direct Loan Program (Direct Loans), or for FFELP and/or Perkins loans the Department holds.”).

79. *Id.* at 1–2.

80. *Id.* at 11. Elsewhere, the letter refers to the “conclusion” that repayment would impose

At one point, the letter states that the holder “should consent to, or not oppose, the discharge”<sup>81</sup> in this circumstance. At another point, it states that the holder “can” consent to discharge if undue hardship is present.<sup>82</sup> The latter formulation could be read to mean that the holder has the freedom to choose whether to consent, but probably the “should consent” is controlling. Given that the Department is instructing holders about what to do, “should” most likely indicates a requirement rather than a mere suggestion.<sup>83</sup> So read, “should” is consistent with “can,” whereas interpreting “can” to mean “may choose whether to” is inconsistent with “should.” The “should” interpretation thus technically gives effect to both terms, although it is strange for the Department to say the holder “can” do something when it means “should.”

“Undue hardship” is a term used in the Bankruptcy Code and courts have interpreted it in that context.<sup>84</sup> The 2015 Dear Colleague Letter states that holders’ analysis of undue hardship “would necessarily be made according to the legal standards set by the Federal courts,”<sup>85</sup> asserting that the Congress “has not delegated to the Department the authority” to define “undue hardship.”<sup>86</sup> The letter discusses two tests the federal courts have used to evaluate undue hardship, the *Brunner* test and the totality-of-the-circumstances test.<sup>87</sup>

If the holder determines that “requiring repayment would not impose an undue hardship,”<sup>88</sup> analysis proceeds to a second step. In that step, the holder must “evaluate the cost of objecting to the borrower’s claim of undue hardship in court.”<sup>89</sup> Specifically, the holder is to determine whether “the costs to pursue the matter in bankruptcy court are estimated to exceed one-third the total amount owed on the loan.”<sup>90</sup> If the estimated costs do exceed the one-third threshold, the holder “may

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undue hardship. *Id.* at 10.

81. *Id.* at 10.

82. *Id.* at 2 (stating that the holder “can consent to or not oppose the discharge”).

83. *See, e.g.,* United States v. Davis, 724 F.3d 949, 955 (7th Cir. 2013) (explaining that “both words”—that is, “should” and “must”—are “imperative when used to instruct a jury on whether to convict a defendant”); United States v. Kerley, 838 F.2d 932, 940 (7th Cir. 1988) (finding no substantive difference between “should” and “must” when used in jury instructions); State v. Lovelace, 607 P.2d 49, 55 (Kan. 1980) (“should” and “must” “can be used interchangeably in criminal instructions”).

84. *See e.g.,* Ann K. Wooster, Annotation, *Discharge of Student Loan on Ground of Undue Hardship Under Bankruptcy Code of 1978 (11 U.S.C.A. § 523(a)(8)(B))—Good Faith Based on Compliance with Congressional Policy*, 59 A.L.R. Fed. 2d 563 (2011) (collecting decisions); Ann K. Wooster, Annotation, *Discharge of Student Loan on Ground of Undue Hardship Under Bankruptcy Code of 1978 (11 U.S.C.A. § 523(a)(8)(B))—Good Faith Based on Making Payments and Negotiating Repayment Plan*, 62 A.L.R. Fed. 2d 545 (2012); Ann K. Wooster, Annotation, *Discharge of Student Loan on Ground of Undue Hardship Under Bankruptcy Code of 1978 (11 U.S.C.A. § 523(a)(8)(B))—Good Faith Based on Maximizing Income and Minimizing Expenses*, 60 A.L.R. Fed. 2d 375 (2011).

85. 2015 Dear Colleague Letter, *supra* note 22, at 3.

86. *Id.*

87. This Article discusses those tests *infra* at Section III.B.2.

88. 2015 Dear Colleague Letter, *supra* note 22, at 2.

89. *Id.*

90. *Id.* at 3.

accept and/or not oppose an undue hardship claim.”<sup>91</sup> If the estimated costs fall under the one-third limit, the holder apparently “must” oppose discharge.<sup>92</sup>

The 2015 Dear Colleague Letter is a guidance document rather than a regulation.<sup>93</sup> The regulations for the Perkins and FFEL programs control those programs and are the source of the rules in the letter,<sup>94</sup> although the letter reflects the Department’s interpretation of the regulations and does not simply repeat them.

#### *D. Overview of Discharge Consent Regulation History*

Section I.D gives a summary overview of the history of the regulations governing consent to discharge in student loan bankruptcies. A companion paper gives a complete history of the regulations.<sup>95</sup>

As discussed, the Department’s current rules governing consent to discharge contemplate a two-step analysis. First, the holder evaluates whether discharge is necessary to avert “undue hardship” on the borrower’s part. Second, the holder determines whether opposing discharge is cost-effective (that is, would cost less than one-third the amount outstanding on the loan).<sup>96</sup>

The Perkins program is the source of the two-step framework, which originates in Perkins program rules adopted in 1987.<sup>97</sup> The only later development of interest in the Perkins rules is that the Department amended them in 1999 to add the statement that the “institution must use due diligence . . . to avoid discharge of the loan.”<sup>98</sup> As discussed below,<sup>99</sup> this requirement is of unclear scope.

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91. *Id.* at 3–4.

92. *Id.* at 11. The quoted sentence actually does not refer to the one-third test by name. Instead, it states that the holder must oppose discharge “unless the cost of opposing it warrants otherwise, as set forth in 34 C.F.R. §§ 674.49(c) and 682.402(i)(1).” *Id.* The reference to cost of opposition is presumably to the one-third test, which is the only test for cost-effectiveness mentioned in the letter and is described in the regulations the quoted sentence cites. *See id.*; 34 C.F.R. §§ 674.49(c), 682.402(i)(1) (2019). The cited regulations govern the Perkins and FFEL programs respectively. *See* 34 C.F.R. pt. 674 (Perkins); *id.* pt. 682 (FFEL). Interestingly, the letter discusses evaluating cost-effectiveness of discharge litigation five times, *see* 2015 Dear Colleague Letter, *supra* note 22, at 2, 3–4, 8 & n.5, 11, and mentions the one-third test only once (in addition to the cross-reference to the test at 11). One might speculate that this treatment suggests a discomfort with the rigid one-third test and an interest in a more nuanced analysis of cost-effectiveness.

93. 2015 Dear Colleague Letter, *supra* note 22, at 1 (“This letter provides guidance . . .”).

94. *Id.* (providing guidance to holders “as they continue to implement [Perkins and FFELP regulations] which govern their actions in defending bankruptcy adversary proceedings” and “to assist loan holders in fulfilling their regulatory duty”).

95. *See* John Patrick Hunt, *The Development of Student Loan Bankruptcy Policy*, 45 J.C. & U.L. 85, 89–110 (2020).

96. *See supra* Section I.C.

97. *See* Perkins Loan Program, 52 Fed. Reg. 45,552, 45,560 (Nov. 30, 1987) (codified at 34 C.F.R. § 674.49(b)(2)) [hereinafter 1987 Perkins Rules].

98. Federal Perkins Loan Program, 64 Fed. Reg. 58,298, 58,313 (Oct. 28, 1999) (codified at 34 C.F.R. § 674.49(c)(1)) [hereinafter 1999 Perkins Rules].

99. *See infra* Section II.B.1.

Turning to the GSL program, and its successor, the FFEL program, here the Department first adopted bankruptcy discharge opposition rules in 1986. These rules provided that holders “shall diligently contest” discharge.<sup>100</sup> In 1992, the Department adopted rules for the FFEL program that prescribed a two-step process paralleling the one it adopted for the Perkins program in 1987.<sup>101</sup> In 1999, the Department added to the FFEL rules a requirement that holders “must use diligence . . . to avoid discharge of the loan.”<sup>102</sup> As with the corresponding requirement for the Perkins program, the scope here is unclear. In 2001, the Department added that the holder “may, but is not required to” oppose discharge if it determines that the cost of doing so would be more than one-third the balance due on the loan.<sup>103</sup>

As for the Ford program, no regulations govern consent to discharge under it. The Department’s 2015 Dear Colleague Letter appears to be the only source of guidance for this, the largest student loan program. It is not clear why there are no regulations; perhaps their absence reflects the Department’s commitment to reserve the “full discretion accorded [it]” under the statutes, as it declared its intention to do in 1985.<sup>104</sup>

## II. “TRANS-SUBSTANTIVE” OBSERVATIONS AND RECOMMENDATIONS

Part II offers observations and recommendations on “trans-substantive” aspects of the rules, that is, aspects other than how readily the Department grants or withholds discharge. “Trans-substantive” is in quotation marks because some of the recommendations, such as the recommendation to create safe harbors, may affect the substance of the regulations. However, the effect of such recommendations is different enough from actually adding new grounds for consent to discharge that they are included here. Part II addresses three aspects of the rules: (1) thoughtfulness; (2) completeness, uniformity, and clarity; and (3) predictability.

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100. Guaranteed Student Loan and PLUS Programs, 51 Fed. Reg. 40,886, 40,905 (Nov. 10, 1986) (codified at 34 C.F.R. § 682.402(g)(1)) [hereinafter 1986 GSL PLUS Final Regulations].

101. See Federal Family Educational Loan Programs, 57 Fed. Reg. 60,280, 60,349 (Dec. 18, 1992) (to be codified at 34 C.F.R. § 682.402(g)(1)) [hereinafter 1992 FFEL Rules].

102. Federal Family Education Loan Program and William D. Ford Federal Direct Loan Program, 64 Fed. Reg. 58,938, 58,960 (Nov. 1, 1999) (codified at 34 C.F.R. § 682.402(i)(1)(iv)) [hereinafter 1999 FFEL Ford Final Rules].

103. Federal Family Education Loan Program and William D. Ford Federal Direct Loan Program, 66 Fed. Reg. 34,762, 34,763 (June 29, 2001) (codified at 34 C.F.R. § 682.402(i)(1)(iii)) [hereinafter 2001 FFEL Ford Final Rules].

104. Guaranteed Student Loan Program and PLUS Program, 50 Fed. Reg. 35,964, 35,966 (Sept. 4, 1985) (codified at 34 C.F.R. pts. 682–83) [hereinafter 1985 GSL PLUS NPRM]. Although the Department has stated that it follows the process set forth in the 2015 Dear Colleague Letter, *see supra* Section I.C, that letter is subject to being changed without notice-and-comment rulemaking, *see infra* note 380 and accompanying text. Thus, in the absence of regulations, the Department enjoys considerable freedom of action.

### A. On Thoughtful Rules

It is currently difficult to tell why the Department has the rules it does because its rules were offered with very little explanation.<sup>105</sup> In particular, the Department apparently has never considered whether its bankruptcy discharge policies do or should reflect the overall purposes of the student loan programs.<sup>106</sup> The Department should offer a better account of the reasons for its policies, and its current proceeding to reconsider the rules offers an excellent opportunity to do so.

#### 1. The Rules Have Been Issued Without Thorough Explanation

The Department took the key steps in the development of discharge consent policy with little or no explanation. The proposal to require holders to oppose discharge appeared in a 1985 notice of proposed rulemaking (NPRM) for the Perkins program. The single sentence supporting the proposal stated that it “reflect[ed] changes in bankruptcy law.”<sup>107</sup> A NPRM later that year for the FFELP’s predecessor, the GSL program, proposed a requirement that guaranty agencies “diligently contest” discharge,<sup>108</sup> which was adopted as a final rule in 1986.<sup>109</sup> The Department did not offer a specific justification for either proposal.<sup>110</sup>

The 1987 Perkins final rule adopting the two-step framework in effect today was explained in a single paragraph. That paragraph defended the decision to issue regulations rather than the regulations’ content, although there is a suggestion that the Department was trying to avoid litigation costs that did not generate a financial return.<sup>111</sup>

A 1990 NPRM that proposed to apply the Perkins two-step framework to the much larger GSL program provided no specific explanation for the proposal.<sup>112</sup> The NPRM did reference “various policy initiatives designed to reduce defaults and increase collection on loans that do go into default,” and perhaps this was an oblique reference to the new bankruptcy rules, but there was no further explanation.<sup>113</sup> The

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105. For the history of the Department’s regulations, see Hunt, *supra* note 95, at 89–110.

106. *See infra* Sections III.A–III.B.1.

107. National Direct Student Loan Program, 50 Fed. Reg. 7872, 7873 (Feb. 26, 1985) (codified at 34 C.F.R. § 674.49) [hereinafter 1985 NDSL/Perkins NPRM].

108. 1985 GSL PLUS NPRM, *supra* note 104, at 35,981.

109. 1986 GSL PLUS Final Regulations, *supra* note 100, at 40,905.

110. *See* 1985 GSL PLUS NPRM, *supra* note 104; 1986 GSL PLUS Final Regulations, *supra* note 100.

111. *See* 1987 Perkins Rules, *supra* note 97, at 45,555 (“[B]ecause the regulations now permit institutions to charge to the Fund the costs of the litigation required in bankruptcy, it is appropriate to prescribe here the circumstances in which particular activities are reasonable and cost-effective.”).

112. *See* Guaranteed Student Loan Programs, 55 Fed. Reg. 48,324 (Nov. 20, 1990) [hereinafter 1990 GSL NPRM].

113. *Id.* at 48,324. The quoted language may not have referred to default: it appears that bankruptcy generally is not a default on FFELP loans. *See* U.S. Dep’t Educ., *Student Loan Delinquency and Default*, FED. STUDENT AID, <https://studentaid.ed.gov/sa/repay-loans/default#default> [<https://perma.cc/D66L-TE9S>] (defining “default” as failure to make scheduled payments for 270 days).



1992 FFEL final rule adopted the discharge opposition proposal from the 1990 NPRM without any discussion at all.<sup>114</sup> Nor did the Department give a justification for its 1999<sup>115</sup> and 2001<sup>116</sup> changes to the FFEL and Perkins regulations.

As for the Ford program, the largest federal loan program by far and the only one of the three that is still making loans, we have only a Dear Colleague letter that describes, but does not defend, the two-step analytical framework that it apparently borrowed from the FFEL and Perkins regulations.<sup>117</sup>

## 2. The Department Should Thoughtfully Explain Its Rules

The Department's relative inattention to discharge consent policy is inappropriate in light of the importance of student loan bankruptcies. Jason Iuliano has estimated that over 238,000 debtors with student loans made consumer bankruptcy filings in 2007,<sup>118</sup> but only a tiny fraction of student loan debtors who filed bankruptcy sought to discharge their student loans.<sup>119</sup> Given the relatively high rate of relief for cases

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114. See 1992 FFEL Rules, *supra* note 101.

115. See 1999 FFEL Ford Final Rules, *supra* note 102; 1999 Perkins Rules, *supra* note 98.

116. See 2001 FFEL Ford Final Rules, *supra* note 103.

117. See *supra* Section I.C.

118. Jason Iuliano, *An Empirical Assessment of Student Loan Discharges and the Undue Hardship Standard*, 86 AM. BANKR. L.J. 495, 504 (2012) (deriving estimate by multiplying the percentage of bankruptcy debtors who indicated in the Consumer Bankruptcy Project survey that they had student debt by the total number of bankruptcy filings). Although Professor Rafael Pardo has criticized Iuliano's study at length, the criticisms do not seem to extend to this particular estimate. See Pardo, *The Undue Hardship Thicket*, *supra* note 8, at 2122–42 (criticizing several aspects of Iuliano's study but not his estimate of the total number of student-loan consumer bankruptcy filings).

119. Iuliano estimates that the fraction is "0.1" percent. Iuliano, *supra* note 118, at 505. He examines adversary proceedings to discharge student debt filed against the ten largest student-loan lenders (and Educational Credit Management Corporation) in 2007. *Id.* at 502. The surveyed entities reportedly held 71.2% of student loans in that year, so Iuliano estimates that 71.2% of the 238,446 bankrupt debtors with student loans, or 169,774 debtors total, owed money to these entities. *Id.* at 504–05. He then reports based on PACER searches that 217 adversary proceedings to discharge student debt, filed by 213 separate debtors, were initiated against the ten lenders and ECMC. *Id.* at 503. From these numbers, one can compute an estimate of the overall rate at which student-loan debtors sought discharge:  $213/169,774 = 0.125\%$ . This computation is apparently the basis for the 0.1% number in Iuliano's text. See *id.* at 504–05. Pardo subsequently argued that Iuliano's method probably undercounted adversary proceedings. See Pardo, *The Undue Hardship Thicket*, *supra* note 8, at 2127–29. In response, Iuliano counted the number of student-loan adversary proceedings directly by searching PACER on a special "nature of suit" (NOS) code for such proceedings in a way that he asserted was not possible when he conducted his initial study. This search found that 445 student loan debtors filed undue hardship proceedings during 2007. See Iuliano, *supra* note 3, at 381–82. The author makes the following observations: because the 445 adversary proceedings found using the NOS code is the total number of suits filed in the United States against all defendants, we can estimate the rate at which student-loan debtors filed adversary proceedings by dividing 445 by the total number of student-loan debtors who filed bankruptcy. Using Iuliano's estimate of 238,446 student-loan bankruptcies in 2007 for the latter number, we arrive at an estimate of  $445/238,446 = 0.187\%$  for the rate at which bankrupt student-loan

that are actually brought<sup>120</sup> and the cost and uncertainty that currently attend student loan discharge proceedings,<sup>121</sup> more bankrupt debtors probably should try to discharge their student loans. It is reasonable to suppose that many borrowers are living with undue hardship created by their student loans.

