

New DOJ/DOE Guidance re: § 523(a)(8) Proceedings

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**Hon. Hannah L. Blumenstiel
(Bankr. N.D. Cal. – San Francisco)**

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I. Guidance Regarding Student Loan Bankruptcy Litigation

- A. Effective Nov. 17, 2022
- B. Developed by U.S. Dep’t of Justice, in coordination with U.S. Dep’t of Education
- C. Objectives:
 - 1. To set clear, transparent, and consistent expectations for discharge that debtors understand regardless of representation;
 - 2. To reduce debtors’ burdens in pursuing an adversary proceeding by simplifying the fact gathering process; and
 - 3. Where the facts support it, to increase the number of cases where the government stipulates to the facts demonstrating a debt would impose an undue hardship and recommends to the court that a debtor’s student loans be discharged.
- D. Application of the Guidance

1. Currently applies only to student loans held by DOE, but might apply more broadly in the future
2. Applies to § 523(a)(8) proceedings commenced on/after 11/17/2022, as well as (wherever practical) to such proceedings pending as of 11/17/2022
 - a. § 523(a)(8) does not apply to Health Education Assistance Loans or private education loans that meet the definition of qualified education loans under the Internal Revenue Code. *See* 26 U.S.C. § 221(d)(1).

II. Applicable Law

A. Statutory Framework

1. 11 U.S.C. § 523
 - (a) A discharge under section 727, 1141, 1192, 1228(a), 1228(b), or 1328(b) . . . does not discharge an individual debtor from any debt –
 - (8) unless excepting such debt from discharge would impose an undue hardship on the debtor and the debtor’s dependents, for –
 - (A)(i) an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution; or
 - (ii) an obligation to repay funds received as an educational benefit, scholarship, or stipend, or
 - (B) any other educational loan that is a qualified educational loan . . . incurred by a debtor who is an individual.

2. Fed. R. Bankr. P. 7001(6)

- a. Determination of dischargeability requires commencement of adversary proceeding

3. Fed. R. Bankr. P. 7004(b)(5)

- a. Governs service of process on United States

B. Caselaw

- 1. *Brunner v. New York State Higher Educ. Svcs. Corp.*, 831 F.2d 395 (2d Cir. 1987)

- a. *Brunner* Test (Majority Rule)

- i. 2d Cir. (*Brunner*)
- ii. 3d Cir. (*In re Faish*, 72 F.3d 298, 306 (3d Cir. 1995))
- iii. 4th Cir. (*In re Frushour*, 433 F.3d 393, 400 (4th Cir. 2005))
- iv. 5th Cir. (*In re Gerhardt*, 348 F.3d 89, 91 (5th Cir. 2003))
- v. 6th Cir. (*In re Cheesman*, 25 F.3d 356, 359-60 (6th Cir. 1994))
- vi. 7th Cir. (*Matter of Roberson*, 999 F.2d 1132, 1135 (7th Cir. 1993))
- vii. 9th Cir. (*In re Pena*, 155 F.3d 1108, 1112 (9th Cir. 1998))
- viii. 10th Cir. (*Educ. Credit Mgmt. Svcs. Corp. v. Polleys*, 356 F.3d 1302, 1309 (10th Cir. 2004))
- ix. 11th Cir. (*In re Cox*, 338 F.3d 1238, 1241 (11th Cir. 2003))

- b. Standard

- i. Debtor must prove that:
 - aa. They cannot maintain, based on current income and expenses, a “minimal” standard

of living for themselves and their dependents if forced to repay the loans;

- bb. Additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment period of the student loans; and
- cc. They have made a good faith effort to repay the loans

2. *In re Long*, 322 F.3d 549, 554 (8th Cir. 2003)

- a. Totality of Circumstances Test (Minority Rule)
 - i. 8th Cir. (*Long*)
- b. Standard
 - i. Bankruptcy Court should consider:
 - aa. Debtor's past, present, and reasonably reliable future financial resources;
 - bb. A calculation of the debtor's and debtor's dependents reasonable necessary living expenses; and
 - cc. Any other relevant facts and circumstances surrounding each particular bankruptcy case

