Bankruptcy as Consumer Protection: The Case of Student Loans

John Patrick Hunt*

ABSTRACT

Over 300,000 student loan borrowers have applied to the Department of Education for administrative relief from federal student loans on the ground that they were deceived or otherwise victimized by their schools. The Department adopted relatively borrower-friendly rules for this process in 2016. But under Secretary DeVos, the Department changed course and adopted new rules that make it "nearly impossible" for student borrowers to prevail. After a presidential veto of a resolution that would have stopped the new rules, they went into effect on July 1, 2020.

With victimized students effectively deprived of administrative relief, bankruptcy provides at least a partial solution. Many such borrowers will be candidates for bankruptcy: The median loan default rate at for-profit colleges sued or investigated for wrongdoing against students is estimated at thirty-one percent.

To get bankruptcy relief, a debtor must show that repayment would cause "undue hardship." Courts currently do not consider school wrongdoing in assessing undue hardship; this article argues that they should. When repayment will entail some hardship and the borrower's decision to incur the student loan was induced by the school's deceptive representations or unfair, abusive, or unconscionable practices, bankruptcy courts should provide relief. They should discharge at least the amount of the loan corresponding to the difference between the cost of the schooling and any value the loan holder can prove the education actually had.

Considering school misconduct is consistent with the policies underlying nondischargeability of student loan debt because victimized students are not abusing the system when they seek relief and because collection from them is

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* Professor of Law and Martin Luther King, Jr. Research Scholar, University of California, Davis School of Law (King Hall), jphunt@ucdavis.edu. Thanks to King Hall Dean Kevin Johnson and Senior Associate Dean for Academic Affairs Afra Afsharipour for financial support. Thanks also to Katherine Florey and Jasmine Harris for helpful comments and insights. For research assistance, thanks to Gavin Ralphs, Jee Whan (James) Youn, and the Mabie Law Library staff.

unlikely to be cost-effective. Moreover, discharge advances the goals of the student loan program.

It might be objected that the federal government is not itself a wrongdoer in school-misconduct cases, so it should not bear losses arising from bankruptcy discharge of federal student loans. But the FTC's Holder Rule has provided since 1976 that consumer lenders are responsible for sellers' misconduct in analogous situations. The assumptions underlying the Holder Rule are met in student-loan cases. As between the two innocent parties, government and student, the government is better able to absorb school-misconduct losses. The government is also better situated to prevent such losses due to its extensive supervisory powers over schools.

INTRODUCTION

American postsecondary education has a consumer protection problem. More specifically, American for-profit postsecondary education has a problem. Company after company in the sector—Trump University,[1] FastTrain College,[2] Corinthian Colleges,[3] ITT Technical Institutes,[4] Alta Colleges (Westwood),[5] Education Management Corporation (Argosy

1. *See* Tom Winter & Dartunorro Clark, *Federal Court Approves $25 Million Trump University Settlement*, NBC NEWS (Feb. 6, 2018, 1:49 PM), https://www.nbcnews.com/politics/white-house/federal-court-approves-25-million-trump-university-settlement-n845181 [https://perma.cc/5B3V-NZD3].

2. *See* Michael Vasquez, *FastTrain College Owner Convicted of Theft, Conspiracy*, MIA. HERALD (Nov. 25, 2015, 11:32 AM), https://www.miamiherald.com/news/local/education/article46253760.html [https://perma.cc/VG6Z-E9CP].

3. *See* discussion *infra* Part II.A.

4. *See* discussion *infra* Part II.A.

5. *See* Ashley A. Smith, *Fall of a For-Profit*, INSIDE HIGHER ED (Dec. 8, 2015), https://www.insidehighered.com/news/2015/12/08/profit-westwood-college-wont-accept-new-students [https://perma.cc/7Y4S-N7T2].

University, Art Institutes),[6] Education Corporation of America[7]—has fallen amid investigations into and lawsuits over deceptive and unfair practices in recruiting and lending. Over 300,000 student borrowers[8]—98.6% of them from for-profit schools[9]—have filed applications to discharge their loans based on school wrongdoing.

In recent years, the Department of Education made the problem worse. Under Secretary Betsy DeVos, it dismantled the team investigating fraud against students[10] and rolled back protections for student borrowers inherited from the previous administration.[11]

The Department had taken a step in the direction of consumer protection in 2016. That year, it adopted a new borrower defense rule for administrative discharge of federal student loans based on school misconduct,[12] one that featured relatively generous substantive terms for relief and that provided a new process under which groups of similar claims could be processed together.[13]

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6. *See* Danielle Douglas-Gabriel, *Argosy University Closes Its Doors; Students Scramble To Transfer*, WASH. POST (Mar. 10, 2019, 1:14 PM), https://www.washingtonpost.com/education/2019/03/09/argosy-university-closes-its-doors-students-scramble-transfer/ [https://perma.cc/8TEY-MEUL]; Annie Nova, *His Two Year Degree Cost Him $90,000. Now He's in a Battle with the Education Department*, CNBC (Apr. 11, 2019, 7:33 AM), https://www.cnbc.com/2018/06/22/thousands-of-students-who-say-they-were-defrauded-by-the-art-institute-awaiting-an-answer-from-the-government--.html [https://perma.cc/R2MN-SRRL].

7. *See* Yan Cao, *How Betsy DeVos Got Schooled by the Education Corporation of America*, CENTURY FOUND. (Dec. 14, 2018), https://tcf.org/content/commentary/betsy-devos-got-schooled-education-corporation-america/ [https://perma.cc/TGW7-UQ26].

8. *See* FED. STUDENT AID, BORROWER DEFENSE—MONTHLY REPORT—FOR MONTH END 5/31/2020 (2020), https://studentaid.gov/data-center/student/loan-forgiveness/borrower-defense-data [https://perma.cc/8X4B-RDBP] (select the "May 2020" report). The author recognizes that not all student loan borrowers are students (some are parents, for example) but uses the term "student borrowers" for economy.

9. Yan Cao & Tariq Habash, *College Complaints Unmasked*, CENTURY FOUND. (Nov. 8, 2017), https://tcf.org/content/report/college-complaints-unmasked/ [https://perma.cc/4TVA-8PJ4] (reporting data through August 15, 2017).

10. *See* Danielle Ivory et al., *Education Department Unwinds Unit Investigating Fraud at For-Profits*, N.Y. TIMES (May 13, 2018), https://www.nytimes.com/2018/05/13/business/education-department-for-profit-colleges.html [https://perma.cc/H9AH-ECFV].

11. *See* Danielle Douglas-Gabriel, *DeVos Dials Back Consumer Protections for Student Loan Borrowers*, WASH. POST (Apr. 11, 2017, 1:30 PM), https://www.washingtonpost.com/news/grade-point/wp/2017/04/11/devos-dials-back-consumer-protections-for-student-loan-borrowers/ [https://perma.cc/Z822-YVMN].

12. *See* Student Assistance General Provisions, 81 Fed. Reg. 75,926, 75,926 (Nov. 1, 2016) (to be codified at 34 C.F.R. pt. 30, 668, 674, 682, 685, 686). To save space, where a Federal Register entry title references multiple subjects, the entry is cited using only the first named subject.

13. *See* discussion *infra* Part II.C.

Upon taking power, the DeVos administration sought to do away with the 2016 rule. It first delayed the rule's implementation and eventually, in September 2019, replaced it altogether.[14] The new rule[15] imposed a test for discharge that one observer aptly called "nearly impossible" for borrowers to meet.[16] After President Trump vetoed a joint resolution that would have stopped the DeVos rules,[17] they went into effect on July 1, 2020.[18]

Bankruptcy law can, at least in part, fill the consumer-protection gap created by the new borrower defense rule. Bankruptcy provides relief from student loans, but only if the borrower shows that repayment would cause "undue hardship."[19] In applying this standard, courts generally have not taken school misconduct[20] into account.[21]

This article makes a specific proposal for considering school wrongdoing in assessing undue hardship. It argues that when a school induces a borrower to enroll and borrow money through deceptive or unfair acts or practices, the resulting loan should be dischargeable in bankruptcy, as long as the borrower can show that repayment involves some degree of hardship, that is, difficulty in repaying.[22]

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14. *See* Stacy Cowley, *DeVos Toughens Rules for Student Borrowers Bilked by Colleges*, N.Y. TIMES (May 20, 2020), https://www.nytimes.com/2019/08/30/business/betsy-devos-student-loan-forgiveness.html [https://perma.cc/8TJE-V9JV].