Student loan bankruptcy remains vital despite the advent of income-driven repayment (IDR) plans that base loan payments on the borrower's income. Although IDR programs do reduce the need for bankruptcy proceedings by reducing payments, bankruptcy remains important because IDR may extend indebtedness,<sup>122</sup> result in negative amortization,<sup>123</sup> and impose significant tax burdens when debt is forgiven at the end of the IDR period.<sup>124</sup> For debtors with unavoidable high expenses, such as

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debtors initiate adversary proceedings in bankruptcy. Although this computation suggests that Iuliano may have underestimated the rate of filing by about a third, 0.187% is, like 0.125%, a tiny fraction. Even the 0.187% estimate can be criticized because some adversary proceedings are filed in a year after the year in which the bankruptcy is filed, *see* Pardo, *The Undue Hardship Thicket*, *supra* note 8, at 2126–27, so that the 445 and the 238,446 are not perfectly comparable. Moreover, perhaps applying the rate of owing student loans from the Consumer Bankruptcy Project sample to the entire population of bankruptcy debtors could be criticized. However, these issues do not seem likely to change the fundamental conclusion that only a tiny fraction of student-loan debtors seek discharge.

120. Iuliano finds that 39% of student-loan debtors who filed adversary proceedings in 2007 seeking discharge of their loans received a full or partial discharge, and that 12% more received administrative repayment plans. *See* Iuliano, *supra* note 118, at 505. Other researchers have made broadly similar findings. *See* Rafael I. Pardo, *Taking Bankruptcy Rights Seriously*, 91 WASH. L. REV. 1115, 1118, 1137–38 (2016) (finding in study of 1430 student-loan discharge proceedings from around the country that debtors experienced litigation success, designated as entry of an order granting any form of relief, 39% of the time); Pardo & Lacey, *The Real Student-Loan Scandal*, *supra* note 50, at 213 (concluding based on review of 115 cases filed in the Western District of Washington in 2002 to 2006 that “[a]pproximately 57% of the adversary proceedings resulted in an undue hardship discharge”); Pardo & Lacey, *Undue Hardship in the Bankruptcy Courts*, *supra* note 9, at 410, 479 (concluding based on examination of bankruptcy-court opinions issued from 1993 to 2003 that “[m]ore than half (57%) of the 286 discharge determinations in the sample granted the debtor some form of relief—whether in the form of full discharge, partial discharge, or equitable adjustment” and that “[n]early half (45%) of the discharge determinations analyzed concluded that failing to discharge a debtor’s student loans would impose an undue hardship on the debtor”); Aaron N. Taylor & Daniel J. Sheffner, *Oh, What a Relief It (Sometimes) Is: An Analysis of Chapter 7 Bankruptcy Petitions to Discharge Student Loans*, 27 STAN. L. & POL’Y REV. 295, 320 (2016) (based on a sample of cases filed between 2005 and 2014, finding undue-hardship discharge rates of 54% for the First Circuit and 24% for the Third Circuit in cases where the proceeding went all the way to an undue-hardship decision); *id.* at 323 (finding overall rates of student-loan relief of 51% in the First Circuit and 46% in the Third Circuit when considering all cases in which relief was sought, not just ones that went to decision, and when considering settlements and default judgments in addition to undue-hardship discharges as forms of relief).

121. *See infra* Section II.C.2.

122. *See* John Patrick Hunt, *Help or Hardship? Income-Driven Repayment in Student-Loan Bankruptcies*, 108 GEO. L.J. 1287, 1333–38 (2018).

123. *See id.* at 1339–40.

124. *See id.* at 1340–49.

medical costs, IDR may be unaffordable.<sup>125</sup> Moreover, IDR is an inappropriate solution to overwhelming indebtedness when the debt has been in repayment for more than five years and there is no prospect of significant financial recovery. That is because financial recovery is the only justification Congress advanced for nondischargeability of such older student debts.<sup>126</sup>

Reflecting the continuing importance of student loan bankruptcy, the Department issued a request for information on the subject in 2018. The Department invited the public to comment on the “circumstances under which loan holders should concede an undue hardship claim by the borrower” and “whether and how the 2015 Dear Colleague Letter should be amended,” among other questions about the Department’s undue-hardship policy.<sup>127</sup> Response to the Department’s call was robust. The Department received 419 comments, notably including responses from the offices of the Attorneys General of New York and Massachusetts and from stakeholder groups such as the Consumer Bankers Association, the National Association of Student Financial Aid Administrators, the National Consumer Law Center, and the Student Loan Servicing Alliance.<sup>128</sup> The Department should stay the course, consider the input it has received, and produce a carefully and thoroughly reasoned statement of its bankruptcy policies.

One set of comments is particularly noteworthy. Twenty-one academics (a number that later grew to over forty) suggested that the Department presume undue hardship for borrowers who meet certain objective criteria.<sup>129</sup> In other words, these commenters suggest that the Department adopt “safe harbors” for borrowers, an idea this Article discusses in Section II.C.2.

### *B. On Complete, Uniform, and Clear Rules*

The Department’s discharge consent rules are incomplete, nonuniform, and ambiguous. Although the 2015 Dear Colleague Letter, generously interpreted, addresses these issues, it is only a guidance document. The Department should consider notice-and-comment rulemaking to fix the regulations themselves.

#### 1. The Rules Have Been Incomplete, Nonuniform, and Ambiguous

Both the Perkins and the FFEL regulations have significant gaps and ambiguities (collectively called “defects” here). The 2015 Dear Colleague Letter probably fills

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125. *See id.* at 1330–33.

126. *See id.* at 1338–39.

127. Request for Information on Evaluating Undue Hardship Claims in Adversary Actions Seeking Student Loan Discharge in Bankruptcy Proceedings, 83 Fed. Reg. 7460, 7461 (Feb. 21, 2018).

128. *See* Request for Information on Evaluating Undue Hardship Claims in Adversary Actions Seeking Student Loan Discharge in Bankruptcy Proceedings Under 11 U.S.C. § 523(a)(8), REGULATIONS.GOV, <https://www.regulations.gov/docket?D=ED-2017-OPE-0085> [<https://perma.cc/B4F3-U9UJ>]. The academics’ comments also appear at Jiménez et al., *supra* note 16. Over forty academics had signed on to the comments by the time of law-review publication. *Id.* at 114.

129. *See* Jiménez et al., *supra* note 16, at 115.

those gaps and resolves those ambiguities, although it may itself be ambiguous in at least one respect.

The first defect is that neither the Perkins nor the FFEL regulations have ever explicitly told the holder what to do if it determines that repayment would entail undue hardship.<sup>130</sup> However, in each case only the absence of undue hardship triggers a second step of analysis, the comparison of likely costs of opposing discharge to one-third of the loan balance.<sup>131</sup> That the presence of undue hardship terminates the analysis before consideration of the costs of opposing discharge strongly suggests that the holder either may or must consent to discharge if undue hardship is present, although it sheds no light on whether the operative verb is “may” or “must.” The 2015 Dear Colleague Letter probably fills the gap here. It provides that if repayment would cause undue hardship, the holder “should consent to or not oppose the discharge,”<sup>132</sup> although the letter may be ambiguous on this point.<sup>133</sup>

The second defect is that the FFEL and Perkins regulations are ambiguous. Each has a provision of unclear scope, added in 1999 without substantive explanation, that holders “must use due diligence . . . to avoid discharge of the loan.”<sup>134</sup> These provisions could be interpreted to impose an unqualified duty to oppose discharge in all circumstances. Because these provisions may impose a universal duty to oppose discharge, while another part of each program’s regulations provides a two-step framework for deciding whether to oppose discharge,<sup>135</sup> the regulations are ambiguous. Although universally mandating opposition probably is not the 1999 insertions’ purpose,<sup>136</sup> the provisions detract from the regulations’ clarity. The 2015 Dear Colleague Letter deals with the ambiguity after a fashion: it simply ignores the 1999 requirements, perhaps reflecting an implicit interpretation that they specify the diligence required once a holder has decided to oppose discharge, rather than instructing the holder when to oppose discharge in the first place.

The third defect relates to the regulations’ one-third-of-balance test, the second step in the two-step analysis the regulations prescribe.<sup>137</sup> If the holder determines that undue hardship is absent, both the Perkins and the FFEL regulations direct the holder to compare the expected costs of opposing discharge with one-third the loan

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130. For the GSL/FFEL program, see 2001 FFEL Ford Final Rules, *supra* note 103; 1999 FFEL Ford Final Rules, *supra* note 102; 1992 FFEL Rules, *supra* note 101; 1986 GSL PLUS Final Regulations, *supra* note 100. For the Perkins program, see 1999 Perkins Rules, *supra* note 98; 1987 Perkins Rules, *supra* note 97. As discussed, no regulations govern the Ford program. *See supra* Section I.D.

131. *See* 34 C.F.R. § 674.49(c)(4) (2019) (Perkins); *id.* § 682.402(i)(1)(iii) (FFEL).

132. 2015 Dear Colleague Letter, *supra* note 22, at 10.

133. *See id.* at 2 (providing that holder “can” consent to discharge if undue hardship is present). Section II.B.1, *supra*, discusses the ambiguity.

134. 1999 Perkins Rules, *supra* note 98, at 58,313 (“[I]nstitution must use due diligence . . . to avoid discharge of the loan.”); 1999 FFEL Ford Final Rules, *supra* note 102, at 58,960 (holders “must use diligence . . . to avoid discharge of the loan”).

135. *See supra* notes 97 (Perkins), 101 (FFELP).

136. The detailed two-step process for deciding whether to oppose discharge would be superfluous if the cited provisions always required holders to do so. It seems likely, though not certain, that the cited provisions govern holders’ conduct once they have decided to oppose discharge, or at least not to consent to it. *See* Hunt, *supra* note 95, at 92, 96–97, 106–07.

137. *See supra* Section I.D.

balance.<sup>138</sup> However, the regulations for the two programs differ in the consequence of the comparison. The Perkins regulations prescribe that the holder “shall” oppose discharge if the cost of opposition is *less* than one-third of the balance.<sup>139</sup> The FFEL regulations, which once contained the same requirement,<sup>140</sup> now prescribe that the holder “may, but is not required to” oppose discharge if the cost of opposition is *more* than one-third of the balance.<sup>141</sup>

Thus, the regulations also have gaps relating to the one-third test: the Perkins regulations are silent about what to do if estimated costs exceed one-third of the loan balance,<sup>142</sup> and the FFEL regulations are silent about what to do if estimated costs are less than one-third of the balance.<sup>143</sup>

Moreover, the one-third test is nonuniform across programs: the shall-oppose-if-less-than-one-third requirement of the Perkins program differs from the may-oppose-if-more-than-one-third requirement of the FFEL program. Ideally, the rules probably should be uniform. Debtors may have more than one type of loan; there does not appear to be a substantive reason to have different rules for different programs, and relatedly, the difference that exists seems to be one of wording rather than a policy choice.<sup>144</sup>

The 2015 Dear Colleague Letter appears to impose uniformity and fill the gaps. It provides, for all three programs, that if undue hardship is absent and the estimated cost of litigation is less than one-third the loan balance, the holder “must” oppose discharge,<sup>145</sup> while the holder “may” consent to discharge if the estimated litigation cost is greater than one-third of the loan balance.<sup>146</sup>

The 2015 Dear Colleague Letter’s resolution of the first two defects might be considered “pro-bankrupt-debtor.” The letter specifies that the holder “should consent” to discharge in cases of undue hardship and reads out of the regulations a provision that could be read to require universal opposition to discharge.<sup>147</sup>

The letter’s approach to the third defect, by contrast, is “anti-bankrupt-debtor” in its effect. Gaps about what to do if expected opposition costs fall below the one-third threshold are filled with the “must oppose discharge” requirement from the Perkins regulations<sup>148</sup> when “may oppose discharge” would be a plausible alternative for the non-Perkins programs. Likewise, gaps about what to do if expected costs exceed the

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138. See 34 C.F.R. §§ 674.49(c)(4), 682.402(i)(1)(iii) (2019).

139. See *id.* §§ 674.49(c)(5), 682.402(i)(1)(iii).

140. See 1992 FFEL Rules, *supra* note 101, at 60,349.

141. See 34 C.F.R. § 682.402(i)(1)(iii).

142. See 34 C.F.R. § 674.49(c).

143. See 34 C.F.R. § 682.402(i).

144. If the Department adds grounds for consent to discharge as this Article suggests without engaging in notice-and-comment rulemaking to amend the restrictive Perkins regulations, rules that are nonuniform across programs could result. See *infra* Sections III.C.4–III.C.5. A desire for uniformity should not in this case overcome the important substantive interest in promoting the programs’ goals by liberalizing discharge, particularly in light of the small size of the Perkins program.

145. 2015 Dear Colleague Letter, *supra* note 22, at 11.

146. *Id.* at 3–4.

147. See *supra* note 134 and accompanying text.

148. See *supra* note 139 and accompanying text.

one-third threshold are filled with the “may consent to discharge” provision from the FFEL regulations<sup>149</sup> when “must consent to discharge” would be a plausible alternative for the non-FFEL programs. Although both these decisions promote a desirable uniformity across programs, they are unfriendly to bankrupt student loan debtors.

## 2. The Department Should Consider Notice-and-Comment Rulemaking to Complete, Make Uniform, and Clarify the Rules

This Section argues that the Department should consider remedying the defects in the regulations with notice-and-comment rulemaking, the process required for the Department to amend its discharge-consent regulations.<sup>150</sup> It first addresses ratifying the pro-borrower provisions of the 2015 Dear Colleague Letter and then considers rejecting the anti-borrower provisions.

For the pro-bankrupt-debtor aspects of the letter (i.e., consent to discharge in case of undue hardship and restricted scope of possible universal-opposition section of regulations), a reason for the Department to consider notice-and-comment rulemaking is that the Dear Colleague Letter, a guidance document, may not be authoritative. At least for the Perkins and FFEL programs, the 2015 Dear Colleague Letter interprets existing regulations.<sup>151</sup> But agencies’ claim to deference to their interpretations of their regulations is under threat in the Supreme Court.<sup>152</sup> Although the 2015 Dear Colleague Letter’s status as a guidance document might shield it on finality and ripeness grounds from judicial review,<sup>153</sup> there is no assurance of such protection. Accordingly, the 2015 Dear Colleague Letter may be vulnerable. Notice-and-comment rulemaking would enable the Department to issue new regulations that unambiguously reflect the 2015 Dear Colleague Letter’s position and would therefore be immune from attack as improper interpretations of regulations.

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149. See *supra* notes 140–41 and accompanying text.

150. See *Homemakers North Shore, Inc. v. Bowen*, 832 F.2d 408, 413 (7th Cir. 1987) (“[O]nce a regulation is adopted by notice-and-comment rulemaking . . . its text can only be amended in that fashion.”); see also 1 CHARLES H. KOCH, JR. & RICHARD MURPHY, *ADMINISTRATIVE LAW & PRACTICE* § 4:60 (2018) (“[A]n agency must follow notice-and-comment rulemaking in order to amend or repeal a legislative rule.”).

151. See 2015 Dear Colleague Letter, *supra* note 22, at 1–2.

152. Current precedent provides for judicial deference to agencies’ interpretations of their own regulations. See *Auer v. Robbins*, 519 U.S. 452, 463 (1997); *Bowles v. Seminole Rock & Sand Co.*, 325 U.S. 410, 414 (1945). The Court recently upheld the so-called *Auer* deference doctrine, but Justice Roberts, the deciding vote, did so on the ground of *stare decisis* only. See *Kisor v. Wilkie*, 139 S. Ct. 2400, 2424 (2019) (Roberts, J., concurring in part). Justice Roberts wrote separately to emphasize that the difference between the *Auer* doctrine as formulated in *Kisor* and no deference at all “is not as great as it may initially appear,” *id.*, and Justice Kavanaugh also emphasized this point, *id.* at 2448 (Kavanaugh, J., concurring). Justice Gorsuch described the decision as “more a stay of execution than a pardon” for the *Auer* doctrine. *Id.* at 2425 (Gorsuch, J., concurring).

153. See, e.g., Mark Seidenfeld, *Substituting Substantive for Procedural Review of Guidance Documents*, 90 TEX. L. REV. 331, 375 (2011) (“[D]octrines of finality and ripeness often shield the agency from the potentially paralyzing effects of ‘direct’ substantive judicial review of guidance documents—that is, review of such documents when issued.”).

A major reason not to engage in notice-and-comment rulemaking is the familiar point that that process is costlier and more time-consuming than issuing a guidance document.<sup>154</sup> That issue is relatively significant here, where risk of legal attack may not be that great: the two pro-borrower provisions have not, to the author's knowledge, been controversial. On the other hand, as discussed shortly, this Article unequivocally recommends notice-and-comment rulemaking for at least the Perkins program.<sup>155</sup> If the Department is carrying out a rulemaking anyway, there may not be much additional burden involved in addressing the provisions under discussion.

To be sure, additional considerations could potentially be relevant.<sup>156</sup> But the decision about notice and comment to ratify the two pro-borrower provisions depends on weighing the resource consumption of such a process against the legal risk of relying solely on a guidance document.