3. Unclear – No Circuit-Level Authority

- a. 1st Cir. – Likely Totality of Circumstances
 - i. *In re Bronsdon*, 435 B.R. 791, 800 (B.A.P. 1st Cir. 2010) (adopting Totality of Circumstances test)
- b. D.C. Cir. – Likely *Brunner*

- i. *In re Zook*, 2009 WL 512436, *1 (Bankr. D.C. Cir. Feb. 27, 2009) (adopting *Brunner* test)
4. Practically speaking, there isn't much difference between the *Brunner* and Totality of the Circumstances tests

III. Process

A. Provision of Debtor's Student Loan Record

1. DOE will provide DOJ with its record of the debtor's account history, loan details, and – where available – educational history. DOJ will share this record with Debtor/Plaintiff.
 - a. Not clear how quickly this will occur

B. Submission of Attestation

1. Attestation form is Appendix A to Guidance
2. Requires detailed information about debtor's current income and expenses, employment status, future (in)ability to repay student loans, prior efforts to repay loans, current assets, and any additional relevant circumstances
3. Contemplates corroborating documentation, such as tax returns, paystubs, Sch. I and J and/or Forms 122A-2 and 122C-2 (Means Test) filed in bankruptcy case. DOJ may request additional evidence where necessary to support debtor's representations in the Attestation

C. DOE/DOJ Consultation

1. DOJ and DOE confer regarding debtor's attestation and supporting materials

D. DOJ and Debtor/Plaintiff Meet and Confer

E. Stipulation and Recommendation of Full or Partial Discharge

1. Where the DOJ/DOE are satisfied that the Debtor/Plaintiff can establish that repayment of all or part of their student loans will cause them and their dependents undue hardship, the parties should stipulate to such facts and make a recommendation to the bankruptcy court in support of a judgment discharging the student loans in whole or in part
2. Stipulation/Recommendation are not binding on the court.
 - a. What standards or procedural rules might the court apply in considering such a stipulation?

IV. Relationship Between Guidance and Applicable Law

A. Present Circumstances

1. *Brunner*/Totality of the Circumstances
 - a. No uniform standards for allowable expenses
 - b. Often leads to intrusive discovery concerning discretionary spending, such as restaurant meals, alcohol, internet, streaming services, etc.
 - c. DOJ/DOE typically argue repayment should be based on Income-Driven Repayment
2. Guidance
 - a. Relies in part on the IRS Collection Financial Standards¹ to determine the debtor's allowable expenses
 - i. National IRS Standards – same dollar amounts as used in Means Test
 - ii. IRS Local Standards – debtors are limited to actual expense, with IRS Local Standards serving as a cap

¹ <https://www.irs.gov/businesses/small-businesses-self-employed/collection-financial-standards>.

- b. Whether IRS National or Local Standards are applied, Guidance instructs DOJ/DOE to consider *and accept* a debtor's reasonable explanation where their actual expenses exceed what the relevant Standard provides
- c. Guidance requires consideration of Other Necessary Expenses, in addition to the National or Local Standard expenses, where they are consistent with a "minimal standard of living" and necessary and reasonable in amount. Other Necessary Expenses can include baby-sitting/child care, preschool costs, alimony and/or child support payments
- d. Guidance requires consideration of expenses for unmet needs. E.g., Where a debtor lives with relatives or in substandard housing or forgoes spending on healthcare, expenses for better housing and healthcare can be added to the Attestation
 - i. Guidance states: "Unless the amount of the projected expenses exceeds the IRS Local Standards, it is not necessary to probe the debtor's calculation"
- e. Comparing Expense with Debtor's Gross Income
 - i. Gross Income includes Social Security and unemployment benefits
 - ii. Guidance requires DOJ/DOE to calculate student loan payments under "standard" repayment plan, rather than income-driven repayment plans
 - iii. If debtor's reasonable expenses exceed their income, Guidance instructs DOJ/DOE to find no present ability to repay student loans
 - iv. If debtor's income permits standard student loan repayment, Guidance does not require a recommendation in favor of full or partial discharge