15. *See* discussion *infra* Part II.C.

16. Kery Murakami, *Borrower-Defense Veto Override Fails*, INSIDE HIGHER ED (June 29, 2020), https://www.insidehighered.com/quicktakes/2020/06/29/borrower-defense-veto-override-fails [https://perma.cc/H8BP-GDD9] (quoting Eileen Connor, Legal Director, Harvard Law School Project on Predatory Student Lending).

17. *See* Danielle Douglas-Gabriel, *Trump Stands with DeVos, Vetoes Measure To Overturn Her Controversial Student Loan Forgiveness Rule*, WASH. POST (May 29, 2020, 4:47 PM), https://www.washingtonpost.com/education/2020/05/29/trump-stands-with-devos-vetoes-bill-overturn-her-controversial-student-loan-forgiveness-rule/ [https://perma.cc/FN2Z-7A7J].

18. Student Assistance General Provisions, 84 Fed. Reg. 49,788, 49,788 (Sept. 23, 2019) (to be codified at 34 C.F.R. pt. 668, 682, 685) (providing for July 1, 2020 effective date).

19. *See* 11 U.S.C. § 523(a)(8) (providing student loans are nondischargeable absent a showing of "undue hardship").

20. The article uses the terms "misconduct" and "wrongdoing" to refer to the deceptive, unfair, abusive, and unconscionable acts and practices that the proposal in Part III.A covers. The author recognizes that it may be debatable whether each and every act or practice the proposal covers is wrongful but believes the terms the article uses fairly characterize most of the conduct the proposal addresses. A similar observation applies to the article's use of "victimized borrowers" to describe those affected by the practices covered by Part III.A.

21. *See* discussion *infra* Part III.B.

22. *See* discussion *infra* Part III.A.

Although bankruptcy is not a complete solution, it does address some of the worst aspects of the problem of student debt, the economic,[23] racial justice,[24] and personal[25] dimensions of which are increasingly well documented. Debt outcomes at for-profit schools that have been sued or investigated for consumer-protection violations are abysmal,[26] even worse than those for the troubled for-profit sector overall.[27] Some for-profit schools stand accused not just of practicing deceptive and unfair tactics but also of

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23. Student loans have been found to be associated with many negative effects, including "lower post-graduation income; lower future net worth (with net worth calculated excluding the student loans) and satisfaction with personal finances; lower probability of owning a house or car . . . ; a higher risk of experiencing future financial difficulties; and a lower probability of pursuing future education." John Patrick Hunt, *Tempering Bankruptcy Nondischargeability To Promote the Purposes of Student Loans*, 72 SMU L. REV. 725, 759–60 (2019) (footnotes omitted) (citing studies). Student loan debt also has been linked to falling small-business formation and lower retirement savings. *See* Christopher Ingraham, *7 Ways $1.6 Trillion in Student Loan Debt Affects the U.S. Economy*, WASH. POST (June 25, 2019, 7:24 AM), https://www.washingtonpost.com/business/2019/06/25/heres-what-trillion-student-loan-debt-is-doing-us-economy/ [https://perma.cc/3FKK-WHMZ].

24. Professors Dalié Jiménez and Jonathan Glater report that

> Black students are disproportionately likely to borrow, to borrow larger amounts, to take out student loans to attend for-profit schools with worse career outcomes, and to default on their loans relative to their White peers. Latinx students are less likely to borrow than White students but when they do, they borrow nearly as much, and like Black students are more likely to attend a for-profit institution and more likely to default than White students.

Dalié Jiménez & Jonathan D. Glater, *Student Debt Is a Civil Rights Issue: The Case for Debt Relief and Higher Education Reform*, 55 HARV. C.R.-C.L. L. REV. 131, 132–33 (2020) (footnotes omitted) (citing studies). Recent research from the Student Borrower Protection Center reports that negative student debt outcomes in several major cities are concentrated in areas with high Black and Latinx populations. *See* STUDENT BORROWER PROT. CTR., DISPARATE DEBTS: HOW STUDENT LOANS DRIVE RACIAL INEQUALITY ACROSS AMERICAN CITIES 9 (2020), https://protectborrowers.org/wp-content/uploads/2020/06/SBPC-Disparate-Debts.pdf [https://perma.cc/879L-ZH8N].

25. *See* Thomas Richardson et al., *The Relationship Between Personal Unsecured Debt and Mental and Physical Health: A Systematic Review and Meta-Analysis*, 33 CLINICAL PSYCH. REV. 1148, 1153 (2013) (reporting that meta-analysis of sixty-five studies covering 34,000 people revealed "a statistically significant relationship between debt and presence of a mental disorder, depression, . . . suicide completion or attempt, problem drinking, drug dependence, neurotic disorders . . . and psychotic disorders"); Hunt, *supra* note 23, at 759–60 (reporting other personal harms arising from student loans).

26. *See infra* notes 439–440 and accompanying text (reporting median student loan default rate of thirty-one percent and median loan distress rate of fifty percent at such schools).

27. On issues with the for-profit sector generally, see Jonathan D. Glater, *To the Rich Go the Spoils: Merit, Money, and Access to Higher Education*, 43 J. COLL. & U.L. 195, 203 (2017) (footnotes omitted) (reporting that for-profit institutions have "lower rates of completion, higher levels of undergraduate student indebtedness and higher rates of student loan default"); *see also* Matthew Adam Bruckner, *Higher Ed "Do Not Resuscitate" Orders*, 106 KY. L.J. 223, 237 (2017).

aiming those tactics at prospective students who are low income, Black, Latinx, or veterans.[28] Relieving borrowers who were targeted because of perceived vulnerability and induced to sign up for loans through trickery is even more urgent than helping other borrowers whose loans are causing them equal hardship.

Scholars have studied the bankruptcy[29] and consumer-protection[30] aspects of the student loan problem but generally have not addressed bankruptcy relief as a consumer-protection solution. An important exception is that Professors Dalié Jiménez and Jonathan Glater argue briefly in their study of student debt as a civil rights issue that in some jurisdictions bankruptcy courts can properly consider exploitative misconduct by schools or servicers in deciding whether a borrower has suffered undue hardship.[31]

This article extends and expands upon that proposal. It is the first to develop at length the proposition that bankruptcy courts in all jurisdictions properly can consider schools' misconduct toward students in deciding whether to discharge student debt. In doing so, the article presents new

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28. *See* discussion *infra* note 187 and accompanying text.

29. *See, e.g.*, John Patrick Hunt, *Student Loan Purpose and the* Brunner *Test*, HARV. L. & POL'Y REV. (forthcoming 2020) (manuscript at 1), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3536649 [https://perma.cc/5XLC-QS52] [hereinafter Hunt, *Purpose*]; Jiménez & Glater, *supra* note 24; Matthew Bruckner et al., *A No-Contest Discharge for Uncollectible Student Loans*, 91 U. COLO. L. REV. 183, 183 (2020); Hunt, *supra* note 23; Dalié Jiménez et al., *Comments of Bankruptcy Scholars on Evaluating Hardship Claims in Bankruptcy*, 21 J. CONSUMER & COM. L. 114, 115 (2018); John Patrick Hunt, *Help or Hardship?: Income-Driven Repayment in Student-Loan Bankruptcies*, 106 GEO. L.J. 1287, 1287 (2018) [hereinafter Hunt, *Help*]; Rafael I. Pardo, *Taking Bankruptcy Rights Seriously*, 91 WASH. L. REV. 1115 (2016).