We now turn to the anti-bankrupt-debtor provision of the 2015 Dear Colleague Letter, the one that unnecessarily requires opposition to discharge if the cost of opposition would be less than one third of the loan balance and unnecessarily permits opposition to discharge if the cost of opposition would be more than one third of the loan balance.<sup>157</sup> Here, this Article's recommendation is unequivocal: the Department should engage in notice-and-comment rulemaking, at least to amend the Perkins regulations' provision that the holder "shall" oppose discharge if undue hardship is absent and expected opposition costs fall below the one-third threshold.<sup>158</sup>

The reason is that the "shall oppose" requirement is counter to the central recommendation of this Article. As explained below, the Department can promote the purposes of the student loan programs more effectively by providing for consent to discharge on substantive grounds other than undue hardship.<sup>159</sup> For example, it could consent on the grounds of borrower discouragement or harm.<sup>160</sup> The Perkins "shall oppose" regulation makes it difficult to implement this suggestion—at least for the Perkins program—because it requires the holder to oppose discharge whenever undue hardship is absent and opposition is expected to cost less than one-

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154. See Steven J. Lindsay, *Timing Judicial Review of Agency Interpretations in Chevron's Shadow*, 127 YALE L.J. 2448, 2451 (2017) ("Th[e] process of notice-and-comment rulemaking can be costly and time-consuming."). The Department is subject to a special provision requiring it to engage in a negotiated rulemaking process before starting notice and comment. See 20 U.S.C. § 1098a(b)(1) (2018) ("[B]efore publishing proposed regulations in the Federal Register, the Secretary shall prepare draft regulations implementing this title [i.e., Title IV of the Higher Education Act] and shall submit such regulations to a negotiated rulemaking process."). It is not clear whether negotiated rulemaking increases or decreases the burden imposed by notice and comment. See, e.g., David Thaw, *Enlightened Regulatory Capture*, 80 WASH. L. REV. 329, 338 (2014) ("Scholars are split over whether the consensual regulatory responses, such as negotiated rulemaking, were ever effective in addressing the problems of the 1980s.").

155. See *infra* notes 159–63 and accompanying text.

156. Such considerations include the flexibility of acting through guidance and the potentially better engagement resulting from notice-and-comment rulemaking. See *infra* Section III.C.5.

157. See *supra* Section II.B.1.

158. 34 C.F.R. § 674.49(c)(5)(i) (2019).

159. See *infra* Section III.C.

160. See *infra* Section III.B.4.

third of the loan balance.<sup>161</sup> It seemingly leaves no room for non-undue-hardship grounds for discharge.

To advance the purposes of the student loan programs, the Department should engage in notice-and-comment rulemaking and repeal the Perkins program's "shall oppose" requirement.<sup>162</sup> The Department should also reverse its guidance applying that requirement to the other two programs.<sup>163</sup> Indeed, the Department should take the latter step even if it determines that notice-and-comment rulemaking for the relatively small<sup>164</sup> Perkins program is too burdensome.

### C. On Predictable Rules

The Department's regulations in many cases reserve broad—in some cases, unlimited—discretion to loan holders in deciding whether to consent to discharge.<sup>165</sup> FFELP guaranty agencies in particular gained steadily more discretion as the regulations evolved.<sup>166</sup> Although the 2015 Dear Colleague Letter structures the exercise of discretion,<sup>167</sup> considerable scope remains for nontransparent, unpredictable decision making.

#### 1. The Rules Have Reserved Broad, Unpredictably Exercised Discretion to Loan Holders

The gaps in the regulations described above may confer discretion on loan holders. Because there are no explicit instructions about what to do if undue hardship is present,<sup>168</sup> perhaps the regulations permit holders to decide for themselves what to do in this circumstance. For federally held loans, including loans under the giant Ford program, there are no regulations, so the Department may have retained discretion in all circumstances. Indeed, in 1985, the Secretary announced the intention to "exercise the full discretion accorded" under the statute to decide "on a case-by-case basis" whether to pursue collection of loans the Department holds.<sup>169</sup> The Secretary has since given more concrete guidance in the 2015 Dear Colleague Letter, as described in Section II.B.

In addition to any scope for discretion to be found in the regulatory gaps, the regulations affirmatively confer discretion in some areas. Indeed, the FFEL regulations have continually changed to give guaranty agencies more and more discretion. In 1986, the regulations provided that the guaranty agency "shall

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161. *See supra* note 139 and accompanying text.

162. *See supra* note 139 and accompanying text.

163. *See supra* Section II.B.1.

164. As of the end of the first quarter of 2020, the \$5.9 billion in Perkins loans outstanding accounted for less than 0.4% of the federal student loan portfolio. *See* U.S. Dep't of Educ., *supra* note 53.

165. *See infra* Section II.C.1.

166. *See infra* notes 170–73 and accompanying text.

167. *See supra* Section II.B.1.

168. *See supra* notes 130–31 and accompanying text.

169. 1985 GSL PLUS NPRM, *supra* note 104, at 35,966.



diligently contest” discharge.<sup>170</sup> In 1992, the Department amended the regulations so that they affirmatively instructed the guaranty agency to oppose discharge only where undue hardship was absent and opposition was cost-effective.<sup>171</sup> The rules were silent as to what to do in other cases.

In 1999, the Department removed any remaining affirmative requirement to oppose discharge,<sup>172</sup> leaving it unclear what the guaranty agency was supposed to do under any outcome of the analysis it was to perform. In 2001, the Department partially filled this gap with an affirmative grant of discretion. It provided that if undue hardship was absent but discharge opposition was cost-ineffective, the guaranty “may, but need not” oppose discharge.<sup>173</sup> Thus, the FFEL regulations evolved from providing direction in all circumstances to affirmatively granting discretion in one circumstance and being silent in all others.

As discussed, the 2015 Dear Colleague Letter probably prescribes that holders should not oppose discharge when undue hardship is present.<sup>174</sup> When undue hardship is absent, the letter requires holders to oppose discharge if the costs of doing so are less than one-third of the amount outstanding on the loan and provides that holders “may” oppose discharge if the costs of doing so are above the one-third threshold.<sup>175</sup> The letter thus cabins holders’ discretion somewhat by filling the outright gaps in the regulations, although it does so only as a guidance document.

However, the 2015 Dear Colleague Letter does not, and cannot,<sup>176</sup> supersede the FFEL regulations’ affirmative grant of discretion in one important scenario: where undue hardship is absent but opposing discharge is cost-ineffective. Indeed, the letter extends the grant of discretion in this case beyond the FFEL program. Under the letter, Perkins and Ford loan holders enjoy the same flexibility that the regulations confer on FFEL holders.<sup>177</sup>

Perhaps more importantly, the decisions the letter and regulations require holders to make involve discretion and are not transparent to borrowers. As the letter points out, the undue hardship determinations the letter requires in its first step of analysis<sup>178</sup> “often are difficult and require the exercise of judgment by the holder.”<sup>179</sup> In the second step, the letter requires estimates of litigation cost,<sup>180</sup> which are themselves

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170. 1986 GSL PLUS Final Regulations, *supra* note 100, at 40,905.

171. 1992 FFEL Rules, *supra* note 101, at 60,349.

172. *See* 1999 FFEL Ford Final Rules, *supra* note 102, at 58,960–61 (omitting any requirement to do anything in particular based on outcome of two-step analysis). As discussed, the guaranty agency may have been under an unqualified duty to use due diligence to oppose discharge at this point, but that reading is probably incorrect. *See supra* Section II.B.1

173. 2001 FFEL Ford Final Rules, *supra* note 103, at 34,762.

174. *See supra* Section II.B.1.

175. *See supra* Section I.C.

176. A guidance document may not amend regulations adopted through notice-and-comment rulemaking. “[A]n amendment to a legislative rule must itself be legislative.” *Am. Mining Cong. v. Mine Safety & Health Admin.*, 995 F.2d 1106, 1109 (D.C. Cir. 1993) (quoting *Nat’l Family Planning & Reprod. Health Ass’n v. Sullivan*, 979 F.2d 227, 235 (D.C. Cir. 1992)).

177. 2015 Dear Colleague Letter, *supra* note 22, at 3–4.

178. *See supra* Section I.C.

179. 2015 Dear Colleague Letter, *supra* note 22, at 4.

180. *See supra* Section I.C.

subjective and debatable. Thus, holders continue to enjoy a great deal of freedom of action, and borrowers have correspondingly little concrete guidance.

## 2. The Department Should Alleviate Borrower Uncertainty by Creating Safe Harbors

The Bankruptcy Code's undue-hardship provision reflects a view—well-founded or not—that some debtors do not deserve bankruptcy's fresh start.<sup>181</sup> However, as Professors Rafael Pardo and Michelle Lacey demonstrated in a study published in 2009,<sup>182</sup> the provision impinges on the debtor's fresh start and access to justice in a way that goes beyond what underlying policy justifies.<sup>183</sup> It does so with respect to both substance and procedure: courts apply the undue-hardship standard inconsistently and because litigating undue hardship is costly.<sup>184</sup> By adopting judicially defined undue hardship as the sole substantive basis for consent to discharge, the Department seemingly imports into its decisions the geographic inconsistency of judicial opinions in this area.<sup>185</sup> The Department could go a long way toward remedying both the substantive and the procedural problems by adopting "safe harbors," that is, objectively defining classes of debtors whose claims of dischargeability the Department will not contest.

The substantive problem Pardo and Lacey mention is that the undue-hardship standard is applied inconsistently, so that the litigation process produces "noise rather than clarity."<sup>186</sup> It is notoriously difficult to predict how a bankruptcy court will rule in an undue-hardship proceeding.<sup>187</sup> The unpredictability of success could cause a decrease in the likelihood of settlement, increasing the likelihood that creditors use superior resources to wear debtors down in a "war of attrition."<sup>188</sup> It could make debtors less likely to press valid claims for relief because success is uncertain.<sup>189</sup> And theoretically it could also make debtors more likely to press invalid claims because failure is uncertain.

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181. See Hunt, *supra* note 122, at 1302–07 (demonstrating Section 523(a)(8)'s origin in concerns that some student borrowers were abusing the system).

182. Pardo & Lacey, *The Real Student-Loan Scandal*, *supra* note 50.

183. See *id.* at 182–83. Pardo and Lacey had previously demonstrated empirically that the substantive standard is inconsistently applied. See Pardo & Lacey, *Undue Hardship in the Bankruptcy Courts*, *supra* note 9, at 479–80.

184. See Pardo & Lacey, *The Real Student-Loan Scandal*, *supra* note 50, at 183.

185. See 2015 Dear Colleague Letter, *supra* note 22, at 3 (noting adoption of different tests for undue hardship in different judicial circuits).

186. See Pardo & Lacey, *The Real Student-Loan Scandal*, *supra* note 50, at 190.

187. See Pardo & Lacey, *Undue Hardship in the Bankruptcy Courts*, *supra* note 9, at 479–80 ("[W]hat has proven to be most troublesome regarding application of the law has not been the infrequency with which relief has been granted, but rather the haphazard fashion in which courts have determined whether a debtor's circumstances support a claim of undue hardship that warrants forgiveness of educational debt.")

188. See Pardo, *The Undue Hardship Thicket*, *supra* note 8, at 2109–10, 2146.

189. Compare Pardo & Lacey, *The Real Student-Loan Scandal*, *supra* note 50, at 191 ("[I]nconsistency of the doctrine gives . . . creditors room to maneuver and argue that a debtor should not prevail . . . Perhaps, then, some of the most sympathetic cases of undue hardship fail to wend their way through the court system.")

Although one familiar with law's rules-standards debate might be inclined to dismiss the unpredictability as a necessary cost of making a nuanced, context-sensitive determination of undue hardship,<sup>190</sup> Pardo and Lacey's study suggests that the uncertainty here is pernicious: factors other than the merits of the debtor's case drive outcomes.<sup>191</sup> A borrower might get some guidance from a lawyer's or the borrower's own legal research on the peculiarities of the relevant jurisdiction. However, financially strapped debtors may lack the money to fund legal research, which in any event might not be illuminating.

That lack of money is relevant to the procedural problem Pardo and Lacey identify, which is that it is expensive and difficult to seek an undue-hardship discharge. The borrower must bring an adversary proceeding<sup>192</sup>—essentially a separate civil action within the bankruptcy<sup>193</sup>—in order to find out if the undue-hardship claim will prevail. In such a proceeding, the borrower bears both the burden of proof of undue hardship<sup>194</sup> and the cost of funding the action.<sup>195</sup> Financially distressed debtors may not be able to finance the effort.<sup>196</sup>

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190. On the rules-standards debate, see Louis Kaplow, *Rules Versus Standards: An Economic Analysis*, 42 DUKE L.J. 557 (1992); Kathleen M. Sullivan, *The Justices of Rules and Standards*, 106 HARV. L. REV. 22 (1992).

191. See, e.g., Pardo & Lacey, *Undue Hardship in the Bankruptcy Courts*, *supra* note 9, at 480 (“[W]hat has proved to be most troublesome regarding application of the law has not been the infrequency with which relief has been granted, but rather the haphazard fashion in which courts have determined whether a debtor’s circumstances support a claim of undue hardship.”). In a subsequent study, Pardo and Lacey found that “the identity of the judge assigned to the adversary proceeding is associated with the extent of discharge,” highlighting the ex ante unpredictability of the undue-hardship standard. Pardo & Lacey, *The Real Student-Loan Scandal*, *supra* note 50, at 234.

192. FED. R. BANKR. P. 7001(6) (“The following are adversary proceedings . . . (6) a proceeding to determine the dischargeability of a debt.”); *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260, 272 (2010) (referring to “the requirement that a bankruptcy court make this finding [i.e., a finding of undue hardship] in an adversary proceeding”).

193. See 6A BANKRUPTCY SERVICE LAWYER’S EDITION § 57:11 (2018) (“[A]n ‘adversary proceeding’ is essentially indistinguishable from a civil action . . .”).

194. See, e.g., *United States v. Wood*, 925 F.2d 1580, 1583 (7th Cir. 1991). The creditor bears the initial burden of establishing that the debt exists and is covered by the undue-hardship provision. The burden then shifts to the debtor to demonstrate undue hardship. See Pardo, *The Undue Hardship Thicket*, *supra* note 8, at 2110. Pardo argues that under prevailing doctrine, the creditor has a “much easier evidentiary showing.” *Id.* at 2113. See generally *id.* at 2113–21.

195. See Pardo & Lacey, *The Real Student-Loan Scandal*, *supra* note 50, at 183 (“Debtors who have filed for bankruptcy in the first instance as a result of financial distress must somehow find the resources to litigate a full-blown lawsuit in order to prove that their predicament qualifies them for relief from their student loans.”).

196. See Pardo, *The Undue Hardship Thicket*, *supra* note 8, at 2112 (“[T]he consumer bankruptcy bar has emphasized that many debtors do not have the financial wherewithal to litigate an undue hardship adversary proceeding.”); Pardo & Lacey, *The Real Student-Loan Scandal*, *supra* note 50, at 186 (“A debtor who has filed for bankruptcy as a result of financial distress generally will not be well positioned to expend resources to litigate a dispute relating to his or her prebankruptcy debts.”).

The Department could alleviate the uncertainty facing borrowers by clearly stating certain circumstances under which it will oppose or not oppose discharge. Currently, however, it misses this opportunity. The rules specified in the 2015 Dear Colleague Letter track the judicial interpretations of the undue-hardship standard and thus incorporate the unpredictability those interpretations create.<sup>197</sup> Moreover, as discussed, they confer broad, nontransparently exercised discretion on holders.<sup>198</sup>

To reduce the uncertainty arising from inconsistent judicial application of the undue-hardship standard, the Department could create “safe harbors,” “exposed outcroppings,”<sup>199</sup> or both. A safe harbor would be a set of circumstances in which the loan holder will not oppose discharge. An “exposed outcropping” would be a set of circumstances in which the loan holder definitely will oppose discharge. The term is the author’s effort to coin an opposite to “safe harbors.”

As between safe harbors and exposed outcroppings, safe harbors are probably more urgently needed because meritorious claims of undue hardship that are not asserted are probably a bigger problem than meritless claims that are asserted. The fact that as few as 0.187% of bankrupt student loan debtors seek relief, combined with a success rate that may be well over 50% when borrowers do seek relief,<sup>200</sup> strongly suggests that borrowers with meritorious claims are not bringing them. In defending the student loan nondischargeability provision in 1978, Representative John Erlenborn of Illinois responded to what he called the “very persuasive” argument of Representative Caldwell Butler of Virginia that some students would need bankruptcy.<sup>201</sup> Erlenborn argued, “[I]f there is true hardship, the loan can be discharged.”<sup>202</sup> Erlenborn’s promise seems empty if only 0.187%<sup>203</sup> of bankrupt student loan debtors even try to discharge their loans.

A safe harbor seems likely to induce debtors to assert claims of undue hardship that they otherwise would not pursue because they would not face uncertainty and expense for pursuing an undue-hardship claim within the safe harbor.<sup>204</sup> Assuming that the safe harbors would be designed so that the claims they cover are predominantly meritorious ones, inducing debtors to use the safe harbors would be a good thing.<sup>205</sup>

Moreover, establishing a safe-harbor rule may lead to better decisions about which debtor claims of undue hardship to oppose. Because the Department would

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197. See 2015 Dear Colleague Letter, *supra* note 22, at 1–2 (“[A] holder must . . . determine whether . . . repayment would constitute an undue hardship according to the legal standards set by the Federal courts.”).