- v. Where a debtor's income allows for partial monthly payments, Guidance instructs DOJ/DOE to consider recommending a partial discharge

B. Future Circumstances

1. *Brunner*/Totality of the Circumstances

- a. Requires debtors to somehow prove that their financial future will always be as hopeless as it currently is
- b. DOJ/DOE typically argue that debtors must prove that inability to repay will persist longer than loan repayment period, which can be 20-25 years under income-driven repayment plans

2. Guidance

- a. Applies a rebuttable presumption that a debtor's inability to repay will persist in certain circumstances, including:
 - i. Debtor is age 65 or older
 - ii. Debtor has a disability or chronic injury impacting their income potential
 - iii. Debtor has been unemployed for at least 5 of the last 10 years
 - iv. Debtor has failed to obtain the degree for which they procured the loan
 - v. Student loan has been in payment status other than "in-school" for at least 10 years
- b. Foregoing list is non-exclusive
- c. Other circumstances justifying a finding of future inability to repay might include, for example, a prolonged history of unemployment that differs from that

described above; a degree from an institution that has closed, where that closure has negatively impacted or inhibited a debtor's future earning capacity

- d. Rebuttal of the presumption of persistent inability to repay must be based on “concrete factual circumstances”, not simply conjecture

C. Good Faith

1. *Brunner*/Totality of the Circumstances

- a. Requires evidence of loan repayment history and efforts to obtain employment and maximize income
- b. DOJ/DOE have frequently argued that participation in income-driven repayment plan is required to show good faith
- c. Akin to a “morality test” that calls debtor's life choices – having children, serving as caregiver to a family member – into question

2. Guidance

- a. Reminds DOJ/DOE that good faith should not be used as a means to impose their own values on debtors' life choices
- b. Focuses on objective factors, such as:
 - i. Making a payment
 - ii. Applying for deferment or forbearance (other than in-school or grace period deferments)
 - iii. Applying for an income-driven repayment plan
 - iv. Applying for a federal consolidation loan

- v. Responding to outreach from a servicer or collector
 - vi. Engaging meaningfully with DOE or its loan servicer regarding payment options, forbearance and deferment options, or loan consolidation
 - vii. Engaging meaningfully with a third party they believed would assist them in managing their student loan debt
- c. Debtor's efforts to obtain employment, maximize income, and minimize expenses must be considered
 - i. Per the Guidance, "[a] debtor has minimized expenses if their expenses fall within the IRS Standards"
- d. Good faith can be found where a debtor's personal or family obligations significantly reduce their employment opportunities or increase their expenses
- e. Guidance expressly acknowledges that administrative errors and dissemination of confusing and inaccurate information by student loan servicers might have given rise to a lack of trust and caused debtors to avoid meaningful engagement with the repayment process and repayment options
 - i. Guidance instructs DOE/DOJ to "give significant weight to the fact that . . . [DOE] has found widespread problems with income-driven repayment plan servicing
 - ii. The fact that a debtor did not enroll in an income-driven repayment plan does not control the good faith inquiry, and should be considered in context of debtor's explanation for non-enrollment

- iii. Per Guidance, acceptable explanations of non-enrollment include, but are not limited to:
 - aa. Debtor was denied access to, or diverted or discouraged from using an income-driven repayment plan, and instead relied on forbearance or deferment
 - bb. Debtor received inaccurate, incomprehensible, or incomplete information about the merits of an income-driven repayment plan
 - cc. Debtor had a plausible belief that an income-driven repayment plan would not have meaningfully improved their financial situation
 - dd. Debtor was unaware, after reasonable engagement, of availability or benefit of an income-driven repayment option
 - ee. Where permitted under applicable law, Debtor was concerned about the potential tax consequences of loan forgiveness at the conclusion of an income-driven repayment plan
- iv. Per Guidance, where a debtor's explanation of non-enrollment is based in part on contact or attempted contact with DOE, student loan servicers, or trusted third parties, such explanation constitutes evidence of good faith
- v. Per Guidance, "we would expect [DOJ] not to oppose discharge for lack of good faith where there is a basis to conclude that the debtors . . . non-enrollment was not a willful attempt to avoid repayment"