30. *See, e.g.*, John R. Brooks & Adam J. Levitin, *Redesigning Education Finance: How Student Loans Outgrew the "Debt" Paradigm*, 109 GEO. L.J. 5, 48–58 (2020) (describing consumer-protection problems with student loan servicing); Camilla E. Watson, *Federal Financing of Higher Education at a Crossroads: The Evolution of the Student Loan Debt Crisis and the Reauthorization of the Higher Education Act of 1965*, 2019 MICH. ST. L. REV. 883, 934–40, 953–61 (describing the borrower defense rule and problems of predatory lenders and for-profit colleges); Jacob Hale Russell, *Unconscionability's Greatly Exaggerated Death*, 53 U.C. DAVIS L. REV. 965, 1013–14 (2019) (considering student loan consumer protection through contract law's unconscionability doctrine); David L. Noll, *Deregulating Arbitration*, 30 LOY. CONSUMER L. REV. 51, 64–66 (2017) (discussing the borrower defense rule's arbitration provisions); William J. Cox, *The Student Borrower: Slave to the Servicer?*, 27 LOY. CONSUMER L. REV. 189, 189–201 (2015) (discussing consumer-protection problems with student loan servicing). Many of these works address the very real consumer-protection issues with student loan servicing; this article does not discuss servicing issues for reasons of space.

31. *See* Jiménez & Glater, *supra* note 24, at 186.

evidence on the meaning of "undue hardship" in the Bankruptcy Code[32] as well as novel arguments based on bankruptcy[33] and consumer-law policy.[34]

The article also contributes to the debate about the importance of bankruptcy in an era of income-driven repayment ("IDR"). Most federal student loan borrowers can choose to make payments based on their income,[35] and this choice can provide substantial relief to low-income borrowers relative to plans that call for repayment of the entire loan principal and interest over a fixed period of time.[36] Thus, there is an argument that IDR reduces the importance of bankruptcy, as Professors John Brooks and Adam Levitin have recently emphasized.[37] But bankruptcy serves a consumer-protection function that IDR does not. A student induced to take out loans by deceptive or unfair practices arguably should not have to make IDR payments, even if they are affordable. IDR does not consider the merits of the student borrower's debt, but bankruptcy can.

The article begins by addressing the meaning of "undue hardship" in the Bankruptcy Code. Part I demonstrates, using evidence from contemporary dictionaries, the use of the term "undue hardship" in eight other federal law contexts, and the legislative history of the student loan undue-hardship provision, that the phrase should be understood as "unjustifiable hardship."[38] The statutory term does not mean, as some courts have stated, "unusual hardship."[39] The broad understanding of "undue hardship" advanced in Part I sets up the argument that the fairness with which a student loan was originated is relevant in evaluating "undue hardship."

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32. *See* discussion *infra* Part I.

33. *See* discussion *infra* Part III.B.

34. *See* discussion *infra* Part III.C.

35. *See Income-Driven Repayment Plans*, FED. STUDENT AID, https://studentaid.gov/manage-loans/repayment/plans/income-driven [https://perma.cc/R4YT-8HHR].

36. The author's calculations indicate that for an undergraduate borrower with an average federal loan balance (approximately $36,500) and an income of $20,000, the IDR payment would be over $4,000 less than the amount needed to repay an initial balance of $36,500 under the standard plan. At an income of $50,000, IDR payments are still over $1,000 less than standard payments. Sources and calculations on file with author.

37. They argue that under a reconceptualized, expanded, and reformed IDR program, "the anomalous and notoriously uncharitable treatment of student loans in bankruptcy would cease to be an issue." Brooks & Levitin, *supra* note 30, at 12. This author supports Brooks and Levitin's insightful proposal to reconceptualize student loans as something more akin to grants coupled with a tax surcharge, but notes, as Brooks and Levitin themselves do, that fully realizing this reconceptualization would entail significant changes to the existing student loan programs. *See Id.* at 73–79 (outlining changes needed to implement Brooks & Levitin's reconceptualization).

38. *See* discussion *infra* Parts I.B–I.D.

39. *See* discussion *infra* Part I.

Part II gives background on findings and allegations of school misconduct, including false placement statistics and misrepresentations of programs' accreditation and the transferability of credits.[40] It also traces the history of the borrower defense rule, from its origin in 1994, to the major changes the Obama administration adopted in 2016 in response to the collapse of Corinthian Colleges, to the litigation over those rules and their ultimate replacement in 2019.[41] Part II also covers the major substantive provisions of the 2016 and 2019 rules.[42]

Part III presents and defends the article's proposal for taking account of school misconduct in student loan bankruptcies: Provided hardship is shown, a borrower who was induced to enroll through deceptive or unfair tactics should be able to discharge loans at least corresponding to the difference between the cost of the schooling and the value actually received and arguably should be able to discharge all loans induced through school misconduct.[43]

The fundamental point is simple and intuitive: It is more unfair, and therefore less justifiable, to demand repayment of a borrower who was victimized in connection with taking out the loan than it is to expect repayment from a borrower suffering equal hardship who was not victimized.[44] Granting relief to victimized borrowers is consistent with the policies underlying loan dischargeability and actively promotes the legislative policies underlying the student loan programs.[45] Moreover, taking account of school misconduct in deciding whether student debts are nondischargeable is consistent with how courts apply other nondischargeability provisions.[46] Finally, the article's proposal is generally consistent with existing doctrinal tests for undue hardship, although the majority *Brunner* test may obstruct implementation of the proposal somewhat unless the test is leniently interpreted.[47]

The creditor in a student loan bankruptcy is usually the federal government and not the school.[48] The government thus is usually the party that suffers any

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40. *See* discussion *infra* Part II.A.
41. *See* discussion *infra* Part II.B.
42. *See* discussion *infra* Part II.C.
43. *See* discussion *infra* Part III.A.
44. *See* discussion *infra* Part III.B.1.
45. *See* discussion *infra* Part III.B.2.
46. *See* discussion *infra* Part III.B.3.
47. *See* discussion *infra* Part III.B.4.
48. This article focuses primarily on federal direct student loans. After discontinuation of the Federal Family Education Loan program in 2010 and of the Perkins loan program in 2017, the direct loan program is now the only major postsecondary federal loan program. *See FFEL*

financial harm from discharge, and one might object that the government should not be held responsible for the school's wrongdoing. As Senator Lamar Alexander put it, "If your car is a lemon, you don't sue the bank—you sue the dealer."[49] But in fact you can sue the bank if the dealer refers you there. Since 1976, the Federal Trade Commission's (FTC) Holder Rule has made consumer lenders that finance sales responsible for borrower claims and defenses against sellers if the seller and lender have an affiliate or referral relationship.[50]

The Holder Rule probably does not apply to federal direct loans because the federal government is probably not a "person" covered by the FTC's enabling statute.[51] However, the assumptions underlying the rule do apply: The federal government is better positioned than individual loan borrowers both to police and to absorb losses from school misconduct, and the relationship between the school seller and the government lender is far closer than the referral relationship that would trigger the Holder Rule.[52]

The article then turns to why bankruptcy is appropriate as at least a partial solution to the problem of school wrongdoing. Bankruptcy courts routinely adjudicate consumer-protection claims, including claims of borrowers against sellers of goods or services such as schools.[53] The borrower defense rule does not itself foreclose bankruptcy discharge: The article's suggestion is consistent with the policies underlying both recent iterations of the borrower defense rule,[54] and provisions for administrative relief generally do not interfere with discharge in bankruptcy.[55] Finally, bankruptcy is likely to be an attractive solution for many victimized borrowers in light of their poor economic outlook,[56] and even financially strapped borrowers should be able

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Program Lender and Guaranty Agency Reports, FED. STUDENT AID, https://studentaid.gov/data-center/lender-guaranty [https://perma.cc/3ZLJ-MKJV]; *Perkins Loans*, FED. STUDENT AID, https://studentaid.gov/understand-aid/types/loans/perkins [https://perma.cc/7Q34-SFLQ]. Federal direct loans account for eighty-eight percent of all student loans, a category that includes state, institutional, and private loans. *See* COLL. BD., TRENDS IN STUDENT AID 2019, at 15 fig.6 (2019), https://research.collegeboard.org/pdf/trends-student-aid-2019-full-report.pdf [https://perma.cc/3F34-JFXB].