198. See *supra* Section II.C.1.

199. The author, unable to find a term for the opposite of “safe harbor,” offers this one.

200. See *supra* Section II.A.2.

201. 124 CONG. REC. 1797 (1978) (statement of Rep. Butler).

202. *Id.* (statement of Rep. Erlenborn).

203. See *supra* note 119.

204. See Jiménez et al., *supra* note 16, at 115 (“The dual aims of our clear-cut [safe-harbor] procedures are to encourage individuals suffering undue hardship to seek a discharge and to avoid the need for an attorney.”).

205. Conversely, to the extent debtors are currently initiating meritless undue-hardship proceedings because they are hoping not to be opposed, an “exposed outcropping” might deter that practice.

craft the safe harbors outside the adversarial context of bankruptcy litigation, it would avoid certain factors that might motivate holders to fight discharge even where it is warranted. Such factors include the desire of Justice Department lawyers to notch wins in cases they litigate<sup>206</sup> and the inclination, suggested by Pardo and Lacey, of more powerful creditors to wage “wars of attrition,” rather than seeming to acquiesce when challenged.<sup>207</sup>

The BFGJO group has proposed just such a safe-harbor rule, suggesting that the Department consent to discharge in nine specifically defined sets of circumstances.<sup>208</sup> For example, the Department would not oppose discharge if the borrower’s income is currently below 150% of the poverty level and the borrower receives Social Security disability benefits,<sup>209</sup> or if the borrower has had an income below the federal poverty level for the last four years.<sup>210</sup> This author supports the BFGJO group’s proposal and notes that additional safe harbors may also be justified. For example, a companion article considers whether and when the Department should consent to discharge for debtors whose debt-to-income ratio exceeds a prescribed level.<sup>211</sup>

The Department’s website currently states that the Department does not provide “specific guidance related to settlements and compromises” because providing such information “is not in the best interest of the government as it could enable borrowers to reduce their repayments below the amount they can legitimately afford.”<sup>212</sup> This Article argues against a purely pecuniary definition of the government’s interest when it comes to student loan repayment.<sup>213</sup> Moreover, the concern expressed on the website may not apply to many suggestions to provide borrowers guidance regarding bankruptcy. For example, take the just-mentioned BFGJO group proposal. It seems unlikely that the prospect of a bankruptcy discharge will induce many people to live in poverty for four years or reduce their income to less than 150% of the poverty level and become disabled.

Although objectively defined safe harbors should be an important part of Department discharge consent policy, they should not be the only grounds for consent. The goals of the student loan programs and Bankruptcy Code may require the Department to consider circumstances that do not easily lend themselves to objective definition and easy documentation. For example, a companion paper argues that a borrower should not be barred from getting a discharge just because the borrower could leave lower-paid work using their education for higher-paid work

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206. See Neal Devins & Michael Herz, *The Uneasy Case for Department of Justice Control of Federal Litigation*, 5 U. PA. J. CONST. L. 558, 588 (2003).

207. See Pardo & Lacey, *The Real Student-Loan Scandal*, *supra* note 50, at 191–92.

208. See Bruckner et al., *supra* note 18, at 190–91; Jiménez et al., *supra* note 16, at 115.

209. See Bruckner et al., *supra* note 18, at 190–91; Jiménez et al., *supra* note 16, at 115 (describing similar proposal based on eligibility for, rather than receipt of, benefits).

210. See Bruckner et al., *supra* note 18, at 190; Jiménez et al., *supra* note 16, at 115 (describing similar proposal based on five years of living in poverty).

211. See Hunt, *supra* note 33, at 775–78.

212. U.S. Dep’t of Educ., *Loan Servicing and Collection—Frequently Asked Questions*, SETC-Q1, FED. STUDENT AID, <https://ifap.ed.gov/loan-servicing-and-collection-frequently-asked-questions#SETC-Q1> [<https://perma.cc/EG6L-NBQC>].

213. See *infra* Section III.B.1.

that does not use the education.<sup>214</sup> This circumstance may not be proven as conclusively with standard documents as income and disability eligibility, but the Department should be willing to consider it in deciding whether to consent to discharge.

The Department could implement safe harbors in different ways. The BFGJO group has suggested that the Department do so through creating a rebuttable presumption of undue hardship in certain circumstances.<sup>215</sup> This Article suggests adding grounds for consent to discharge other than undue hardship, as described in the Part III.

### III. “SUBSTANTIVE” OBSERVATIONS AND RECOMMENDATIONS: LIBERALIZING DISCHARGE CONSENT POLICY

Part III offers observations and recommendations that go to the heart of the Department’s discharge policy: they address how freely the Department should consent to discharge. The Department has treated discharge consent largely, if not entirely, as a problem of debt collection.<sup>216</sup> That should change. The Department’s policy should reflect the fact that the Department is running an educational benefit program, not a bank. The discharge consent rules should reflect statutory purposes of the student loan program that go beyond debt collection. The Department can and should further these purposes by consenting to discharge on bases other than undue hardship.

#### A. *The Rules Have Treated Consent to Discharge as a Debt Collection Issue*

The underlying goal of the Department’s bankruptcy discharge opposition policy to date appears to have been cost-effective collection of loans. The 2015 Dear Colleague Letter seems to instruct holders to oppose discharge whenever it is cost-effective to do so, unless the holder reaches the “clear conclusion” that repayment would work undue hardship.<sup>217</sup>

The explanations the Department has given for its discharge opposition regulations, scant as they are, focus on pecuniary considerations. The 1987 Perkins rules, which contain the closest thing to an explanation of the Department’s bankruptcy-discharge policy to be found in the regulatory history, mention “the weight to be given to the cost of litigation”<sup>218</sup> and justify the decision to regulate discharge opposition on the ground that institutions were permitted “to charge to the [Perkins] Fund the costs of the litigation required in bankruptcy.”<sup>219</sup> Other aspects of the regulatory history evidence a policy in favor of collection where it is cost-effective, although this is expressed obliquely.<sup>220</sup>

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214. See Hunt, *supra* note 33, at 773–75.

215. See Bruckner et al., *supra* note 18, at 244; Jiménez et al., *supra* note 16, at 115.

216. See *infra* Section III.A.

217. 2015 Dear Colleague Letter, *supra* note 22, at 10–11.

218. 1987 Perkins Rules, *supra* note 97, at 45,555.

219. *Id.*

220. The 1990 GSL NPRM references a policy of “reduc[ing] defaults and increas[ing] collections on loans that do go into default.” 1990 GSL NPRM, *supra* note 112, at 48,324.

The Department apparently has treated undue hardship as a constraint on its ability to collect, rather than as something to be avoided for its own sake. The 2015 Dear Colleague Letter instructs holders to consent to discharge where undue hardship is “clear[ly]” present.<sup>221</sup> And despite language about “balanc[ing]” collection and undue hardship,<sup>222</sup> the letter states that the decision whether undue hardship is present “would necessarily” be made according to the standards the judiciary has devised for proving undue hardship in court.<sup>223</sup> In other words, the letter instructs holders to consent to discharge based on undue hardship only when they clearly would lose in court anyway.

*B. The Department Should Advance the Goals of the Student Loan Programs by Adopting a More Generous Discharge Consent Policy*

Section III.B.1 argues that the Department should take account of all relevant purposes of the student loan programs in setting discharge policy. Section III.B.2 argues that the Department has failed to do that because it has adopted “undue hardship,” as defined by the courts, as the sole substantive basis for consent to discharge.

Sections III.B.3 and III.B.4 consider how the Department could go about liberalizing its policy. Section III.B.3 considers the possibility that the Department could act by adopting a broader definition of “undue hardship,” and concludes that that is a risky path. Section III.B.4 argues that the Department should consider providing for consent to discharge on bases other than “undue hardship,” and gives three examples of possible bases the Department could add.

1. The Department Should Take Account of All Relevant Purposes of the Student Loan Programs in Setting Discharge Policy

To be sure, debt collection in general and nondischargeability in particular serve goals Congress specifically articulated: protecting the loan programs from financial

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This formulation that may have been intended to embrace borrower bankruptcies, although these apparently generally are not defaults. *See supra* Section II.A.1. A policy in favor of debt collection may be implicit in the regulations themselves. The Perkins regulations provide that the institution “shall oppose discharge” if undue hardship is absent and collection costs are less than one-third of the loan balance. 34 C.F.R. § 674.49(c)(5)(i) (2019). The FFEL regulations do not have a comparable bankruptcy-specific provision, but they do provide that the guaranty agency must use due diligence up until discharge in order to receive payment on its claim against the government resulting from discharge. *See id.* § 682.402(k)(2)(v); *see also id.* § 674.41(a) (stating that, in Perkins program, institution is to “exercise due diligence in collecting loans”).

221. *See* 2015 Dear Colleague Letter, *supra* note 22, at 11.

222. *Id.* at 1 (explaining that holders must “balance their obligation to collect debts with judging whether the repayment of loans would constitute an undue hardship to borrowers in the bankruptcy discharge process”); *see also id.* at 10 (stating that letter is “to assist loan holders in fulfilling their regulatory duty to protect the integrity of taxpayer dollars provided through student loans while consenting to and/or not opposing the undue hardship discharge petition of a student loan borrower where appropriate”).

223. *See id.* at 3.

loss and combating borrower bad faith.<sup>224</sup> But the student loan program has other purposes as well. They include promoting access to higher education regardless of wealth,<sup>225</sup> providing students freedom in choosing careers,<sup>226</sup> producing an educated population for the benefit of the country,<sup>227</sup> and benefiting students.<sup>228</sup> Scholars have noted some of these objectives.<sup>229</sup>

As developed more fully in a companion paper,<sup>230</sup> broad nondischargeability of student debt can interfere with accomplishing all of the goals just mentioned. Economically disadvantaged students who do not pursue higher education for fear of

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224. See Hunt, *supra* note 122, at 1310–11 (discussing purposes of student-loan nondischargeability).

225. See, e.g., *Hearings Before the Special Comm. on Educ. of the H. Comm. on Educ. & Labor on H.R. 3220*, 89th Cong. 48 (1965) (testimony of Francis Keppel, Comm’r of Education, Dep’t of Health, Educ., & Welfare) (“On the question of priorities . . . the first order of business . . . is to assure the opportunity for the children from families with low incomes to go on to higher education. That is Priority No. 1.”).

226. See, e.g., 153 CONG. REC. H. 7,554 (2007) (statement of Rep. Miller) (stating that changes to student-loan program “say[] to those individuals who are fully qualified to go to college, we will not deny you access . . . to the career of your choice[] . . . because you can’t afford to pay for it”).

227. See, e.g., S. REP. NO. 89-673, as reprinted in 1965 U.S.C.C.A.N. 4027, 4053 (1965) (identifying as reasons for Title IV the “continuing shortage of trained, educated persons in many areas” and the “present and future shortage of competent, well-trained professional and technical personnel[]”).

228. See, e.g., Lyndon B. Johnson, *Recorded Remarks on the Message on Education*, AM. PRESIDENCY PROJECT (Jan. 12, 1965), <https://www.presidency.ucsb.edu/documents/recorded-remarks-the-message-education> [<https://perma.cc/L8FL-SSCQ>] (“Every child must be encouraged to get as much education as he has the ability to take. We want this for his sake, and we want this for the country’s sake.”).

229. Professor Abbye Atkinson has found that the legislative history of the programs indicates that the programs’ goals include making education financially accessible and benefiting the country through educating the population. See Atkinson, *supra* note 32, at 12–13. She also argues that student-loan policy should not, in a way that tracks racial or socioeconomic differences, discourage people from pursuing careers requiring education. *Id.* at 25. Professor Jonathan Glater has emphasized that “[i]n the 1960s, lawmakers sought to promote access to higher education for an unprecedented number of young Americans.” Jonathan D. Glater, *The Other Big Test: Why Congress Should Allow College Students to Borrow More Through Federal Aid Programs*, 14 N.Y.U. J. LEGIS. & PUB. POL’Y 11, 36 (2011); see also *id.* at 35–38 (substantiating Glater’s claim about access). Professor Michael Simkovic has asserted that “government support for higher education has primarily been driven by economic considerations, particularly during the mid-twentieth century when Federal Student Loan programs were established.” Michael Simkovic, *Risk-Based Student Loans*, 70 WASH. & LEE L. REV. 527, 531 (2013). Atkinson’s and Glater’s work call this assertion into question. Notably, Simkovic acknowledges that “in approving subsequent [i.e., post-1958] federal student loan programs, such as the guaranteed loan program established by the Higher Education Act of 1965, Congress emphasized the need for greater equality of opportunity and social mobility as well as the need for a skilled labor force.” *Id.* at 550. A companion article by this author discusses the purposes of the Higher Education Act more fully. See Hunt, *supra* note 33, at 732–42.

230. See Hunt, *supra* note 33, at 742–62.



taking on nondischargeable debt do not have equal access to education.<sup>231</sup> A graduate who does not embark on a lower-paying but valuable career because of fear of nondischargeability does not have free career choice.<sup>232</sup> Graduates who cannot work in the fields for which they have been trained because their debt is nondischargeable are not fully using their learning for the good of the nation.<sup>233</sup> And loans may harm, rather than help, borrowers who cannot find work after leaving higher education and suffer hardship that is not “undue” under prevailing judicial interpretations.<sup>234</sup> Thus, to respect all purposes of the student loan programs, policy must balance how nondischargeability frustrates some goals of the student loan programs even as it advances others.

The Department should balance the dischargeability-favoring and dischargeability-disfavoring goals of the programs in regulating, for its charge is to regulate to advance the purposes—plural—of the federal student loan programs. For the FFELP, Congress was quite explicit in expressing this intention. The Higher Education Act provides that the Secretary may issue “such regulations as may be necessary to carry out the purposes of this part,”<sup>235</sup> referring to the part of the Act that authorizes the FFELP. Similarly, the Department issued the critical 1987 Perkins regulations under a provision instructing it to act “to promote the purposes” of the program.<sup>236</sup> Although there is no directly parallel provision for the Ford

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231. See Rick Seltzer, *Antidote to Med Student Debt*, INSIDE HIGHER ED (Aug. 17, 2018), <https://www.insidehighered.com/news/2018/08/17/nyu-scholarships-cover-medical-school-tuition-doctors-debt-continues-raise-concern> [<https://perma.cc/2HWD-6Z5Q>] (“High costs have for years stoked concerns about how debt affects aspiring doctors. Leaders worry some of the best and the brightest students, particularly those from poor and immigrant communities, are dissuaded from attending medical school at all.”). Although the reference here is to debt in general rather than to nondischargeability, other scholars have posited that nondischargeability might discourage students from pursuing higher education. See Atkinson, *supra* note 32, at 1, 12 (“For potential borrowers, this burden [i.e., the burden of nondischargeable debt] may deter members of this group from seeking an education if, in doing so, they must make themselves more vulnerable financially.”).

232. See Jesse Rothstein & Cecilia Elena Rouse, *Constrained After College: Student Loans and Early-Career Occupational Choices*, 95 J. PUB. ECON. 149, 149 (2011) (“[D]ebt causes graduates to choose substantially higher-salary jobs and reduces the probability that students choose low-paid ‘public interest’ jobs.”). Again, the connection is to debt generally, but it is reasonable to suppose that nondischargeability stokes debt fears.

233. See Dep’t of Educ. v. Gerhardt (*In re Gerhardt*), 348 F.3d 89, 93 (5th Cir. 2006) (“[N]othing in the Bankruptcy Code suggests that a debtor may choose to work only in the field in which he was trained, obtain a low-paying job, and then claim that it would be an undue hardship to repay his student loans.”).

234. *Brunner v. N.Y. State Higher Educ. Servs. Corp.* (*In re Brunner*), 46 B.R. 752, 753 (S.D.N.Y. 1985), *aff’d*, *Brunner v. N.Y. State Higher Educ. Servs. Corp.*, 831 F.2d 395 (2d Cir. 1987) (“The existence of the adjective ‘undue’ indicates that Congress viewed garden-variety hardship as insufficient excuse for a discharge of student loans . . .”).

235. 20 U.S.C. § 1082(a)(1) (2018).

236. See 1987 Perkins Rules, *supra* note 97, at 45,561 (citing 20 U.S.C. § 424 as basis for rules). Section 424 of the Education Code is the codification of Section 204 of the National Defense Education Act. Compare National Defense Education Act (NDEA), Pub. L. 85-864, § 204, 72 Stat. 1580, 1584 (1958) (codified at 20 U.S.C. § 424 (2012)), with Pub. L. 88-665, § 204, 78 Stat. 1100, 1101 (1964). Section 204 in turn directs the Secretary to “include such

program instructing the Secretary to regulate to promote statutory purposes, it would be strange if Congress intended the Secretary to regulate in light of all the purposes of the FFELP and Perkins programs, but not those of the Ford program.

Other provisions direct the Secretary to regulate specific aspects of the FFELP federal insurance program,<sup>237</sup> FFELP guaranty-agency program,<sup>238</sup> Perkins program,<sup>239</sup> and Ford program<sup>240</sup> according to the overall purposes of those programs. The District Court for the District of Columbia recently upheld the Department's gainful-employment rule for institutional eligibility for student loan funds, in part because the rule "advance[d] the purposes of . . . the Higher Education Act and Title IV."<sup>241</sup>

More generally, administrative agencies are to advance statutory purpose, where the purpose is discernible. As the Court of Appeals for the D.C. Circuit recently held, the courts owe deference to an agency's interpretation of an ambiguous statute "if it

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other provisions as may be necessary to protect the financial interest of the United States and promote the purposes of this title." NDEA, § 204(5), 72 Stat. at 1584.