- f. Guidance instructs DOE/DOJ to look at the entire life of the loan rather than just its recent history

D. Debtor's Assets

- 1. A debtor's assets must be considered, but Guidance instructs DOJ/DOE not to give dispositive weight to assets that are not easily converted to cash or that are otherwise critical to the debtor's well-being
 - a. Some assets, such as residential real property or retirement accounts may be exempt from collection under state law, and although that fact is not dispositive, the Guidance "recognizes that liquidating a primary residence or retirement account is an extreme measure . . . [and] requests to liquidate those assets should be exceptionally rare"

V. Full v. Partial Discharge

- A. Where applicable law permits partial discharge, and where DOE/DOJ conclude that a debtor has the ability to make some payment on student loans while maintaining a minimal standard of living consistent with the Guidance or where a debtor has the ability to liquidate assets to pay a portion of their student loan debt but remains unable to pay the balance, the Guidance encourages DOE/DOJ to recommend partial discharge
- B. Caveats
 - 1. Partial Discharge should not result in a remaining (non-discharged) balance larger than what the debtor's discretionary income permits them to pay off in monthly payments over the remaining term of the loan
 - 2. Avoid conditional discharges, where debt springs back if payments aren't made

VI. Impact of Guidance on FRCP/FRBP Deadlines

A. Relevant Deadlines

1. FRBP 7012(a)
 - a. United States must answer or otherwise respond to a complaint within 35 days after issuance of the summons
2. FRCP 16(b)(2)/FRBP 7016(a)
 - a. Requires court to issue a scheduling order “as soon as practicable, but unless the judge finds good cause for delay, the judge must issue it withing the earlier of 90 days after any defendant has been served with the complaint or 60 days after any defendant has appeared”
3. FRCP 26(f)(1)/FRBP 7026
 - a. Requires the parties to an adversary proceeding to convene their discovery conference at least 21 days prior to an initial scheduling conference or a scheduling order is due under FRCP 16(b)/FRBP 7016
 - b. Parties must discuss the issues set forth in FRCP 26(f)(2) and develop a discovery plan
4. FRCP 26(f)(2)/FRBP 7026
 - a. Parties must submit their discovery plan to the court within 14 days after conducting their discovery conference
5. FRCP 26(a)(1)(C)/FRBP 7026
 - a. Parties must exchange the material described in FRCP 26(a)(1)(A) within 14 days after conducting their discovery conference

B. Impact of Guidance on Deadlines

1. Given the amount of material the Guidance requires the parties to exchange, the need to consultation between DOJ and DOE, the need for DOJ and the Debtor/Plaintiff to meet and confer regarding the Attestation and issues addressed therein – none of which can happen until the debtor commences an adversary proceeding and properly serves DOE with process – courts and litigants should consider extending the foregoing deadlines
2. Benefits the court by avoiding a significant investment of resources in a proceeding that might be amicably resolved through the process contemplated in the Guidance
3. Benefits the parties by allowing them to focus their resources on trying to resolve the proceeding without expensive formal discovery and other work that might be rendered unnecessary if the proceeding is resolved per the Guidance

C. Approaches

1. Court could adopt Local Rule(s) or Procedures to facilitate the process contemplated by the Guidance
 - a. Bankr. N.D. Cal. Guidelines and Forms
 - i. After filing of complaint and service of process in compliance with FRBP(b)(5), parties complete and file a Stipulation that:
 - aa. Extends the deadline by which DOE must answer or otherwise respond to the complaint by 120 days;
 - bb. Continues the initial scheduling conference to a date no sooner than 60 days after DOE's extended responsive pleading deadline;
 - cc. Instructs the parties to calculate the deadlines set forth in FRCP 26(a)(1)(C)