49. *See* Erica L. Green & Stacy Cowley, *Senate Rejects DeVos Rule Restricting Debt Relief for Bilked Students*, N.Y. TIMES (Mar. 11, 2020), nytimes.com/2020/03/11/us/politics/student-debt-relief-senate-devos.html [https://perma.cc/76JG-7CQP].

50. *See* discussion *infra* Part III.C.1.

51. *See* discussion *infra* Part III.C.1.

52. *See* discussion *infra* Part III.C.2.

53. *See* discussion *infra* Part IV.A.

54. *See* discussion *infra* Part IV.B.1.

55. *See* discussion *infra* Part IV.B.2.

56. *See* discussion *infra* Part IV.C.1.

to prove most types of deception and unfairness of which schools have been accused.[57]

I. "UNDUE" HARDSHIP IS UNJUSTIFIABLE HARDSHIP, NOT UNUSUAL HARDSHIP

Part I argues that the statutory command to evaluate "undue hardship" directs courts to consider whether the debtor's hardship is unjustifiable under the circumstances. It also makes the related argument that "undue" hardship need not be unusually severe. Part I.A reviews existing appellate authority on the meaning of "undue hardship." Part I.B builds on prior work in demonstrating that the ordinary meaning of "undue" is not in line with these courts' decisions. Part I.C turns to eight other places in federal law besides Section 523(a)(8) where the phrase "undue hardship" appears. In none of those eight contexts do judicial decisions or agency rules state that undue hardship is by its nature unusual. Part I.D shows that the legislative history of the provision does not undermine the conclusion that "undue" means "unjustified" and not "unusual."

A. Appellate Precedent on the Meaning of "Undue Hardship"

Understanding "undue hardship" as unjustifiable hardship is compatible with existing appellate interpretations of the term in most jurisdictions. Courts currently use one of two tests to evaluate undue hardship. The Eighth Circuit[58] and the Bankruptcy Appellate Panel in the First Circuit[59] have adopted the "totality of the circumstances" test. It calls on the court to consider "any . . . relevant facts and circumstances"[60] in making the undue-hardship determination and does not foreclose equating unjustifiable and "undue" hardship.

Nine circuits employ a second test, the *Brunner* test.[61] *Brunner* defines "undue hardship" as consisting of three elements: (1) inability to repay loans

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57. *See* discussion *infra* Part IV.C.2.

58. *See* Long v. Educ. Credit Mgmt. Corp. (*In re* Long), 322 F.3d 549, 553 (8th Cir. 2003).

59. *See* Bronsdon v. Educ. Credit Mgmt. Corp. (*In re* Bronsdon), 435 B.R. 791, 800 (B.A.P 1st Cir. 2010); *see also* Brown v. Educ. Credit Mgmt. Corp. (*In re* Brown), 581 B.R. 695, 699 (D. Me. 2017) ("Most courts in the First Circuit analyze the existence of an undue hardship under the totality of the circumstances test.").

60. *See* Educ. Credit Mgmt. Corp. v. Jesperson, 571 F.3d 775, 779 (8th Cir. 2009) (citing *In re Long*, 322 F.3d at 554).

61. *See* Letter from Lynn Mahaffie, Deputy Assistant Sec'y for Pol'y, Plan., and Innovation, Off. of Postsecondary Educ., U.S. Dep't of Educ. 16 (July 7, 2015),

while maintaining a minimal standard of living,[62] (2) that is likely to persist for a significant portion of the repayment period,[63] and (3) that is accompanied by "good faith efforts to repay the loans."[64] In most jurisdictions, the *Brunner* test also does not foreclose courts from asking whether hardship is justified because the issue can be considered in the "good faith efforts to repay" analysis. Part III.B.4 develops this argument in detail.

Five courts of appeals have, however, stated that the use of the term "undue" indicates that the debtor must show difficulties that exceed the normal hardship that typically accompanies bankruptcy. As the foundational *Brunner* opinion itself put the claim, "The existence of the adjective 'undue' indicates that Congress viewed garden-variety hardship as insufficient excuse for a discharge of student loans, but the statute otherwise gives no hint of the phrase's intended meaning."[65] The Courts of Appeals for the Fourth,[66] Fifth,[67] Seventh,[68] and Ninth[69] Circuits have explicitly adopted this interpretation. The Fourth,[70] Fifth,[71] and Ninth[72] Circuits have made explicit the view that "undue" hardship must be unusually severe relative to the hardship of other bankrupt debtors, as opposed to, for example, the hardship of all student borrowers repaying loans.

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https://ifap.ed.gov/sites/default/files/attachments/dpcletters/GEN1513.pdf [https://perma.cc/N6VL-RA4V] (citing cases adopting the *Brunner* test from the Second, Third, Fourth, Fifth, Sixth, Seventh, Ninth, Tenth, and Eleventh Circuits). Bankruptcy court decisions from the D.C. Circuit also follow the *Brunner* test. *See, e.g.*, Stout v. U.S. Dep't of Educ. (*In re* Stout), No. 08-00617, 2010 WL 3719938, at *1 (Bankr. D.D.C. Sept. 21, 2010).

62. *See* Brunner v. N.Y. State Higher Educ. Servs. Corp., 831 F.2d 395, 396 (2d Cir. 1987) ("[T]he debtor cannot maintain, based on current income and expenses, a 'minimal' standard of living for herself and her dependents if forced to repay the loans.").

63. *See id.* ("[A]dditional circumstances exist indicating that this state of affairs [i.e., a state of hardship] is likely to persist for a significant portion of the repayment period of the student loans.").

64. *See id.*

65. 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*, 831 F.2d at 399.

66. *See* Educ. Credit Mgmt. Corp. v. Frushour (*In re* Frushour), 433 F.3d 393, 399 (4th Cir. 2005) ("[T]he required hardship . . . must be more than the usual hardship that accompanies bankruptcy.").

67. *See* Thomas v. Dep't of Educ. (*In re* Thomas), 931 F.3d 449, 454 (5th Cir. 2019) ("The threshold by definition must be greater than the ordinary circumstances that might force one to seek bankruptcy relief.").

68. *See* O'Hearn v. Educ. Credit Mgmt. Corp. (*In re* O'Hearn), 339 F.3d 559, 564 (7th Cir. 2003) (finding "'garden-variety' hardship" insufficient).

69. *See* Educ. Credit Mgmt. Corp. v. Nys (*In re* Nys), 446 F.3d 938, 944 (9th Cir. 2006); Rifino v. United States (*In re* Rifino), 245 F.3d 1083, 1087 (9th Cir. 2001); United Student Aid Funds, Inc. v. Pena (*In re* Pena), 155 F.3d 1108, 1111–12 (9th Cir. 1998).

70. *See In re Frushour*, 433 F.3d at 399.

71. *See In re Thomas*, 931 F.3d at 454.

72. *See In re Rifino*, 245 F.3d at 1088–89.

To be sure, an argument can be made that the courts' statements endorsing the unusual-hardship requirement should not affect how the *Brunner* test is to be applied. The decisions indicate that the unusual-hardship idea is a reason for adopting the *Brunner* test, rather than a component of the test or a rule for applying it.[73] However, these courts' interpretation of "undue hardship" could significantly restrict the use of justifiability in the undue-hardship analysis: Their interpretation could require the debtor to show hardship that is more severe than that endured by the average bankrupt debtor, no matter how unjustified repayment might be. As the following sections demonstrate, that interpretation is wrong.

B. Ordinary Meaning of the Bankruptcy Code

The *Brunner* court and other courts adopting the unusual-hardship requirement have viewed the stricture as one imposed by the text of the statute, specifically the word "undue." Thus, this section begins by considering an important source of textual meaning: dictionary definitions.[74]

Previous work has demonstrated that dictionaries of today define "undue" as "unjustified."[75] The dictionaries do not indicate that "undue" necessarily implies "unusual," and in most cases they do not even include "unusual" as a possible meaning of "undue."[76] Some authorities suggest, however, that dictionary definitions from the time of enactment of a statute are particularly important in interpreting that statute.[77] For the undue-hardship provision, that

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73. *See* 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); *In re Frushour*, 433 F.3d at 399; *In re O'Hearn*, 339 F.3d at 564; *In re Nys*, 446 F.3d at 944; *In re Thomas*, 931 F.3d at 454. The arguments in Part I that the courts' textual claim is wrong support reevaluating *Brunner*, as this author has suggested elsewhere. *See* Hunt, *Purpose*, *supra* note 29, at 11–14.