237. See 20 U.S.C. § 1075(a)(1)(B) (2018) (Secretary can create exceptions to statutory loan limits if she "determines, pursuant to regulations, that a higher amount is warranted in order to carry out the purposes of this part"); *id.* § 1082(a)(3) (regulating as "Secretary determines to be necessary to assure that the purposes of this part will be achieved"); *id.* § 1079(b)(1) (Secretary may grant lender comprehensive insurance coverage certificate under "[s]uch requirements . . . as in the Secretary's judgment will best achieve the purpose of this subsection while protecting the United States from the risk of unreasonable loss and promoting the objectives of this part").

238. See *id.* § 1078(a)(3)(A)(v) (2012) (Secretary may make certain payments if state law "threatens to impede the carrying out of the functions of this part"); *id.* § 1078(b)(2)(B) (program agreement to "include such other provisions as may be necessary to protect the United States from the risk of unreasonable loss and promote the purposes of this part"); *id.* § 1078(c)(2)(I) (program agreements "may include such other provisions as may be necessary to promote the purpose of this part"); *id.* § 1078-1(b)(2)(A)(viii) (program agreements may include reporting requirements "as the Secretary may require to carry out the purposes of the programs under this title"); *id.* § 1078-1(b)(2)(G) (program agreements may include "such . . . provisions as the Secretary may determine to be necessary to protect the United States from the risk of unreasonable loss and to promote the purposes of this part"); *id.* § 1078-8(d)(2)(A) (permissible exception to loan limits "where the Secretary determines that a higher amount is warranted in order to carry out the purpose of this part").

239. See *id.* § 1087cc(a)(1) (agreement with institution under Perkins program "shall provide for the establishment and maintenance of a student loan fund for the purposes of this part").

240. See *id.* § 1087c(b)(2)(F) (institution may be approved to originate Ford loans only if it meets "such . . . criteria as the Secretary may establish to protect the financial interest of the United States and to promote the purposes of this part."); *id.* § 1087d(a)(6) (Ford program participation agreement shall "include such . . . provisions as the Secretary determines are necessary to protect the interests of the United States and to promote the purposes of this part"); *id.* § 1087f(a)(2) (giving special consideration to certain state agencies in awarding servicing contracts "to the extent practicable and consistent with the purposes of this part").

241. *Ass'n of Private Sector Colls. & Univs. v. Duncan*, 110 F. Supp. 3d 176, 199 (D.D.C. 2015), *aff'd*, 640 F. App'x 5 (D.C. Cir. 2016); see also *id.* at 201 ("[F]ederal law also gives the Department the power to 'carry out' programs like Title IV.')

is reasonable and consistent with the statute's purpose."<sup>242</sup> Courts routinely cite consistency with statutory purpose as a reason to uphold agency action.<sup>243</sup> And scholars have affirmed that agencies generally should regulate to promote statutory purpose. Professor Kevin Stack has put it quite forcefully: "The core obligation" of administrative agencies is to "evaluate alternatives, justify their choices, and act to further the goals, aims, and principles—the purposes—their authorizing statutes establish."<sup>244</sup>

## 2. By Specifying Judicially Defined "Undue Hardship" as the Only Substantive Basis for Discharge, the Department Ignores Critical Purposes of the Loan Programs

The Department has adopted "undue hardship" as the only ground other than cost-effectiveness for consenting to discharge.<sup>245</sup> Thus, one could say that undue hardship is the only substantive ground for consent. The Department has said that the meaning of this term in its regulations and policies "would necessarily" track the courts' interpretation of the phrase in section 523(a)(8) of the Bankruptcy Code.<sup>246</sup>

The judicial tests for undue hardship upon which the Department relies ignore the discharge-favoring goals of the student loan programs that were just discussed. The leading test, the *Brunner* test, focuses instead on the borrower's inability to maintain a minimal standard of living while repaying loans, the likely persistence of that condition, and the borrower's good-faith efforts to repay.<sup>247</sup> Neither *Brunner* nor the appellate decisions that adopt its test considered how a stingy undue-hardship standard could interfere with achieving the dischargeability-favoring purposes of the

242. *UC Health v. NLRB*, 803 F.3d 669, 675 (D.C. Cir. 2015); *see also* *Atl. City Elec. Co. v. F.E.R.C.*, 295 F.3d 1, 8–9 (D.C. Cir. 2002) ("The agency's interpretation of the statute is entitled to deference only if it is 'reasonable and consistent with the statute's purpose.'" (quoting *Indep. Ins. Agents of Am., Inc. v. Hawke*, 211 F.3d 638, 643 (D.C. Cir. 2000))).

243. *See, e.g., Fed. Exp. Corp. v. Holowecki*, 552 U.S. 389, 402–03 (2008) (upholding EEOC's definition of a "charge" on grounds that "the agency's proposed test implements . . . the purposes of the [Age Discrimination in Employment] Act"); *Catskill Mtns. Chapter of Trout Unltd. v. EPA*, 846 F.3d 492, 524 (2d Cir. 2017), *cert. denied sub nom. New York v. EPA*, 138 S. Ct. 1164 (2018) (upholding EPA rule where agency "justified the [r]ule by reference to statutory purpose"); *Duncan*, 110 F. Supp. 3d at 199 (upholding Department student-loan rule in part because it "advance[d] the purposes of . . . the Higher Education Act and Title IV").

244. Kevin M. Stack, *Purposivism in the Executive Branch: How Agencies Interpret Statutes*, 109 *Nw. U. L. Rev.* 871, 888 (2015).

245. *See supra* Section I.C.

246. *See* 2015 Dear Colleague Letter, *supra* note 22, at 3. It is not clear that this must be the case. It seems the Department could give "undue hardship" a different meaning in its own regulations and policies than the phrase has in the statute. However, now that the Department has taken the position that its regulations track the statutory meaning as interpreted by courts, it may be difficult to backtrack. *See, e.g., Christopher v. SmithKline Beecham Corp.*, 567 U.S. 142, 146 (2012) (refusing to defer to changed agency interpretation of its regulations where the change created "unfair surprise").

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

programs.<sup>248</sup> The decisions do not address, for example, whether inability to escape crushing student debts that discourage participation in the economy and society thwart the purposes of bringing the advantages of an educated population to the country, helping students, or fostering career choice.

The minority judicial test for undue hardship, the totality-of-the-circumstances test, is supposedly more expansive than *Brunner*.<sup>249</sup> However, it likewise does not take account of the statutory purposes discussed in Section III.B.1. Instead, the “totality” test’s inclusiveness seems to apply to “micro” factors of the individual debtor’s circumstances, rather than “macro” factors such as the effect of denying discharge on achieving the overall purposes of the student loan programs.<sup>250</sup>

The appellate courts have ignored discharge-favoring purposes of the student loan programs even though they have relied on discharge-disfavoring purposes. Courts repeatedly have invoked the goal of keeping the student loan programs solvent, a purpose supposedly advanced by making discharge difficult.<sup>251</sup> The *Brunner*

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248. *Brunner* adopted its test “for the reasons set forth in the district court’s order.” *Id.* The district court’s opinion, recognizing that promoting access was an “enlightened social policy,” did not consider how a high standard for nondischargeability might interfere with access or other goals of the program. *Brunner v. N.Y. State Higher Educ. Servs. Corp (In re Brunner)*, 46 B.R. 752, 756 (S.D.N.Y. 1985). Subsequent decisions applying *Brunner* cited in the 2015 Dear Colleague Letter have also failed to consider that issue. *See Hedlund v. Ed. Res. Inst.* 718 F.3d 848, 851 (9th Cir. 2013); *Educ. Credit Mgmt. Corp. v. Frushour (In re Frushour)*, 433 F.3d 393, 399–401 (4th Cir. 2005); *Oyler v. Educ. Credit Mgmt. Corp. (In re Oyler)*, 397 F.2d 382, 385 (6th Cir. 2004); *Educ. Credit Mgmt. Corp. v. Polleys*, 356 F.3d 1302, 1306–10 (10th Cir. 2004); *Dep’t of Educ. v. Gerhardt (In re Gerhardt)*, 348 F.3d 89, 91(5th Cir. 2003); *Hemar Ins. Corp. of Am. v. Cox (In re Cox)*, 338 F.3d 1238, 1241–42 (11th Cir. 2003); *In re Roberson*, 999 F.2d 1132, 1135–37 (7th Cir. 1999); *Penn. Higher Educ. Assistance Auth. v. Faish (In re Faish)*, 72 F.3d 298, 304–06 (3d Cir. 1995). The letter cites the *Hedlund* case from the Ninth Circuit, but that court adopted the *Brunner* test in *In re Pena*, 155 F.3d 1108, 1111–12 (9th Cir. 2001). The court did not discuss nondischargeability’s potential interference with the overall goals of the student-loan programs in *Pena*.

249. The “totality of the circumstances” test—as its name suggests—permits consideration of “the unique facts and circumstances that surround each particular bankruptcy.” *Long v. Educ. Credit Mgmt. Corp. (In re Long)*, 322 F.3d 549, 554 (8th Cir. 2003). The Eighth Circuit, the only appellate court to have adopted this test, has described it as “less restrictive” than *Brunner* and as preserving the court’s “inherent discretion.” *Id.* Professor Rafael Pardo found, in a study of 1430 cases filed in 2011 and 2012, no significant difference in rates of debtor success based on the legal test used. *See Pardo, supra* note 120, at 1118, 1141.

250. The “totality” test’s inclusiveness seems to apply to “micro” factors of the individual debtor’s circumstances, rather than “macro” factors such as the effect of denying discharge on achieving the overall purposes of the student loan programs. *See, e.g., Fern v. FedLoan Servicing (In re Fern)*, 563 B.R. 1, 4 (B.A.P. 8th Cir. 2017) (listing nine factors considered under the totality-of-the-circumstances test, all having to do with individual characteristics of the debtor and the debtor’s bankruptcy).

251. *See Frushour*, 433 F.3d at 400 (stating that “heightened” undue hardship standard “protects the integrity of the student-loan program and saves it from fiscal doom” (internal quotation marks and citation omitted)); *Educ. Credit Mgmt. Corp. v. Polleys*, 356 F.3d 1302, 1306 (10th Cir. 2004) (“In enacting § 523(a)(8), Congress was primarily concerned about abusing student debtors and protecting the solvency of student loan programs.”); *Faish*, 72 F.3d at 306 (stating that the *Brunner* test “safeguards the financial integrity of the student loan

decision itself is based almost entirely on legislative history and the court's view of statutory purpose, but the only materials it cites on those points relate to the nondischargeability provision itself taken in isolation. The decision cites nothing relating to the purposes of the student loan programs more broadly.<sup>252</sup>

Courts have ignored overall goals of the student loan programs even though those goals are relevant to a proper interpretation of the statutory term “undue hardship.”<sup>253</sup> Answering the open-ended question what hardship is “undue,” or unjustified,<sup>254</sup> requires weighing the creditor's interest in opposing discharge against the hardship discharge would avert. That analysis in turn requires considering the overall purposes of the student loan programs along with the purposes of the nondischargeability provision, because the statutes in question are related<sup>255</sup> and should be interpreted together to promote the purposes of both enactments.<sup>256</sup> The Supreme Court affirmed this view in considering the Bankruptcy Act together with a related statute. It held that the proper approach is to take, together with the specific clause at issue, “the whole statute (or statutes on the same subject) and the objects and policy of the law . . . and give to it such a construction as will carry into execution the will of the legislature . . . .”<sup>257</sup> Here, the specific clause at issue would be “undue hardship,” which should be interpreted in light of the purposes of related statutes—that is, the purposes of the student loan programs.

Courts may have ignored most of the student loan programs' larger purposes because judges decide individual cases. A court is relatively well positioned to assess an individual debtor's ability to repay and good or bad faith, as the *Brunner* test demands.<sup>258</sup> But courts are less well situated to evaluate how denying discharge in a

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program”).

252. See *Brunner*, 46 B.R. at 753–56. *Brunner* does state that its test “plainly serves the purposes of the guaranteed student loan program[,]” but cites no authority in support of the assertion. *Id.* at 756.

253. See 11 U.S.C. § 523(a)(8) (2018) (requiring “undue hardship” for discharge of educational debt).

254. See, e.g., “*Undue*”, MERRIAMWEBSTER, <https://www.merriam-webster.com/dictionary/undue> [<https://perma.cc/8J59-MXQF>] (defining undue as “exceeding or violating propriety or fitness: excessive”). For further development of the argument that “undue” means “unjustified,” see Hunt, *supra* note 33, at 764 n. 269.

255. Given the overlapping subject matter, the student-loan nondischargeability provision of the Bankruptcy Code, 11 U.S.C. § 523(a)(8) (2018), seems clearly related to the student-loan provisions of the Higher Education Act, 20 U.S.C. §§ 1087aa–1087ii (2018) (Perkins); *id.* §§ 1071 to 1087-2 (FFELP); *id.* § 1087a–1087j (Ford). The relationship is all the closer because the nondischargeability provision has its origin in the 1976 amendments to the Higher Education Act. See Hunt, *supra* note 122, at 1302–04.

256. See 2A NORMAN SINGER & SHAMBIE SINGER, SUTHERLAND STATUTORY CONSTRUCTION § 45:10 (7th ed. 2018) (“[A] full appreciation of any specific enactment requires an examination of all legislation in a particular field.”); see also *id.* § 51:1 (“Other statutes dealing with the same subject as the one being construed, commonly called statutes *in pari materia*, are another extrinsic aid useful in questions of interpretation.”).

257. *Kokoszka v. Belford*, 417 U.S. 642, 650 (1974) (quoting *Brown v. Duchesne*, 60 U.S. (19 How.) 183, 194 (1857)).

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

particular case thwarts larger program goals. For example, a court can hardly determine the extent to which denying discharge in the case before it will discourage other students from pursuing higher education or taking a financial risk on a lower-paying but important career—both of which are outcomes that would undermine the purposes of the student loan programs.<sup>259</sup> Thus, even though these purposes are germane to determining what hardship is “undue,” courts seem unlikely to evaluate them.

Balancing pro-discharge purposes against the need to keep the student loan programs solvent is a task for which agencies such as the Department are particularly well suited relative to courts. As Professor Kevin Stack has argued, when interpreting “statutes with conflicting purposes, or purposes at different levels of generality that are in tension with one another,”<sup>260</sup> agencies “have decisive advantages over courts” because agencies specialize in the statutes they administer and therefore have specialized staff, among other reasons.<sup>261</sup> The student loan programs exhibit such a policy tension. As Professor Abbye Atkinson has stated, “[w]ith one hand, Congress giveth” by encouraging student borrowing, “yet with the other hand Congress taketh away” by restricting bankruptcy discharge.<sup>262</sup>

### 3. It Is Unclear that the Department Could Expand the Definition of “Undue Hardship”

In light of courts’ limitations in giving effect to all statutory objectives and the Department’s potential advantage in balancing contending purposes, the question arises whether the Department could interpret “undue hardship” itself. Perhaps the Department could adopt an interpretation of the phrase that takes all relevant purposes into account and would, presumably, be more generous than judicial interpretations that do not take account of discharge-favoring purposes of the loan programs. For example, consider the proposal that the Department provide for consent to discharge when the debtor is living below the poverty level.<sup>263</sup> Could the Department decree that hardship is automatically “undue” in such a case, disregarding the debtor’s past efforts to repay and thus departing from the *Brunner* standard?

The Department has taken the position that “undue hardship,” as it uses the term, does have the same meaning as “undue hardship” in section 523(a)(8) of the Bankruptcy Code.<sup>264</sup> Thus, the Department has framed the question just posed as one of authority to interpret that statutory provision.

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259. See Hunt, *supra* note 33, at 74–51.

260. Stack, *supra* note 244, at 908.

261. *Id.* at 907.

262. Atkinson, *supra* note 32, at 22; see also *id.* at 4 (noting a “tension between two federal policies with respect to educational attainment”); Pardo & Lacey, *The Real Student-Loan Scandal*, *supra* note 50, at 235 (noting “schizophrenia” of combining a “public-oriented approach to student-loan origination” with a “business-oriented approach to student-loan collection”).

263. See Bruckner et al., *supra* note 18, at 190; Jimenez et al., *supra* note 16, at 115.

264. See *supra* Section III.B.2.

Given the intertwined nature of the undue-hardship provision and the Higher Education Act,<sup>265</sup> the Department could argue that both are part of a statutory scheme it “administers.” It would then seem to follow under *Chevron v. Natural Resources Defense Council* that the Department would be authorized to interpret “undue hardship” and that its interpretation would be entitled to judicial deference.<sup>266</sup> Moreover, the Department would even be authorized to overrule contrary judicial interpretations, as long as the courts have not held that the statute “unambiguously forecloses” the Department’s interpretation.<sup>267</sup>

However, it is far from clear that such an effort on the Department’s part would be successful. The Supreme Court has shown increasing hostility to administrative interpretation.<sup>268</sup> In particular, it has recently declared that authority to administer a particular statute does not entitle an agency to deference in interpreting a separate statute arguably touching on the same subject matter.<sup>269</sup> This would be an obstacle to the Department’s claim of authority to interpret section 523(a)(8), as would the courts’ undisputed role in interpreting the provision.<sup>270</sup> Finally, the Department’s existing disclaimer of authorization to interpret the statutory term “undue hardship”<sup>271</sup> would complicate any effort to take a contrary position now.<sup>272</sup>

Even if the Department would be justified under existing law in claiming deference to a new definition of “undue hardship” that it might craft, the law seems to be developing in a way that does not favor this strategy. Thus, forthrightly

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265. See *supra* Section III.B.2.