(exchange of initial disclosures), 26(f)(1) (conduct discovery conference), and 26(f)(2) (file discovery plan) from the date of the continued scheduling conference; and

dd. Incorporates a finding that good cause justifies a delay in issuing a scheduling order beyond the deadline set forth in FRCP 16(b)(2)

- b. Parties upload an order approving the Stipulation, which triggers chambers' review of the Stipulation and order
- c. If the parties are able to resolve the proceeding via the Guidance, they shall upload a Stipulated Judgment discharging the student loans in whole or in part
- d. If no resolution is reached, then the action proceeds in accordance with the Stipulation

2. Other jurisdictions

- a. Could use this Stipulation and Order process even in the absence of official court procedures or rules

D. Guidance Does Not Impact Court's Authority

- 1. The Guidance instructs DOJ to "advise debtors that although [DOJ/DOE] may stipulate to facts relevant to undue hardship and recommend to the . . . court that a finding of undue hardship is appropriate," such stipulation or recommendation does not bind the court, "which will render its own determination whether a debtor has met the standard for an undue hardship discharge."

VII. Best Practices and Pitfalls

- A. Intake Forms
- B. Pre-Filing Considerations and Other Information for Case Evaluation
 - 1. Clients should get a complete list of their federal student loans by viewing their National Student Loan Data System (“NSLDS”) report (available at <http://studentaid.gov>) using their FSA ID
 - 2. Attorneys can get an estimate of the standard repayment amount on a student loan by using the Loan Simulator on the Federal Student Aid website (<http://studentaid.gov/loansimulator/>)
 - 3. Timing issues related to presumptions and objective factors
- C. Practical Pointers
 - 1. Attestation
 - a. Send the attestation directly to DOJ; do not file it with the court to avoid publication of PII
 - b. The attestation must be complete; where a case presents a close call on dischargeability, provide an explanation in support of dischargeability
 - c. Respond promptly to follow-up requests for documentation or clarification
 - 2. Different loans might yield different outcomes
 - a. E.g., a borrower might have both an undergraduate loan that has been in repayment for more than 10 years (meeting one of the second prong presumptions) and a graduate or Parent PLUS loan that has been in repayment for only 5 years. DOE and DOJ will consider each loan

individually and may make different recommendations under the Guidance as to each loan

3. Borrower defense to repayment might be a better outcome for many borrowers because it provides a refund of qualifying payments and restores Pell eligibility
4. Debtors in cases under Chapter 13 are eligible for consideration under the Guidance. Where DOJ/DOE and the debtor reach agreement as to a full or partial discharge of student loans, the government will amend its proof of claim accordingly. Discharge will not become effective unless/until the debtor completes payments under their confirmed plan
5. Cases with no prong two presumption can still be discharged, so long as the debtor provides a clear and well-documented explanation about why prong two is satisfied
 - a. Status of occupational licenses and future ability to obtain such a license is difficult for DOE/DOJ to independently evaluate. Be clear about whether the debtor can and intends to be licensed in a specific field or if the debtor is prohibited from obtaining such a license for some reason. Be sure to note other considerations for obtaining employment in the relevant field, such as the impact of a criminal record or a medical condition
 - b. Not working “in your field” is not a presumption, but is helpful information. In such a situation, it is critical that a debtor with an advanced degree or a certificate from a program aimed at obtaining a specific job explain their predicament
6. For the third prong, every action taken by the debtor regarding engagement with and repayment of their loans is important. While most cases will meet all three prongs under the Guidance, caselaw in many jurisdictions could require an analysis of the debtor’s efforts to maximize income and minimize expenses if the dischargeability action goes to trial

D. Consideration of nonbankruptcy discharge options

E. Alternatives/Strategies if settlement not reached

VIII. Future Application of Guidance Under New Administration?