74. 2A NORMAN SINGER & SHAMBIE SINGER, SUTHERLAND STATUTORY CONSTRUCTION § 47:28 (7th ed. 2019) ("[A]ll courts accept that standard, recognized dictionaries are a valuable source to understand a word's approved, common meaning."); BRYAN A. GARNER & ANTONIN SCALIA, READING LAW: THE INTERPRETATION OF LEGAL TEXTS 69 (2012) (arguing that judges should rely on dictionaries to determine the meaning of words).

75. *See* Hunt, *Purpose*, *supra* note 29, at 11–13.

76. *See id.*

77. *See* Food Mktg. Inst. v. Argus Leader Media, 139 S. Ct. 2356, 2363 (2019) (citing dictionaries from the time of the statute's enactment to interpret the statute); 2A SINGER & SINGER, *supra* note 74, § 47:28 ("A fundamental canon of statutory construction instructs that [unless otherwise defined] words are interpreted to take their ordinary, *contemporary*, common meaning in the absence of persuasive reasons to the contrary." (emphasis added)).

proposition directs us to dictionaries current in 1976 and 1978.[78] Those dictionaries say the same thing as contemporary ones. The *American Heritage Dictionary*,[79] *Oxford English Dictionary*,[80] *Scribner-Bantam English Dictionary*,[81] *Webster's New Collegiate Dictionary*,[82] *Webster's Seventh New Collegiate Dictionary*,[83] and *Webster's New World English Dictionary*[84] define "undue" in various ways that are based on unjustifiability and not infrequency. The same is true of *Black's Law Dictionary*.[85] Although the *American Heritage Dictionary* does give "[e]xceeding what is appropriate or normal; excessive" as one definition,[86] it gives another plausibly applicable definition that does not incorporate any idea of unusualness of infrequency.[87] Moreover, "normal" in the *American Heritage* definition seems to have a normative rather than a purely descriptive meaning.[88]

The only dictionary definition the author has located, past or present, that equates "undue" with "unusual" is the one in the current *Bouvier Law Dictionary*, which is based explicitly on a judicial interpretation of the very

78. The exception to bankruptcy dischargeability for student loans entered the law in 1976. *See* Education Amendments of 1976, Pub. L. No. 94-482, § 439(a), 90 Stat. 2081, 2141 (repealed 1978). This provision was repealed in 1978 and replaced with a substantially identical provision included in the Bankruptcy Code. *See* Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, § 523, 92 Stat. 2549, 2590–91 (codified as amended at 11 U.S.C. § 523(a)). For more discussion, see Hunt, *Help*, *supra* note 29, at 1302–07.

79. *See Undue*, AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE (William Morris ed., 1978) ("1. Exceeding what is appropriate or normal; excessive . . . . 2. Not just, proper, or legal . . . . 3. Not yet payable or due.").

80. *See Undue,* OXFORD ENGLISH DICTIONARY (2d ed. 1989) ("1. Not properly owing or payable. 2. Not appropriate or suitable; improper . . . . 3. Not in accordance with what is just and right; unjustifiable; illegal. 4. Going beyond what is appropriate, warranted, or natural; excessive.") (citations omitted).

81. *See Undue*, SCRIBNER-BANTAM ENGLISH DICTIONARY (Edwin B. Williams ed., 1979) ("1 not yet due; 2 inappropriate; improper; 3 excessive; unwarranted").

82. *See Undue*, WEBSTER'S NEW COLLEGIATE DICTIONARY (1981) ("1: not due: not yet payable 2: exceeding or violating propriety or fitness").

83. *See Undue*, WEBSTER'S SEVENTH NEW COLLEGIATE DICTIONARY (1976) ("1: not due: not yet payable 2a: inappropriate, unsuitable b: exceeding or violating propriety or fitness").

84. *See Undue*, WEBSTER'S NEW WORLD DICTIONARY OF THE AMERICAN LANGUAGE (2d college ed. 1978) ("1. not yet due or payable, as a debt 2. not appropriate or suitable; improper 3. excessive; unreasonable; immoderate").

85. *See Undue*, BLACK'S LAW DICTIONARY (5th ed. 1979) ("More than necessary; not proper; illegal.").

86. *Undue*, *supra* note 79.

87. *See id.* ("2. Not just, proper, or legal").

88. *Normal*, AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE, *supra* note 79 ("*Normal* stresses adherence to an established level or pattern that is associated with well-being, although based on group tendencies rather than an arbitrary ideal.") (usage note).

"undue hardship" provision under discussion.[89] *Bouvier* thus provides no independent support for the view that "undue" means "unusual." Taken together, these dictionary definitions show that it is erroneous to conclude that Congress's use of the modifier "undue" meant that the hardship in question had to be greater than what is usual for bankrupt debtors.

C. "Undue Hardship" in Other Statutory Contexts

An important guide to the use of a term in a particular statutory context is its use in other contexts.[90] "Undue hardship" is used in at least eight places in federal law apart from Section 523(a)(8), including once in the Bankruptcy Code. In none of the eight contexts do courts or agency rules indicate that "undue hardship" means anything different from "unjustifiable hardship" or that "undue hardship" is inherently unusual. Indeed, in several such contexts it appears that findings of undue hardship are common.[91] Thus, these sources confirm that the decisions in *Brunner* and succeeding were incorrect in asserting that the modifier "undue" in "undue hardship" inherently requires unusually severe hardship.

The Bankruptcy Code uses the phrase "undue hardship" in one context other than student loan discharge: Reaffirmation agreements generally will not be approved if they cause the debtor "undue hardship."[92] In applying the undue-hardship test to reaffirmations, it does not appear that any court has found that the modifier "undue" means that undue hardship is inherently rare.[93] Instead, courts apparently go straightforwardly about the task of

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89. *See Undue*, BOUVIER LAW DICTIONARY (Stephen Michael Sheppard ed., 2011) ("[U]ndue hardship is hardship that is unexpected in its form or unusual in its severity in a given situation."). *Bouvier Law Dictionary* cites *In re* Gregory, 387 B.R. 182, 185 (Bankr. N.D. Ohio 2008), a case interpreting Section 523(a)(8).

90. *See* Universal Health Servs., Inc. v. United States, 136 S. Ct. 1989, 2000 n.3 (2016) (adopting interpretation of statutory term in part to foster consistency with other statutes); *accord* Gross v. FBL Fin. Servs., Inc., 557 U.S. 167, 178 n.4 (2009); 2B SINGER & SINGER, *supra* note 74, § 53:1 (advocating "[c]onstruing statutes by reference to other statutes").

91. *See generally* Ashley M. Bykerk, *Student Loan Discharge: Reevaluating Undue Hardship Under a Presumption of Consistent Usage*, 35 EMORY BANKR. DEVS. J. 509, 516–39 (2019) (examining the definition of "undue hardship" in different federal law areas).

92. *See* 11 U.S.C. § 524(c)(3)(B), (c)(6)(A)(i). On the complex rules relating to undue hardship and reaffirmation agreements, see 4 COLLIER ON BANKRUPTCY ¶ 524.04[4] (16th ed. 2020).