266. 467 U.S. 837, 844 (1984) (holding that courts should defer to reasonable agency interpretation of statute agency administers).

267. See *Nat’l Cable & Telecomms. Ass’n v. Brand X Internet Servs.*, 545 U.S. 967, 982–83 (2005).

268. See, e.g., Randy J. Kozel, *Statutory Interpretation, Administrative Deference, and the Law of Stare Decisis*, 97 TEX. L. REV. 1125, 1152–53 (2019) (describing Supreme Court Justices’ expressions of skepticism about existing administrative deference doctrines and the Court’s grant of certiorari to reconsider one such doctrine).

269. See *Epic Sys. Corp. v. Lewis*, 138 S. Ct. 1612, 1629 (2018) (demonstrating a conflict where the National Labor Relations Act (NLRA) and the Federal Arbitration Act (FAA) both arguably addressed whether employers could require employees to enter into arbitration agreements with class waivers, the National Labor Relations Board’s (NLRB) interpretation of the FAA was not entitled to deference although the NLRB unquestionably administered the NLRA).

270. See *Adams Fruit Co. v. Barrett*, 494 U.S. 638, 649–50 (1990) (refusing to defer to administrative interpretation where “Congress has expressly established the judiciary and not [the agency] as the adjudicator”); *Crandon v. United States*, 494 U.S. 152, 177 (1990) (Scalia, J., concurring) (“The law in question, a criminal statute, is not administered by the agency but by the courts.”).

271. See 2015 Dear Colleague Letter, *supra* note 22, at 3 (“Congress has never defined ‘undue hardship’ in the Bankruptcy Code and has not delegated to the Department the authority to do so.”).

272. See, e.g., *Good Samaritan Hosp. v. Shalala*, 508 U.S. 402, 417 (1993) (“An agency interpretation of a relevant provision which conflicts with the agency’s earlier interpretation is entitled to considerably less deference than a consistently held agency view.” (internal quotation marks omitted)).

adopting grounds for consent other than undue hardship<sup>273</sup> or adopting a rebuttable presumption of undue hardship in certain circumstances<sup>274</sup> would seem to be surer paths to liberalizing bankruptcy discharge consent policy than broadening the definition of undue hardship.

#### 4. The Department Should Act to Promote the Programs' Purposes by Adopting Additional Bases for Consent to Discharge

Unguided by statutory purposes that counsel mercy, some courts have applied *Brunner* quite harshly, requiring a “certainty of hopelessness” as a prerequisite for relief.<sup>275</sup> Even where the courts are not so stern as that, their tests focus on the borrower’s previous efforts to repay,<sup>276</sup> even in situations where the overall purposes of the student loan programs would favor consent to discharge regardless of borrower’s repayment efforts. By recognizing grounds for consent to discharge other than undue hardship, the Department can promote the goals of the student loan programs and alleviate harshness at the same time.

For example, take one of the bright-line discharge-consent rules that the BFGJO group has proposed. They recommend that the Department not oppose discharge for low-income debtors who did not receive a degree from the program they attended.<sup>277</sup> Although the Department could adopt a rebuttable presumption of undue hardship in this circumstance as those authors suggest, it could also decide to consent to discharge based on the purposes of the student loan programs. Specifically, opposing discharge in such cases might discourage others from pursuing higher education or preserve student loans that are likely to have harmed students rather than benefiting them. Each of those outcomes would thwart the goals of the student loan programs.<sup>278</sup>

As another example, this author suggests elsewhere that borrower discouragement could be recognized as a basis for discharge.<sup>279</sup> Bankruptcy law generally recognizes

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273. See *infra* Section III.B.4.

274. See Bruckner et al., *supra* note 18, at 244; Jiménez et al., *supra* note 16, at 115. The considerations identified in this paragraph apparently would not apply to the Department’s decision to adopt a rebuttable presumption that certain circumstances amount to undue hardship. The Department in that case would not be advancing its own interpretation of the term but rather finding that particular fact patterns indicate that the relevant existing definition is fulfilled.

275. See Tetzlaff v. Educ. Credit Mgmt. Corp., 794 F.3d 756, 759 (7th Cir. 2015); Spence v. Educ. Credit Mgmt. Corp. (*In re Spence*), 541 F.3d 538, 544 (4th Cir. 2008); Barrett v. Educ. Credit Mgmt. Corp. (*In re Barrett*), 487 F.3d 353, 359 (6th Cir. 2007); Educ. Credit Mgmt. Corp. v. Mosley (*In re Mosley*), 494 F.3d 1320, 1326 (11th Cir. 2007); Brightful v. Pa. Higher Educ. Assistance Auth. (*In re Brightful*), 267 F.3d 324, 328 (3d Cir. 2001).

276. See *Brunner v. N.Y. State Higher Educ. Servs. Corp.*, 831 F.2d 395, 396 (2d Cir. 1987) (stating that an element of *Brunner* test is that debtor “has made” good-faith efforts at repayment); *Fern v. FedLoan Servicing (In re Fern)*, 563 B.R. 1, 4 (B.A.P. 8th Cir. 2017) (holding that “whether the debtor has made payments on the student loan” is a factor in totality-of-the-circumstances test).

277. See Bruckner et al., *supra* note 18, at 190; Jiménez et al., *supra* note 16, at 115 (making similar proposal).

278. See Hunt, *supra* note 33, at 743–47, 758–62.

279. See *id.* at 775–78.



that unmanageable debt induces borrowers to give up in frustration and withdraw from participation in the economy and society.<sup>280</sup> Using discharge to remedy such discouragement could advance the goals of the student loan programs. That is because discouraged borrowers are not providing society the benefit of their education, are not pursuing their career of choice, and quite likely have been harmed, rather than helped, by their loans.<sup>281</sup>

Borrower discouragement may be difficult to measure directly. However, a high debt-to-income ratio is a promising proxy for discouragement.<sup>282</sup> The debt-to-income ratio can be calculated based on information in the debtor's bankruptcy petition.<sup>283</sup> Although more research on the connection between debt-income ratio and worker discouragement is needed,<sup>284</sup> the ratio could be an administrable criterion for consent on the ground of debtor discouragement.

It is possible that a discouraged borrower is also suffering undue hardship. But that is far from certain. Consider an analysis under the leading test, the one articulated in *Brunner*.<sup>285</sup> A borrower who has given up on work because of insurmountable student debt may well have a sub-“minimal” standard of living,<sup>286</sup> and it may be the case that the situation will persist for a significant portion of the repayment period.<sup>287</sup> Moreover, the borrower's past efforts to repay may rise to the level of “good faith” and therefore satisfy the third element of the test.<sup>288</sup> But even if a discouraged borrower enjoys an above-minimal standard of living (perhaps because of family resources) or has made insufficient past efforts to repay to satisfy the prevailing interpretation of “good-faith effort,”<sup>289</sup> the borrower is still discouraged. And that

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280. *See id.* at 753–58.

281. *See id.* at 753.

282. *See id.* at 775–78.

283. Income documents that must be filed with a Chapter 7 petition include (1) a schedule of current income and expenditures, *see* 11 U.S.C. § 521(a)(1)(B)(ii) (2018); FED. R. BANKR. P. 1007(b)(1)(B); (2) a statement of monthly net income, *see* 11 U.S.C. § 521(a)(1)(B)(v) (2018); and (3) a statement of current monthly income, FED. R. BANKR. P. 1007(b)(4). On the debt side, the debtor must file a schedule of assets and liabilities. *See* 11 U.S.C. § 521(a)(1)(B)(i) (2018); FED. R. BANKR. P. 1007(b)(1)(A). For a discussion of these requirements, *see* 1 COLLIER BANKRUPTCY PRACTICE GUIDE ¶ 15.03 (2019).

284. *See* Hunt, *supra* note 33, at 775–78.

285. *See* *Brunner v. N.Y. State Higher Educ. Servs. Corp.*, 831 F.2d 395, 396 (2d Cir. 1987) (specifying three-element test).

286. *Id.* (stating that the first element of the *Brunner* test is that the debtor cannot currently maintain a minimal standard of living if forced to repay).

287. *Id.* (stating that the second element of the *Brunner* test is existence of additional circumstances indicating that debtor's inability to maintain a minimal standard of living while repaying is likely to continue for a significant portion of the repayment period).

288. *Id.* (stating that the third element of the *Brunner* test is that the debtor has made good-faith efforts to repay the loans).

289. Given the Department's view that undue hardship “necessarily” is evaluated according to the courts' interpretation, it would appear that the Department's standards for consent to discharge would vary with the different judicial standards used in different localities. *See* Dear Colleague Letter, *supra* note 22, at 3, App. B (detailing tests adopted by judicial circuits). Scholars have documented the wide variation in judicial interpretation of “undue hardship” from jurisdiction to jurisdiction. *See, e.g.*, Bruckner et al., *supra* note 18, at

discouragement thwarts the goals of the student loan programs, regardless of the borrower's level of suffering or past repayment efforts. Thus, adding a borrower-discouragement criterion for consent to discharge promotes the programs' goals more surely than does relying on undue hardship as the only substantive ground for such consent.

As a third example, this author also argues elsewhere that student loans that harmed the borrower should be dischargeable because a purpose of the student loan programs is to help borrowers, rather than simply to enable them to gamble on education at their own risk.<sup>290</sup> When a student has borrowed for education designed to prepare the student for work in a specific field, the borrower's inability to find a solid job in that field suggests that the borrower has on net been harmed by borrowing for education.<sup>291</sup> Although inability to find suitable work may be a less easily administrable criterion than the debt-to-income ratio just discussed, application for discharge on that ground could be handled through an administrative process that would be less burdensome than an adversary proceeding. Perhaps the IRS's Offer in Compromise (OIC) process could be considered as a possible model.<sup>292</sup>

Like the discouraged borrower, the borrower who has been harmed by taking out student loans may suffer undue hardship. But a borrower may be worse off for having incurred the loans despite being able to maintain a "minimal" standard of living while repaying. That seems to have been the case for Audrey Eve Schatz.<sup>293</sup> Although she did not earn more than a de minimis amount as a lawyer<sup>294</sup> despite applying for over 100 legal jobs after law school graduation,<sup>295</sup> she was unable to discharge \$110,000 in law school debt<sup>296</sup> because the court found that she could pay off the loans by selling her house.<sup>297</sup> It seems highly likely that Audrey Schatz ended up worse off than if she had never attended law school. Her student loans probably harmed her, contrary to the purposes of the program.

This Section has provided three concrete examples of how the Department could promote the purposes of the student loan programs by consenting to discharge on grounds other than undue hardship. These examples illustrate a more general point: Department discharge policy has been based on a standard that ignores key purposes of the student loan programs that favor expanding dischargeability. The Department

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196–205.

290. See Hunt, *supra* note 33, at 778–83.

291. *Id.*

292. For a description of the OIC process, see *infra* notes 333–42 and accompanying text.

293. See Schatz v. Dep't of Educ. (*In re Schatz*), 584 B.R. 1 (Bankr. D. Mass. 2018).

294. In the seven months leading up to her bankruptcy filing, Schatz earned approximately \$5300 from running her solo legal practice and helping another law firm with some house closings, as well as approximately \$7000 from performing administrative and legal work for a nonprofit she had founded. *Id.* at 4.

295. *Id.* at 3.

296. *Id.*

297. *Id.* at 9. It appears likely that she owned the house before going to law school and borrowing the money. The opinion does not reveal when she bought it, but she had lived in Massachusetts since 1993, *id.*, and did not find financial success after law school, *id.* at 4. It should be noted that Schatz actually settled with the Department, so that she was seeking to discharge only private loans. *Id.* at 3. Nevertheless, the case illustrates the debtor was probably made worse off by loans despite absence of "undue hardship" in the court's eyes.

should liberalize its dischargeability policy in order to take account of all relevant program goals.

*C. The Department Has the Authority to Consent to Discharge Even Where  
“Undue Hardship” Is Absent*

Currently, the Department consents to discharge only on the grounds of undue hardship or cost-ineffectiveness of opposing discharge.<sup>298</sup> The Department could make relief easier by adding grounds for consent to discharge. As just argued, the Department should consider doing so in order to promote the overall purposes of the student loan programs. Section III.C argues that the Department has the authority to consent to discharge on grounds other than “undue hardship.”

Before discussing the legal grounds on which the Secretary could expand dischargeability, it is worth considering who might challenge the Secretary’s decision in this regard. Expanding dischargeability under the Perkins and FFEL programs could draw a challenge because third-party holders (institutions or guaranty agencies) may have a financial stake in the loans being discharged. It appears that discharging otherwise collectible loans costs Perkins institutions money.<sup>299</sup> The situation with the FFEL program is murkier, but based on the information available, it is at least plausible that guaranty agencies can lose money when FFEL loans are discharged.<sup>300</sup>

For the most important program, the Ford program, it is not clear that the Department’s decision to consent to discharge more readily would be challenged. After all, the Ford loan creditor is the federal government, which would be making the change. Bankrupt debtors, for their part, would be unlikely to complain about a loosening of standards. However, perhaps loan servicers<sup>301</sup> or private lenders who

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298. *See supra* Section I.C.

299. It appears that lending institutions now can make use of funds collected on Perkins loans, less the “federal share” of such funds (recall that Perkins loans are funded by a combination of federal and institutional money). Thus, it would seem that institutional funds are at risk in borrower bankruptcy, at least to the extent collection would occur if discharge is denied. Press Release, Federal Student Aid, Perkins Loan Program – Federal Perkins Loan Revolving Fund Distribution of Assets and Timelines for 2018–19 (July 11, 2018), <https://ifap.ed.gov/electronic-announcements/07-11-2018-campus-based-subject-perkins-loan-program-federal-perkins-loan> [<https://perma.cc/7GFS-AVJF>] (“Institutions must return to the Department the federal share and return to the institution the institutional share of an institution’s Perkins Fund.”).

300. If discharge is granted, the Department pays the guaranty agency “a percentage of the outstanding principal and interest that is equal to the complement of the reinsurance percentage paid on the loan,” but the percentage is not clearly specified. 34 C.F.R. § 682.402(k)(5) (2019). If discharge is denied, the lender “repurchases” the loan from the guaranty agency, but the regulations do not specify the purchase price. *See id.* § 682.402(j)(1)(i). It does not appear possible to determine from the regulations what guaranty agencies’ financial incentives are in cases of borrower bankruptcy. For a fuller discussion, see Hunt, *supra* note 95, at 100–01.

301. Loan servicing contracts are complex, and whether consent policy change would harm servicers’ monetary interests is not immediately apparent. *See Loan Servicing Contracts*, FED. STUDENT AID, <https://studentaid.ed.gov/sa/about/data-center/business-info/contracts/loan>

compete with the Ford program would have the desire and right<sup>302</sup> to mount a challenge. Moreover, the Department should act lawfully even if its action will not be challenged. Thus, it is worthwhile to consider the legal basis for liberalizing the student loan bankruptcy discharge rules.

1. The Secretary Enjoys Authority to Regulate Loan Programs and to Release Claims that on Its Face Encompasses the Power to Consent to Bankruptcy Discharge

The Secretary enjoys broad authority to make “rules and regulations” to “carry out functions . . . vested in the Secretary”<sup>303</sup> and “to administer and manage the functions of the Secretary or the Department.”<sup>304</sup> The District Court for the District of Columbia, in holding that these provisions authorized a Department student loan rule, recently observed that they “fashion an awfully big umbrella,”<sup>305</sup> and that the Higher Education Act and Title IV are a statute and a program “‘administered’ and ‘manage[d]’ by the Department.”<sup>306</sup> In addition to these general grants of power, Congress has specifically authorized the Secretary to “prescribe such regulations as may be necessary to carry out the purposes” of the FFEL program.<sup>307</sup>

Settling borrower bankruptcies is a “function” of the “Secretary” or “Department” and therefore falls within the scope of Congress’s general delegation of rulemaking authority. Moreover, the Secretary is specifically authorized to “compromise,”

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-servicing [<https://perma.cc/D7KB-98QQ>] (posting federal student loan servicing contracts).

302. There could be a question whether a servicer’s or private lender’s financial interests fall “arguably within the zone of interests” “protected or regulated” by the Bankruptcy Act and the Higher Education Act. *Ass’n of Data Processing Serv. Orgs., Inc. v. Camp*, 397 U.S. 150, 153 (1970). If not, the complaining entity would not have a cause of action. *See* 13A CHARLES ALAN WRIGHT, ARTHUR R. MILLER & EDWARD H. COOPER, FEDERAL PRACTICE & PROCEDURE: JURISDICTION § 3531.7 (3d ed. & Supp. 2019) (“The zone-of-interests test asks ‘whether a legislatively conferred cause of action encompasses a particular plaintiff’s claim.’” (quoting *Lexmark Int’l, Inc. v. Static Control Components, Inc.*, 572 U.S. 118, 119 (2014))). *But see* 20 U.S.C. § 1098a(a)(1) (2018) (describing “loan servicers” and “lenders” as “groups involved in student financial assistance programs under” Title IV of the Higher Education Act, and requiring that the Secretary “obtain the advice of and recommendations from” such groups in issuing regulations for student-loan programs).