93. The statement in the text is based on the following two searches, conducted by the author in the Westlaw "All Federal Cases" database on May 5, 2020: First, ("undue hardship" /s reaffirm!) and (undue /p (common frequent normal commonplace everyday natural routine probable regular)); second, ("undue hardship" /s reaffirm!) and (undue /p uncommon rare infrequent unusual "garden variety").

determining whether the debtor can afford to pay the reaffirmed debt.[94] Findings that reaffirmations impose undue hardship apparently are not uncommon.[95]

Probably, the use of "undue hardship" outside the Bankruptcy Code that courts have interpreted most frequently occurs in the Americans with Disabilities Act ("ADA"). The ADA requires employers to make reasonable accommodations for individuals with disabilities unless the employer "can demonstrate that the accommodation would impose an undue hardship."[96] Neither the statutory definition of "undue hardship"[97] nor the EEOC's regulations interpreting the term[98] indicate that hardship must be unusual to be "undue." And it appears that no court has interpreted the phrase that way either.[99]

The Rehabilitation Act of 1973, which forbids discrimination against people with disabilities in federal programs and in programs receiving federal financial assistance,[100] was in many ways the model for the ADA.[101] Although the phrase "undue hardship" does not appear in the text of the relevant provision of the Rehabilitation Act,[102] regulations implementing the statute for programs or activities receiving federal assistance do provide that reasonable accommodations for people with disabilities need not be provided if doing so would entail undue hardship.[103] In this context as well, neither the

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94. *See, e.g.*, Bykerk, *supra* note 91, at 519–20 ("[T]he provision focuses on the debtor's ability to repay a debt determined by the debtor's disposable income . . . .").

95. *See* JOAN N. FEENEY ET AL., BANKRUPTCY LAW MANUAL § 8:4 (5th ed. 2020).

96. 42 U.S.C. § 12112(b)(5)(A).

97. *See id.* § 12111(10) (defining "undue hardship" as "an action requiring significant difficulty or expense" and setting forth factors to be considered in evaluating undue hardship).

98. *See* 29 C.F.R. § 1630.2(p) (2020) (setting forth factors relevant to determination of "undue hardship"); *id.* pt. 1630 app. (2020) (Interpretive Guidance on Title I of the Americans with Disabilities Act) (further elaborating on EEOC's view of the meaning of "undue hardship" under the ADA).

99. The statement in the text is based on the following search conducted by the author in the Westlaw "All Federal Cases" database on May 7, 2020: ("americans with disabilities act" and "undue hardship") and (undue /p common frequent normal commonplace everyday natural routine probable regular uncommon rare infrequent unusual "garden variety"). One older opinion states that one type of undue burden (where accommodation would be "financially crippling") is factually, though not inherently, rare. *See* Anderson v. Gus Mayer Bos. Store of Del., 924 F. Supp. 763, 780 (E.D. Tex. 1996).

100. *See* 29 U.S.C. § 794(a).

101. *See* 2 AMERICANS WITH DISABILITIES: PRACTICE AND COMPLIANCE MANUAL § 7:12 (2020).

102. *See, e.g.*, Borkowski v. Valley Cent. Sch. Dist., 63 F.3d 131, 136 (2d Cir. 1995).

103. *See, e.g.*, 34 C.F.R. § 104.12(a) (2020) (Department of Education); 45 C.F.R. § 84.12(a) (2020) (Department of Health & Human Services). At least twenty-six federal agencies have separately adopted regulations implementing the Rehabilitation Act's nondiscrimination mandate

regulations[104] nor any judicial decision indicates that "undue" hardship is uncommon per se.[105]

"Undue hardship" also appears in Title VII of the Civil Rights Act of 1964, as amended,[106] in connection with the prohibition on religious discrimination. The Act provides that is it an unlawful employment practice to "discriminate against any individual . . . because of such individual's . . . religion."[107] "Religion" is defined to include "all aspects of religious observance and practice . . . unless an employer demonstrates that he is unable to reasonably accommodate to an employee's or prospective employee's religious observance or practice without undue hardship."[108]

It appears that no appellate or trial court opinion holds that undue hardship in this context must be unusual.[109] It is true that in a concurrence joined by another panel member, Judge Thapar of the Sixth Circuit wrote, quoting dictionaries of the 1960s and 1970s, that "the hardship must 'exceed[ ] what is appropriate or normal'; in short, it must be 'excessive.'"[110] But "appropriate," "normal," and "excessive" all have normative meanings, so the quoted sentence does not squarely opine that undue hardship must be unusual. In any event, as the per curiam opinion of the court recognized,[111] the governing standard the Supreme Court has announced in this context is that any hardship that is more than "de minimis" is undue.[112] Given that

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for programs or activities receiving federal assistance; all use the "undue hardship" language. Space does not permit listing all the relevant regulatory citations. *See* 1 AMERICANS WITH DISABILITIES: PRACTICE AND COMPLIANCE MANUAL, *supra* note 101, § 1:4 (listing agencies and citing their regulatory provisions).

104. The assertion in the text is based on a review of all twenty-six agency regulations using the "undue hardship" language. *See* 1 AMERICANS WITH DISABILITIES: PRACTICE AND COMPLIANCE MANUAL, *supra* note 101, § 1:4.

105. The statement in the text is based on the following search conducted by the author in the Westlaw "All Federal Cases" database on May 7, 2020: ("rehabilitation act" and "undue hardship") and (undue /p common frequent normal commonplace everyday natural routine probable regular uncommon rare infrequent unusual "garden variety").

106. Congress added the statutory provision discussed here to the Act in 1972. *See* New York v. Dep't of Health & Hum. Servs., 414 F. Supp. 3d 475, 503–04 (S.D.N.Y. 2019).

107. 42 U.S.C. § 2000e-2(a)(1).

108. *Id.* § 2000e(j).

109. The statement in the text is based on the following search conducted by the author in the Westlaw "All Federal Cases" database on May 8, 2020: (2000e(j) and "undue hardship") and (undue /p common frequent normal commonplace everyday natural routine probable regular uncommon rare infrequent unusual "garden variety").

110. Small v. Memphis Light, Gas & Water, 952 F.3d 821, 827 (6th Cir. 2020) (Thapar, J., concurring), *petition for cert. filed*, No. 19-1388 (U.S. June 15, 2020).

111. *Id.* at 825 (majority opinion).

112. *See* Trans World Airlines, Inc. v. Hardison, 432 U.S. 63, 84 (1977) ("To require TWA to bear more than a de minimis cost in order to give Hardison Saturdays off is an undue hardship.").

above-de-minimis hardships need not be and in fact probably are not uncommon, the view that undue hardship is uncommon per se probably is incompatible with binding precedent in this area.

Another use of "undue hardship" that is frequently the subject of litigation is in Federal Rule of Civil Procedure 26(b)(3)(A)(ii). That rule provides that "documents and tangible things that are prepared in anticipation of litigation"[113] are discoverable only if the party seeking them "shows that it has substantial need for the materials to prepare its case and cannot, without undue hardship, obtain their substantial equivalent by other means."[114] The rule governs, for example, discovery of "fact" attorney work product.[115]

Although courts have on occasion stated that it is "rare" that the standard of Rule 26(b)(3)(A)(ii) is met,[116] no court appears to have grounded such a statement in the meaning of "undue."[117] Instead, courts seem simply to be making the factual observation that parties usually fail to make the required showing; sometimes this observation is tied explicitly to the "substantial need" requirement rather than to the "undue hardship" requirement.[118] Similarly, when the Supreme Court declared that the qualified privilege of Rule 26(b)(3) for work product implied that such material is not "routinely" available in discovery, it based its decision on the fact that the qualified privilege exists in the first place, not on the meaning of "undue."[119] Notably, courts contrast the fact that opinion work product can be discovered only in "very rare and extraordinary circumstances"[120] with the "mere" showing of

113. FED. R. CIV. P. 26(b)(3)(A).

114. *Id.* at 26(b)(3)(A)(ii).

115. "Fact" work product, such as photographs taken by counsel, *see* Johnson v. Westgate Vacation Villas, LLC, No. 6:17-cv-2141-Orl-37GJK, 2018 WL 7461685, at *4 (M.D. Fla. Oct. 23, 2018), is distinguished from "opinion" work product. The latter is work product that contains the attorney's "mental impressions, conclusions, opinions, or legal theories." FED. R. CIV. P. 26(b)(3)(B).