303. 20 U.S.C. § 1221e-3 (2018) (conferring on Secretary authority to make “rules and regulations” “in order to carry out functions otherwise vested in the Secretary”).

304. *Id.* § 3474 (granting Secretary authority to make “rules and regulations” “as the Secretary determines necessary or appropriate to administer and manage the functions of the Secretary or the Department”).

305. *Ass’n of Private Sector Colls. & Univs. v. Duncan*, 110 F. Supp. 3d 176, 199 (D.D.C. 2015), *aff’d*, 640 F. App’x 5 (D.C. Cir. 2016); *see also id.* at 201 (“[F]ederal law also gives the Department the power to ‘carry out’ programs like Title IV.”).

306. *Id.* at 199 (alteration in original).

307. 20 U.S.C. § 1082(a)(1) (2018).

“waive,” or “release” government claims arising under the FFEL<sup>308</sup> and Perkins<sup>309</sup> programs, and to consent to modification of FFELP<sup>310</sup> or Perkins<sup>311</sup> loan terms. As the Court of Appeals for the D.C. Circuit has held regarding the government’s rights as “a surety or guarantor” under the GSL program, the Department “may by regulation decline to enforce those rights in the larger interests of the student loan program.”<sup>312</sup>

The discussion in Sections I.C and I.D demonstrates that the Department has long maintained that its rulemaking power extends to regulating opposition to bankruptcy discharge for the FFEL and Perkins programs. Although some of the Department’s specific claims of statutory authority have been questionable,<sup>313</sup> the just-preceding discussion shows that the Department has been right in substance to claim this prerogative.

For Ford loans, the Higher Education Act apparently contains no grant of modification, compromise, or waiver authority as explicit as the grant for Perkins and FFELP loans. However, the Court of Federal Claims has treated the FFEL grant of power to compromise as applicable to the Ford program.<sup>314</sup> Although the court did not explain why it did so, one argument in favor of the court’s position is that the Ford program incorporates the FFELP grants by reference. Ford program loans have

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308. *See id.* § 1082(a), (a)(6) (“In the performance of . . . the functions, powers, and duties, vested in him by this part, the Secretary may . . . (6) enforce, pay, compromise, waive, or release any right, title, claim, lien, or demand, however acquired . . .”).

309. *See id.* § 1087hh (“In carrying out the provisions of this part, the Secretary is authorized . . . (2) to enforce, pay, compromise, waive, or release any right, title, claim, lien, or demand, however acquired . . .”).

310. *See id.* § 1082(a)(4) (“In the performance of . . . the functions, powers, and duties, vested in him by this part, the Secretary may . . . (4) subject to the specific limitations in this part, consent to modification, with respect to . . . any . . . provision of any note or other instrument evidencing a loan which has been insured by the Secretary under this part.”). The reference to loans “insured by the Secretary” may indicate that this power applies only to loans the government insures directly, rather than to loans it insures indirectly through a reinsurance agreement with a guaranty agency. No court appears to have addressed this potential ambiguity.

311. *See id.* § 1087hh(1) (“In carrying out the provisions of this part, the Secretary is authorized – (1) to consent to modification, with respect to . . . any . . . provision of any note evidencing a loan which has been made under this part.”).

312. *United States v. Griffin*, 707 F.2d 1477, 1482 (D.C. Cir. 1983). The opinion speaks of the powers of the “OE,” the Office of Education of the Department of Health, Education, and Welfare. That office is the predecessor to the Department.

313. In particular, the 1987 Perkins rules relied on Sections 424 and 1087cc of the Education Code. *See* 1987 Perkins Rules, *supra* note 97, at 45,561. These provisions on their face appear to govern provisions that must be included in contracts between the Department and institutions, rather than the Department’s rulemaking power. *See* 20 U.S.C. § 1087cc (2018); National Defense Education Act, Pub. L. No. 85-864, § 204, 72 Stat. 1583, 1584 (1958) (codified at 20 U.S.C. § 424 (1964)). Moreover, as of 2019, Section 424 has been “omitted” from the U.S. Code. *See* 20 U.S.C. §§ 421–25 (2018). A companion paper discusses this issue in more detail. *See* Hunt, *supra* note 95, at 96.

314. *McCain v. United States*, No. 10-264C, 2011 WL 2469828, at \*5 (C.F.C. June 17, 2011) (treating 20 U.S.C. § 1082(a)(6) as a source of authority to compromise Federal Direct Consolidation Loan).

the same “terms, conditions, and benefits” as corresponding FFELP loans,<sup>315</sup> so if bankruptcy discharge opposition rules are “terms, conditions, or benefits” of student loans, the grants of power to regulate and compromise FFELP loans would probably carry over to the Ford program.<sup>316</sup>

Apart from the incorporation-by-reference argument, it makes sense that the government has at least as much authority to compromise or release claims when it is the lender (as under the Ford program) as it has when other parties make the loans (as under the Perkins and FFEL programs). Indeed, the Secretary has long claimed the authority to decide “whether the interests of the United States are served by refraining from collection on all or part of a defaulted loan.”<sup>317</sup>

Moreover, the fact that the Higher Education Act apparently lacks provisions explicitly addressing most aspects of collections under the Ford program<sup>318</sup> weakens any negative inference that might be drawn from the absence of a specific grant relating to modification, compromise, or waiver. Thus, the general grants of regulatory authority to the Secretary should be understood to encompass the power to make discharge opposition rules to promote the overall purposes of the student loan programs.<sup>319</sup>

## 2. Nothing Limits the Secretary’s Authority to Consent to Situations Where “Undue Hardship” Is Present

The Higher Education Act suggests that a broad array of considerations may enter into setting the Department’s collection policy in general, and its bankruptcy discharge opposition policy in particular. No provision of the Higher Education Act appears to make collection the overriding consideration in administering student

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315. 20 U.S.C. § 1087e(a)(1) (2018) (“Unless otherwise specified in this part, loans made to borrowers under this part shall have the same terms, conditions, and benefits . . . as loans made to borrowers, and first disbursed on June 30, 2010 under sections 428 [Stafford], 428B [PLUS], 428C [Consolidation], or 428H [Unsubsidized Stafford].”).

316. A question for prospective regulation of Ford loans under an incorporation-by-reference theory is whether the statute’s provision that Ford loans have the same terms as FFEL loans “first disbursed on June 30, 2010” precludes regulatory changes made after that date. However, changes to FFELP regulations made today that relate to borrower discharge opposition presumably would apply to still-outstanding FFELP loans, including those disbursed on June 30, 2010.

317. 1985 GSL PLUS NPRM, *supra* note 104, at 35,966.

318. Apart from provisions authorizing the Secretary to contract with servicers, *see* 20 U.S.C. § 1087f(a)(1), (b)(2) (2018), to require institutions to provide information “for the servicing and collecting” of loans, and to require defaulting borrowers to pay reasonable collection costs, *see id.* § 1087e(d)(5)(A), the Higher Education Act does not appear to have any provisions at all that address collection of Ford loans, whether out of court, through litigation, in bankruptcy, or otherwise. The Act contains no collection directives analogous to those discussed in the following notes for the FFEL and Perkins programs. *See infra* notes 321–23 and accompanying text.

319. It seems this power would encompass the authority to determine that certain situations give rise to a rebuttable presumption of undue hardship, as scholars have suggested. *See* Bruckner et al., *supra* note 18, at 244; Jiménez et al., *supra* note 16, at 115.

loans.<sup>320</sup> Instead, injunctions to collect in the Act are framed in terms of “reasonable diligence,”<sup>321</sup> “due diligence,”<sup>322</sup> and “appropriate collection efforts.”<sup>323</sup> These open-ended terms imply that the Department, in administering the student loan programs to promote their purposes, can consent to discharge even when undue hardship is absent.

It might be argued that Congress’s establishment of the undue-hardship standard for student loan bankruptcies reflects a decision that discharge should be granted only if undue hardship is present. However, the text of the grants of authority to regulate, waive, and compromise discussed in Section III.C.1 reflects no such limitation. Section 523(a)(8) of the Bankruptcy Code, which contains the undue-hardship standard,<sup>324</sup> is not directed to the Department’s authority to make rules or to its settlement or waiver authority. Although a purpose of section 523(a)(8) was to restrict discharge in some respects,<sup>325</sup> the author’s review of the legislative history of section 523(a)(8) has not turned up any indication that the provision’s purpose was to limit the Secretary’s power in this regard.<sup>326</sup> Courts have looked to the overall purposes of the student loan programs in reviewing the Secretary’s Title IV rules.<sup>327</sup> That suggests that a narrow focus on section 523(a)(8)’s restrictive purpose is inappropriate.

In addition, the Department has implicitly rejected the existence of such a limitation on its rulemaking authority for at least thirty years. At least since 1987, the Department has assumed that it can prescribe consent to discharge on the grounds of cost-effectiveness rather than borrower undue hardship.<sup>328</sup> Its authority to consider

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320. The Federal Debt Collection Procedures Act of 1990, Pub. L. No. 101-647, §§ 3601–31, 104 Stat. 4933 (1990) (codified at 28 U.S.C. §§ 3001–3308), and the Debt Collection Improvement Act of 1996, Pub. L. No. 104-134, §§ 31001–02, 110 Stat. 1321, 1321–358 to 1321–381 (1996) (codified at 31 U.S.C. §§ 3701–20e), govern some aspects of student-loan debt collection. However, neither statute mentions bankruptcy or discharge in the context of bankruptcy.

321. See 20 U.S.C. § 1072b(d)(3)(A)–(B) (2018) (FFELP guaranty agencies); *id.* § 1082(h) (FFELP lenders).

322. See *id.* § 1087cc(a)(4) (Perkins program institutions).

323. See *id.* § 1087gg(b) (Perkins loans held by Secretary). The FFELP part of the Education Code contemplates that the Secretary will try to collect but apparently does not set standards. See *id.* § 1080(b) (referring to “net recovery made by the Secretary” on defaulted loan assigned to Secretary).

324. See 11 U.S.C. § 523(a)(8) (2018).

325. See Hunt, *supra* note 122, at 1310–11 (summarizing purposes of undue-hardship provision).

326. See H.R. REP. NO. 95-595 (1977); S. REP. NO. 94-482 (1976); H.R. REP. NO. 94-1232 (1976); H.R. DOC. NO. 93-137 (1973) (report of the Commission on the Bankruptcy Laws of the United States); 124 CONG. REC. 1791–98 (1978); 122 CONG. REC. 27,977 (1976).

327. *Ass’n of Private Sector Colls. & Univs. v. Duncan*, 110 F. Supp. 3d 176, 199 (D.D.C. 2015), *aff’d*, 640 F. App’x 5 (D.C. Cir. 2016) (upholding rule in part because it “advance[d] the purposes of . . . the Higher Education Act and Title IV”).

328. See 1987 Perkins Rules, *supra* note 97, at 45,560 (codified at 34 C.F.R. § 674.49(c)(4)–(5)) (adopting provision that institution “shall oppose” discharge if undue hardship was absent and expected cost of litigation fell below one-third of amount owed).

this nonhardship ground apparently has never been questioned,<sup>329</sup> and the Department's longstanding, consistent position on the matter is itself a ground for deference.<sup>330</sup> Thus, it seems established that one big-picture statutory goal—that of wisely husbanding resources—justifies consenting to discharge when undue hardship is absent. It is therefore difficult to argue that other such goals—those of promoting access, freedom of choice, and education, and of benefiting students—should be excluded.<sup>331</sup>

### 3. Other Federal Agencies Have Adopted Nonhardship-Based Programs for Compromise of Claims

Both the IRS and the Department of Justice have developed programs to compromise or release federal claims. These programs apparently are based on general grants of authority and the materials describing them do not cite statutory authorization for the particular grounds for compromise or release they adopt.<sup>332</sup> This suggests that the Department's grants of authority create an overall discretionary power to consent to discharge on grounds of the Department's devising, as long as doing so promotes the purposes of the student loan programs.

The Internal Revenue Service operates an Offer in Compromise (OIC) program. An OIC, in the words of the IRS, “allows you to settle your tax debt for less than the full amount you owe.”<sup>333</sup> The Secretary of the Treasury can compromise a claim on

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329. Indeed, the theory that Congress intended undue hardship to be the only ground for both nonconsensual and consensual discharge could foreclose even the Department's independent evaluation of undue hardship. If, for example, deterrence of meritless petitions is important enough, then the Department arguably should not give up the chance to convince the bankruptcy court that undue hardship is absent, even if the Department's view is otherwise.

330. *See, e.g., Alaska Dep't of Env'tl. Conservation v. EPA*, 540 U.S. 461, 487 (2004) (“We normally accord particular deference to an agency interpretation of ‘longstanding’ duration.” (quoting *Barnhart v. Walton*, 535 U.S. 212, 220 (2002))); *see also* Anita S. Krishnakumar, *Longstanding Agency Interpretations*, 83 *FORDHAM L. REV.* 1823, 1825 (2015) (“In principle, virtually everyone seems to agree that longstanding agency statutory interpretations should be entitled to extra weight upon judicial review.”).

331. *See supra* Section III.B.1.

332. Although immigration law enforcement is farther afield than other debt-collection regimes, it provides an example of an agency forbearing, without express statutory authorization, from pursuing individuals. The immigration authorities have, since before 1975, exercised “prosecutorial discretion” to decline to pursue removal in some instances. *See* Shoba Sivaprasad Wadhia, *The Role of Prosecutorial Discretion in Immigration Law*, 9 *CONN. PUB. INT. L.J.* 243, 246 (2010). Justice Scalia described one such exercise of discretion, “deferred action,” as adopted “for humanitarian reasons, or simply for [the agency's] own convenience” and as a “commendable exercise in administrative discretion, developed without express statutory authorization.” *Reno v. Am. Arab Anti-Discrimination Comm.*, 525 U.S. 471, 484–85 (1999) (quoting 6 C. GORDON, S. MAILMAN & S. YALE-LOEHR, *IMMIGRATION LAW AND PROCEDURE* § 72.03(2)(h) (1998)); *see also* Recommendation from Prakash Khatri, Ombudsman, CIS, to Dr. Emilio T. Gonzalez, Director, CIS, at 1 (April 6, 2007) (“There is no statutory basis for deferred action, but the regulations reference this form of relief . . .”).

333. *Offer in Compromise*, INTERNAL REVENUE SERV. (Jan. 3, 2020), <https://www.irs.gov/payments/offer-in-compromise> [<https://perma.cc/5J3H-SNCU>].



any of several bases set forth in regulations.<sup>334</sup> The OIC rules recognize nonhardship bases for compromising federal claims even though hardship is the only specific statutory criterion for compromise.

The only specific statutory criteria for OICs are hardship-related: an OIC should leave the taxpayer “an adequate means to provide basic living expenses”<sup>335</sup> and the Secretary of the Treasury may not reject an OIC from a low-income taxpayer solely because of the amount of the offer.<sup>336</sup> Nevertheless, the OIC regulations provide for acceptance of OICs on grounds other than hardship, such as that compromise would “promote effective tax administration” where, due to “public policy and equity considerations,” “collection of the full [tax] liability would undermine public confidence that the tax laws are being administered in a fair and equitable manner.”<sup>337</sup> In promulgating the OIC regulations, the Secretary did not claim that all the grounds for compromise had an explicit statutory basis, instead citing “[t]he legislative history accompanying” the provision on which it relied.<sup>338</sup>

The OIC program differs from what this Article advocates for student loan bankruptcy in that the IRS will not accept OICs of zero. This, however, is due to an express statutory requirement of partial payment that apparently has no analog in student loan law.<sup>339</sup> Moreover, the IRS reportedly will accept nominal settlement offers when warranted.<sup>340</sup> The OIC statute also expressly authorizes the Secretary of the Treasury to “prescribe guidelines for officers and employees of the Internal Revenue Service to determine whether an offer-in-compromise is adequate and should be accepted to resolve a dispute.”<sup>341</sup> This provision arguably distinguishes the OIC program at least from compromise under the Ford program, where the Secretary is not specifically authorized to compromise claims under that particular program. However, the Secretary’s overall authority to compromise Ford claims by consenting to partial or full discharge does not seem to be in dispute.<sup>342</sup>

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334. See 26 C.F.R. § 301.7122-1(a)(1) (2019) (providing for compromise “[i]f the Secretary determines that there are grounds for compromise under this section”).

335. See 26 U.S.C. § 7122(d)(2)(A) (2018).

336. *Id.* § 7122(d)(3)(A). The Secretary of the Treasury cited both section 7122 and section 7805 as authority for the OIC regulations. See *Compromise of Tax Liabilities*, 67 Fed. Reg. 48,025, 48,026, 48,029 (July 23, 2002) (codified at 26 C.F.R. pt. 301). Section 7805 empowers the Secretary of the Treasury to “prescribe all needful rules and regulations for the enforcement of this title,” which does not mention compromise of tax liability at all, much less establish substantive standards for compromise. *Id.*

337. 26 C.F.R. § 301.7122-1(b)(3)(ii) (2019).