116. *See, e.g.*, Appleton Papers, Inc. v. E.P.A., 702 F.3d 1018, 1023 (7th Cir. 2012); Muhler Co. v. State Farm Fire & Cas. Co., No. 2:17-cv-01200-DCN, 2019 WL 2419016, at *4 (D.S.C. June 10, 2019) ("This burden is a difficult one and is satisfied only in rare situations, such as those involving witness unavailability."); *see also* Scurto v. Commonwealth Edison Co., No. 97 C 7508, 1999 WL 35311, at *2 (N.D. Ill. Jan. 11, 1999); Equal Emp. Opportunity Comm'n v. Koch Meat Co., No. 91 C 4715, 1992 WL 332310, at *4 (N.D. Ill. Nov. 5, 1992).

117. The statement in the text is based on the following search conducted by the author in the Westlaw "All Federal Cases" database on May 7, 2020: (("rule 26" "fed. r. civ. p. 26") and "undue hardship") and (undue /p common frequent normal commonplace everyday natural routine probable regular uncommon rare infrequent unusual "garden variety").

118. *See Appleton Papers, Inc.*, 702 F.3d at 1023 ("'Fact' work product is discoverable in the rare case where [a] party makes the 'substantial need' showing discussed above.").

119. *See* Fed. Trade Comm'n. v. Grolier Inc., 462 U.S. 19, 26–27 (1983).

120. *See In re* Grand Jury Subpoena, 870 F.3d 312, 316 (4th Cir. 2017); *In re* Smith & Nephew Birmingham Hip Resurfacing (BHR) Hip Implant Prods. Liab. Litig., No. 1:17-md-2775,

substantial need and undue hardship needed for discovery of fact work product.[121]

Courts frequently treat "unusual" and "undue" as separate concepts in deciding whether to grant relief from a final judgment, order, or proceedings. Federal Rules of Civil Procedure 60(b)(1)–(5) provide for such relief on enumerated grounds; Rule 60(b)(6) authorizes it for "any other reason that justifies relief."[122] A common formulation in applying Rule 60(b)(6) is to require the moving party to show two distinct things: First, that "unusual and extreme" circumstances exist, and second, that "absent relief, extreme and undue hardship will result."[123] By requiring separate showings that hardship is "unusual" and that it is "undue," these courts indicate that undue hardship need not, as a textual matter, be unusual.

Section 6161(b)(1) of the Internal Revenue Code grants the Secretary of the Treasury discretion to extend the time for payment of certain tax deficiencies. To secure such an extension, the taxpayer must show that timely payment of the deficiency will result in "undue hardship."[124] The Internal Revenue Service has issued regulations interpreting Section 6161(b)(1), and these regulations do not suggest that "undue hardship" is necessarily rare, stating only that undue hardship "means more than an inconvenience to the taxpayer" and must involve "substantial financial loss."[125] It likewise appears that no court interpreting the undue-hardship provision has determined that undue hardship is inherently rare.[126]

Section 1382b(c)(1)(C)(iv) of the Public Health and Welfare Code provides for an exception based on "undue hardship"[127] to the rule that an individual loses eligibility for Supplemental Security Income for the aged, blind, and disabled upon disposing of resources for less than fair market

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2019 WL 2330863, at *2 (D. Md. May 31, 2019); PETA v. Tri-State Zoological Park of W. Md., Inc., No. PX-17-2148, 2018 WL 3546725, at *3 (D. Md. July 24, 2018).

121. *See In re Grand Jury Subpoena*, 870 F.3d at 316; *accord In re Smith & Nephew*, 2019 WL 2330863, at *2; *PETA*, 2018 WL 3546725, at *3.

122. FED. R. CIV. P. 60(b)(1)–(6).

123. Valvoline Instant Oil Change Franchising v. Autocare Assocs., No. 98-5041, 1999 WL 98590, at *3 (6th Cir. Jan. 26, 1999); *see, e.g.*, Nemaizer v. Baker, 793 F.2d 58, 63 (2d Cir. 1986); Settle v. Bell, No. 06-1092-JDT-egb, 2017 WL 1058365, at *2 (W.D. Tenn. March 20, 2017).

124. I.R.C. § 6161(b)(1).

125. 26 C.F.R. § 1.6161-1(b) (2020).

126. The statement in the text is based on the following search conducted by the author in the Westlaw "All Federal Cases" database on May 8, 2020: (6161 and "undue hardship") and (undue /p common frequent normal commonplace everyday natural routine probable regular uncommon rare infrequent unusual "garden variety").

127. *See* 42 U.S.C. § 1382b(c)(1)(C)(iv).

value.[128] Neither the regulations implementing this provision[129] nor any judicial opinion[130] states that "undue hardship" is inherently uncommon.

D. Legislative History of the Undue-Hardship Provision

Courts[131] and commentators[132] continue to regard the legislative history of an ambiguous statutory provision as an important source of meaning despite some textualists' criticism of this view.[133] Part I therefore concludes by considering the legislative history of the "undue-hardship" provision.

Nowhere in the history was it suggested that "undue" meant "unusual" as a textual matter. The history does contain some references to the idea that discharge would be "exceptional," but these assertions seem to be factual, not definitional.[134] Moreover, they appear to refer to all student loan borrowers, not to the much smaller group of bankrupt debtors with student loans.[135]

The Higher Education Amendments of 1976 first imposed nondischargeability on student loan borrowers and contained an undue-hardship exception. The House Committee Report on the statute stated that the exception "permits loans to be discharged in bankruptcy in cases where exceptional circumstances exist."[136] However, the context indicates that undue-hardship cases were thought to be exceptional relative to the total population of student loan borrowers, rather than to the population of bankrupt student loan borrowers. The immediately preceding paragraph

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128. *See id.* § 1382b(c)(1)(A)(i).

129. *See* 20 C.F.R. § 416.1246(d)(3) (2020) (providing that undue hardship exists when the individual alleges that failure to receive SSI benefits would deprive them of food and shelter and the applicable benefit level exceeds a measure of the individual's monthly income and resources).

130. The statement in the text is based on the following search conducted by the author in the Westlaw "All Federal Cases" database on May 8, 2020: (1382b and "undue hardship") and (undue /p common frequent normal commonplace everyday natural routine probable regular uncommon rare infrequent unusual "garden variety").

131. The Supreme Court has long used legislative history to interpret "open-ended" statutory provisions such as Section 523(a)(8). *See* United States v. Taylor, 487 U.S. 326, 333 (1988); Dixson v. United States, 465 U.S. 482, 496 (1984). The Court continues to use legislative history to find the meaning of statutes where, as here, the text is open to more than one reasonable interpretation. *See, e.g.*, County of Maui v. Haw. Wildlife Fund, 140 S. Ct. 1462, 1471–72 (2020); Guerrero-Lasprilla v. Barr, 140 S. Ct. 1062, 1072 (2020).

132. *See* 2A SINGER & SINGER, *supra* note 74, § 45:5 ("To interpret statutes, 'intent of the legislature' is by far the most common . . . criterion."); *id.* § 48:2 (stating intent criterion "normally will support the judicial use of legislative history").

133. *See, e.g.*, Zedner v. United States, 547 U.S. 489, 511 (2006) (Scalia, J., concurring) ("[T]he use of legislative history is illegitimate and ill advised in the interpretation of any statute . . . .").

134. H.R. REP. NO. 94-1232, at 14 (1976).

135. *See id.*

136. *Id.*

states that under existing law, "in most circumstances a student may leave school with several thousand dollars in student loans and no assets, thereby making the student technically eligible to declare bankruptcy."[137] The law was changing bankruptcy from being available in "most circumstances" to being available in circumstances that were "exceptional": "exceptional" for students leaving school, not for bankrupt debtors.[138]

The 1978 Bankruptcy Reform Act replaced the 1976 nondischargeability provision with a substantially identical one contained in the new Bankruptcy Code.[139] The only significant discussion of the undue-hardship exception in connection with the 1978 Act came during the House floor debate. The House committee report had proposed restoring student loans to full dischargeability,[140] and Representative Allan Ertel of Pennsylvania proposed an ultimately successful floor amendment under which student loans would be nondischargeable for five years absent a showing of undue hardship.[141] The House debated the Ertel amendment fairly extensively; however, most of the discussion centered on whether student loans should be nondischargeable at all, rather than on the undue-hardship exception.[142]

Interestingly, most members did not use the phrase "undue hardship" in describing the exception, referring to it instead as an exception for "real"[143] or "true"[144] hardship, "severe hardship,"[145] or simply "hardship."[146] The only instance in which a House member addressed whether undue hardship would be rare was when Representative Bob Michel stated,

> It is time that Congress spoke up for the millions of students who have the decency to do what is right. Yes, I know that there are hardship cases in which bankruptcy is unavoidable. But these are exceptions and as I understand it the amendment offered by Mr. Ertel allows these to occur.[147]

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137. *Id.* at 13–14.