338. *Compromise of Tax Liabilities*, 67 Fed. Reg. at 48,026 (“The legislative history accompanying [the Internal Revenue Service Restructuring and Reform Act of 1998] explains that Congress intended that, in certain circumstances, factors such as equity, hardship, and public policy be taken into account by the IRS in evaluating whether the compromise of individual tax liabilities would promote effective tax administration.”).

339. See 26 U.S.C. § 7122(c)(1) (2018) (requiring that partial payment accompany offer in compromise).

340. See W. Edward Afield, *Compromising Student Loans*, 69 S.C. L. REV. 81, 104–05 (2017). Professor Afield argues that the OIC program can be a model for improving the various income-driven repayment programs available for student loans. See *id.* at 84–86.

341. See 26 U.S.C. § 7122(d)(1) (2018).

342. See *Limkemann v. Dep’t of Educ.* (*In re Limkemann*), 314 B.R. 190, 192 (Bankr.

The Department of Justice also maintains nonhardship-based standards for settlement of certain claims of the United States,<sup>343</sup> including claims against bankrupt debtors.<sup>344</sup> The *Justice Manual* provides that United States Attorneys can settle certain claims of the United States on any of nine bases, including that compromise is “necessary to prevent injustice”<sup>345</sup> or is “in the interests of the United States.”<sup>346</sup> The Manual cites no specific statutory authority for these bases for settlement.

#### 4. The Department Can Add Bases for Dischargeability Under the Ford Program Without Notice-and-Comment Rulemaking

Section III.C has argued so far that the Department can consent to discharge on bases other than the ones it currently recognizes, undue hardship and cost ineffectiveness of opposing discharge. Section III.C.4 argues that, at least for the Ford program, the Department can add such new grounds for consent to discharge without going through notice-and-comment rulemaking.

As noted, the Department has the power to make “rules” to “carry out,” “administer,” and “manage” its functions,<sup>347</sup> and these functions include collecting debts and compromising claims.<sup>348</sup> Under the Administrative Procedure Act (APA), “rules” include not only “legislative” rules, which must be adopted through notice and comment, but also “interpretative rules,”<sup>349</sup> and “rules of agency, organization, procedure, or practice.”<sup>350</sup> Rules in the latter two categories may be adopted without notice and comment.<sup>351</sup>

In addition, the Secretary has “responsibility for the development and promulgation of policy . . . relating to” the federal student loan programs.<sup>352</sup> The

N.D. Iowa 2004) (noting that debtor and Department of Education reached a tentative settlement agreement while debtor’s adversary proceeding was pending). The Department argued against discharge on the ground that the debtor was eligible for IDR “offered by the William D. Ford Program.” *Id.* It appears likely that this was a case in which the Department offered to compromise a Ford loan while bankruptcy was pending.

343. U.S. DEP’T OF JUSTICE, *JUSTICE MANUAL* loc. 4-3.100 to 4-3.432 (2018).

344. *Id.* loc. 4-3.220 (“Claims in Conjunction with Bankruptcy Code Proceedings . . . The same limitations and standards as described in JM 4-3.200 govern compromises under the Bankruptcy Code.”).

345. *Id.* loc. 4-3.200F.

346. *Id.* loc. 4-3.200I. This determination is to be made “in light of [the U.S. Attorney’s] assessment of the litigation risk and the amounts involved in the event of full, partial, or no success.” *Id.* Perhaps unsurprisingly, given the Attorney General’s status as the litigator rather than the client, the guidelines provide, “Hardship, which does not involve inability to pay, is not a proper basis for settlement.” *Id.* loc. 4-3.200D.4; see Devins & Herz, *supra* note 206, at 562 (in government civil actions, “DOJ will not proceed without a client”).

347. See 20 U.S.C. §§ 1221e-3, 3474 (2018).

348. See *supra* Section III.C.1.

349. See 5 U.S.C. § 553(b)(3)(A) (2018).

350. See *id.*

351. See *id.* § 553(b)(3).

352. 20 U.S.C. § 1018(b)(1) (2018). The statute references “programs of student financial assistance under subchapter IV.” *Id.* That is the portion of the Code that governs the federal student-loan programs.

APA exempts “general statements of policy” from its general requirement of notice-and-comment rulemaking.<sup>353</sup>

Thus, the Department does not have to engage in notice and comment if it issues a general statement of policy, interpretive rule,<sup>354</sup> or rule of agency practice announcing that it will consent to discharge on grounds other than undue hardship. The Department has already issued just such a document: the 2015 Dear Colleague Letter. As regards the Ford program, the letter is a policy statement or rule of practice that states that the Department will consent to discharge on the ground of cost-effectiveness<sup>355</sup>—that is, a ground other than undue hardship.

The 2015 Dear Colleague Letter appears to be a general statement of policy. As defined in the 1947 Attorney General’s Manual, adopted a year after enactment of the APA, general statements of policy “advise the public prospectively of the manner in which the agency proposes to exercise a discretionary power.”<sup>356</sup> Given that the HEA does not address collections in borrower bankruptcy at all,<sup>357</sup> it seems difficult to describe the Department’s decision whether to oppose discharge in a Ford-program borrower’s bankruptcy as anything other than “discretionary.”

The 2015 Dear Colleague Letter appears to “advise the public prospectively” of how the Department intends to exercise its discretionary power to consent to discharge. With regard to Ford program loans, the 2015 Dear Colleague Letter sets forth the analysis the Department currently performs “when evaluating whether to consent or not object” to a debtor’s discharge petition.<sup>358</sup>

Although the line between a statement of policy and a legislative rule can be difficult to draw in some instances, the case here does not seem to be all that close. As Professor Keith Werhan has observed, courts often distinguish between legislative rules and policy statements by looking to whether the pronouncement in question binds the agency.<sup>359</sup> The agency commits to following rules, but when issuing a policy statement, it “retains the discretion and authority to change its position—even abruptly—in any specific case.”<sup>360</sup> The letter sets forth the Department’s current policy and does not purport to bind the Department or any other party.

Insofar as the letter is understood as instructing Department employees how to perform their functions, it may be a “rule[] of agency . . . practice.”<sup>361</sup> As noted,

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353. See 5 U.S.C. § 553(b)(3)(A) (2018).

354. Despite the APA’s use of the word “interpretative,” this Article uses the term “interpretive,” which seems to be more common in current discussion. See, e.g., *Azar v. Allina Health Servs.*, 139 S. Ct. 1804, 1807 (2019).

355. See 2015 Dear Colleague Letter, *supra* note 22, at 1, 3–4 (noting that for Ford loans the Department follows the same “two-step analysis” as for non-Ford student loans, and that only first step in analysis involves evaluation of undue hardship; second step involves determining cost-effectiveness of opposing discharge).

356. See U.S. DEP’T OF JUSTICE, ATTORNEY GENERAL’S MANUAL ON THE ADMINISTRATIVE PROCEDURE ACT 30 n.3 (1947).

357. See 20 U.S.C. §§ 1070–99d (2018).

358. 2015 Dear Colleague Letter, *supra* note 22, at 1.

359. See KEITH WERHAN, PRINCIPLES OF ADMINISTRATIVE LAW 284 (3d ed. 2019).

360. *Syncor Int’l Corp. v. Shalala*, 127 F.3d 90, 94 (D.C. Cir. 1997).

361. 5 U.S.C. § 553(b)(3)(A) (2018).

notice and comment is not required for such rules.<sup>362</sup> Whether characterized as a statement of policy or a rule of practice, the 2015 Dear Colleague Letter properly was issued without notice and comment. It is an on-point precedent for the proposition that the Department can decide to consent to discharge on grounds other than undue hardship without notice and comment.

Further evidence of the authority to take such action without notice and comment comes from other agencies. They likewise handle decisions about bankruptcy and collection matters through documents apparently adopted without notice-and-comment rulemaking. The *Internal Revenue Manual* supplies directions to IRS employees for consenting to Chapter 11<sup>363</sup> and Chapter 13 bankruptcy plans,<sup>364</sup> as well as policies relating to the OIC program previously discussed.<sup>365</sup> The manual apparently was not issued through notice-and-comment procedures.<sup>366</sup> The *Justice Manual*, which as discussed provides guidance for when the United States will compromise claims in litigation,<sup>367</sup> also does not appear to have been adopted through notice and comment.<sup>368</sup> It seems that the Department can, following the example of other agencies in federal debt collection and its own precedent in the 2015 Dear Colleague Letter, expand its dischargeability criteria for the Ford program without notice and comment.

Action without notice and comment is more difficult for the other two programs. As previously explained, the Perkins program regulations require holders to oppose discharge whenever undue hardship is absent and collection costs are expected to be less than one-third of the loan balance.<sup>369</sup> This requirement seems to leave no room for adding more grounds for consent discharge, and changing it would seem to require notice-and-comment rulemaking.

The FFEL program has no similar barrier in its regulations, but the Department faces the issue that adding grounds for consent to discharge would regulate the conduct of third parties, namely guaranty agencies,<sup>370</sup> rather than merely stating policies and procedures governing its own conduct as would be the case in acting on Ford program loans. Although the Department could issue an interpretive rule without notice and comment,<sup>371</sup> such rules must “interpret[] ‘existing law’” rather

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362. *See id.* As regards the FFEL and Perkins programs, the letter can be understood as interpreting the Department’s existing regulations, and thus may be an interpretive rule. Such rules also can be issued without notice and comment. *See id.*

363. *See, e.g.*, INTERNAL REVENUE SERVICE, INTERNAL REVENUE MANUAL loc. 5.9.8.14.2. (2019).

364. *See, e.g., id.* loc. 5.9.10.5

365. *See, e.g., id.* loc. 5.8.5.

366. *See id.* loc. 1.11.2 (describing process for making changes to *Internal Revenue Manual*; process described does not include notice and comment).

367. *See supra* Section III.C.3.

368. *See* U.S. DEP’T OF JUSTICE, *supra* note 343, loc. 1-1.300 (describing process for changes to *Justice Manual*; process described does not include notice and comment).

369. *See supra* note 139 and accompanying text.

370. *See* 34 C.F.R. § 682.402(i)(1) (2019) (instructing guaranty agencies on consent to discharge).

371. *See* 5 U.S.C. § 553(b)(3)(A) (2018) (providing exception to notice-and-comment requirement for “interpretative” rules).

than “mak[e] ‘new law.’”<sup>372</sup> This distinction has been criticized and may often be difficult to apply.<sup>373</sup> However, given the policy discretion involved in crafting new grounds for consent to discharge, it may be difficult to characterize the adoption of such grounds as simply “interpreting” statutory commands—even though doing so would advance statutory purpose.<sup>374</sup> Creating new grounds for consent to discharge would seem instead to be an exercise of legislative rulemaking power, requiring notice and comment.<sup>375</sup> Acting through notice and comment to adopt the new rules for the FFEL program would be consistent with the Department’s practices to date.<sup>376</sup>

##### 5. The Department Should Consider Adding Grounds for Consent to Discharge Through Guidance First, Following up with Notice-and-Comment Rulemaking

Assuming the Department can dispense with notice and comment in adopting additional bases for consent to discharge, at least for the Ford program, should it do so? As discussed in the context of fixing gaps and ambiguities in the regulations, one reason not to engage in notice and comment is the time and expense the process consumes.<sup>377</sup> Here, where the change is of greater significance, administrative convenience in adopting it has less relative weight. However, given the scale of the problem,<sup>378</sup> quick relief for borrowers is important.

A second reason for issuing guidance rather than notice and comment is to insulate agency action from judicial review.<sup>379</sup> This motive is of questionable legitimacy.

A third reason for simply issuing a new policy statement rather than pursuing notice-and-comment rulemaking is that the former approach preserves flexibility. Guidance documents such as policy statements can be amended without going through notice and comment.<sup>380</sup> Such flexibility could have its advantages. For

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372. See Michael Asimow, *Nonlegislative Rulemaking and Regulatory Reform*, 1987 DUKE L.J. 381, 394.

373. See Ronald M. Levin, *Rulemaking and the Guidance Exemption*, 70 ADMIN. L. REV. 263, 317–18 (2018) (collecting and endorsing critiques of the definition of an interpretive rule).

374. Instead of announcing new grounds for consent to discharge, the Department potentially could liberalize its dischargeability policy for the Perkins and FFEL programs by reinterpreting the term “undue hardship” on those programs’ regulations. Issuing such an “interpretive rule” would not require notice and comment. See 5 U.S.C. § 553(b)(3)(A) (2018). As discussed, given the Department’s position that “undue hardship” in its regulations means the same as “undue hardship” in section 523(a)(8) of the Bankruptcy Code, the Department’s authority to interpret the phrase authoritatively is in doubt. See *supra* Section II.B.3.

375. See Seidenfeld, *supra* note 153, at 336 (“[L]egislative rulemaking requires notice and comment.”).

376. See *supra* Section I.D.

377. See *supra* Section II.B.2.

378. As noted, one estimate of the number of borrowers each year who should apply for student-loan discharge and do not is 69,000. See *supra* note 14 and accompanying text.

379. For the potential effectiveness of acting through guidance in shielding agency action from judicial review, see *supra* note 153 and accompanying text.

380. See 1 KOCH & MURPHY, *supra* note 150, § 4:60 (“Since guidance documents may be adopted without notice and comment procedures, they may be amended or repealed . . . without notice and comment procedures.”). A district court recently held that a Dear Colleague letter

example, the Department arguably should be able to react quickly to any uptick in apparent strategic default behavior after the Department liberalizes its discharge policy.

In support of notice-and-comment rulemaking, the Department may engage with the public's views more robustly if it presents a specific proposal, receives comment, and responds to the comments it receives.<sup>381</sup> The requirement that the Department negotiate with stakeholders before starting notice-and-comment rulemaking for student loans may further enhance interested parties' participation.<sup>382</sup> In addition, notice-and-comment rulemaking produces more reliable rules from the borrower's perspective precisely because the rules cannot be so easily changed.<sup>383</sup>

Perhaps the best resolution is a sort of compromise. The Department could promptly issue guidance that implements as much of the desired policy liberalization as can be adopted without notice-and-comment rulemaking. After an interval to evaluate whether the new policy is working, the Department could engage in notice and comment to get a broad array of perspectives on the new policy's effectiveness and, if desired, make the policy permanent. This approach provides quick relief to borrowers, preserves flexibility to react to unintended consequences, then takes input

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from the Department governing a student loan program could, depending on the facts, be a "new rule," requiring the Department to acknowledge the change and explain its position. *USA Funds v. King*, 200 F. Supp. 3d 163, 166–67, 172 (D.D.C. 2016). However, there is no suggestion in the opinion that the Department was required to engage in notice-and-comment rulemaking. *See id.*

381. *See, e.g.,* Francesca E. Bignami, *The Democratic Deficit in European Community Rulemaking: A Call for Notice and Comment Rulemaking in Comitology*, 40 HARV. INT'L L.J. 451, 499 (1999) ("Notice and comment rulemaking guarantees pluralist interest participation in rulemaking."). *But see* Jason Webb Yackee & Susan Webb Yackee, *Testing the Ossification Thesis: An Empirical Examination of Federal Regulatory Volume and Speed, 1950-1990*, 80 GEO. WASH. L. REV. 1414, 1425 n.50 (2012) (collecting citations questioning whether notice-and-comment rulemaking brings about participation).

382. *See* 20 U.S.C. § 1098a(b)(1) (2018) ("Participants in the negotiations process shall be chosen by the Secretary from individuals nominated by groups described in subsection (a)(1)."); *id.* § 1098a(a)(1) (listing "groups involved in student financial assistance programs under this subchapter").

383. Notice-and-comment rulemaking would also produce longer-term reliability for third-party holders such as guaranty agencies and higher education institutions. Admittedly, it is not totally clear long-term reliability is desirable here. Chapter 7 bankruptcies typically are completed relatively quickly. *See Chapter 7 - Bankruptcy Basics*, U.S. COURTS, <https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-7-bankruptcy-basics> [<https://perma.cc/AE6C-ABXC>] (reporting that Chapter 7 discharge is usually granted in 60 to 90 days from filing unless a party objects to discharge or moves to extend the time to object to discharge). Thus, a student-loan borrower who is already in financial distress and contemplating Chapter 7 has a relatively short time horizon and is unlikely to develop a reliance interest in particular rules that is then frustrated if the rules are changed. By contrast, a borrower who wants long-term certainty about bankruptcy policy may be a would-be strategic defaulter, taking out loans that the borrower intends to discharge. On the other hand, reliability benefits good-faith planners as well as strategic defaulters. Some presumably recognize that educational investments do not always pan out and want to make an informed decision about them.

from all interested stakeholders and ultimately provides borrowers with reliable rules.

#### CONCLUSION

Historically, the Department's bankruptcy discharge opposition rules have missed the opportunity to alleviate the procedural barriers and substantive unpredictability facing student loan borrowers contemplating bankruptcy. In addition, the regulations reflect relatively little analysis, contain ambiguities and large gaps, and have been aimed narrowly at protecting the federal government's pecuniary interests at the expense of other purposes of the student loan programs. A thoughtful process that refines the bankruptcy discharge opposition rules in light of the overall purpose of the student loan programs is likely to improve the quality of the rules, honor Congressional intent, and help struggling student loan borrowers through more predictable and generous consent to discharge.