138. *Id.*

139. *See* Hunt, *Help*, *supra* note 29, at 1304.

140. *See* H.R. REP. NO. 95-595, at 132 (1977), *as reprinted in* 1978 U.S.C.C.A.N. 5963, 6093.

141. *See* 124 CONG. REC. 1791 (1978) (offering amendment), https://www.govinfo.gov/app/details/GPO-CRECB-1978-pt2/ [https://perma.cc/8LDP-KJ44]; *id.* at 1798–99 (adopting amendment).

142. *See id.* at 1791–98.

143. *See id.* at 1795 (statement of Rep. John Erlenborn).

144. *See id.* ("truly hardship"); *id.* at 1797 (using "true hardship" twice).

145. *See id.* at 1791 (statement of Rep. Allan Ertel); *id.* at 1792 ("severe financial problems"); *id.* at 1797.

146. *See id.* at 1794; *id.* at 1797 (statement of Rep. John Erlenborn) ("the hardship case").

147. *Id.* at 1795 (statement of Rep. Robert Michel).

As with the 1976 House committee report, it appears that Representative Michel considered undue-hardship cases "exceptions" relative to the overall population of student loan borrowers, including the "millions of students who have the decency to do what is right"[148]—not relative to the population of bankrupt student loan debtors.

In any event, the far stronger impression left by the legislative history of the original enactment of student loan nondischargeability is that nondischargeability was intended to combat student borrowers' perceived abuses of bankruptcy.[149] "Undue hardship" was a sort of stand-in for the absence of abuse; debtors for whom repayment would be an undue hardship presumably are not abusing the system.[150] The undue-hardship requirement can serve this main purpose—winnowing out abusive student borrowers—without being understood as inherently rare.

II. SCHOOL MISCONDUCT AND THE BORROWER DEFENSE RULE

Part II presents background on school misconduct and the Department of Education's response in the borrower defense rule. Part II.A reviews a sampling of alleged school misconduct that could justify not holding a borrower responsible for loans taken out to attend the school. Some of the allegations have been substantiated by agency findings or memorialized in default judgments; others come from lawsuits that schools have settled. Part II.B covers the rather convoluted procedural history of the Department of Education's borrower defense rule, which provides for administrative discharge of federal student loans based on wrongdoing by schools in some circumstances. Part II.C covers key substantive provisions of the rule, highlighting differences between the rule adopted under Secretary King in 2016 and the one adopted under Secretary DeVos in 2019.

148. *Id.*

149. *See* Hunt, *Help*, *supra* note 29, at 1302–07 (reviewing legislative history of adoption of nondischargeability in 1976 and 1978 and the importance of combating abuse in that history).

150. *See, e.g.*, 124 CONG. REC. 1792 (1978) (statement of Rep. Allan Ertel) (noting that the nondischargeability proposal would not bar discharge in case of undue hardship and going on to state that "[w]hat it does prevent" is a student's discharging a student loan immediately after graduating because "it is nice to get a fresh start").

A. Findings and Allegations of School Misconduct

Corinthian Colleges, Inc. was a venture reportedly originating in the 1995 leveraged buyout of a "struggling trade school in Irvine, California."[151] The company grew large through acquisitions and at its peak in 2010 operated 105 campuses with 110,000 students and revenues of $1.7 billion.[152] Of that $1.7 billion, up to $900 million came from federal student loans.[153] In addition, Corinthian ran a private student loan program that lent at least $568 million.[154]

Corinthian announced the closure of all its campuses in April 2015 after years of government investigations into potentially false and deceptive advertising to students.[155] In April 2015, the Department of Education announced its intention to fine Corinthian almost $30 million for 946 violations of the Department's regulations requiring truthful and complete disclosure of job placement rates to prospective students and others.[156]

The Department found, for example, that Corinthian claimed a placement rate of one-hundred percent for a criminal justice program while failing to disclose that it had classified fifty-eight percent of the graduates as "unavailable for employment,"[157] that it counted as "placed in field" IT-Network Systems Administration graduates that the company itself had hired

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151. *See* Lance Williams, *How Corinthian Colleges, a For-Profit Behemoth, Suddenly Imploded*, REVEAL (Sept. 20, 2016), https://www.revealnews.org/article/how-corinthian-colleges-a-for-profit-behemoth-suddenly-imploded/ [https://perma.cc/6NRS-2H4A].

152. *Id.*

153. The Senate Committee on Health, Education, Labor and Pensions reported that $1.4 billion of Corinthian's 2010 revenues came from Title IV education funds and that approximately $510 million of that was Pell grant aid. *See* S. COMM. ON HEALTH, EDUC., LAB. & PENSIONS, 112TH CONG., FOR PROFIT HIGHER EDUCATION: THE FAILURE TO SAFEGUARD THE FEDERAL INVESTMENT AND ENSURE STUDENT SUCCESS 410–12 (Comm. Print 2012), https://www.govinfo.gov/content/pkg/CPRT-112SPRT74931/pdf/CPRT-112SPRT74931.pdf [https://perma.cc/QG6X-JLYH]. Pell grants account for the vast majority of Title IV grant funds other than loans, *see* ALEXANDRA HEGJI, THE HIGHER EDUCATION ACT (HEA): A PRIMER 26–30 (2018), so it is reasonable to surmise that most of the remaining $890 million or so of federal funds came from loans.

154. *See* Williams, *supra* note 151 (reporting that students borrowed $568 million under Corinthian's private-loan program in the years 2011 to 2014).

155. Danielle Douglas-Gabriel, *Embattled For-Profit Corinthian Colleges Closes Its Doors*, WASH. POST (Apr. 26, 2015, 2:57 PM), https://www.washingtonpost.com/news/business/wp/2015/04/26/embattled-for-profit-corinthian-colleges-closes-its-doors/ [https://perma.cc/7MZ9-UZSZ]; *see* Williams, *supra* note 151.

156. Letter from Robin S. Minor, Acting Dir., Admin. Actions & Appeals Serv. Grp., U.S. Dep't of Educ., to Jack D. Massimino, President/Chief Exec. Officer, Corinthian Colls., Inc. 11 (Apr. 14, 2015), https://www2.ed.gov/documents/press-releases/heald-fine-action-placement-rate.pdf [https://perma.cc/V9XD-NWU8].

157. *Id.* at 5–6.

through a temp agency for short-term jobs on campus lasting as little as two days,[158] and that it had counted as "placed in field" the following three people: an accounting graduate who worked a food-service job at Taco Bell,[159] a business administration graduate who had a retail grocery position at Safeway,[160] and another business administration graduate who was not employed at graduation but previously had had a seasonal clerk position in shipping and receiving at a Macy's.[161]

Other misleading tactics, such as simply failing to identify which calendar year's graduates were counted in disclosures—making it more difficult or impossible to know precisely what the disclosures claimed and thus to check their accuracy—were less eye-catching but were pervasive. None of the disclosures the Department reviewed contained the required calendar-year information.[162]

The Consumer Financial Protection Bureau ("CFPB") obtained a default judgment against the then-defunct Corinthian in October 2015.[163] The CFPB had alleged in its complaint that Corinthian schools had used false placement statistics to lure student borrowers to enroll and take out private loans that Corinthian then purchased from the originator, either immediately or upon default.[164] The CFPB alleged that Corinthian counted graduates who held a job for as little as one day as "placed,"[165] created fictitious employers and reported students as placed with them,[166] listed unemployed students as employed,[167] classified graduates as incarcerated based on name matches without verification so that they would not be counted in placement statistics,[168] and bribed employers to hire their graduates for as little as thirty days.[169]

In March 2016, the Superior Court for the County of San Francisco entered a default judgment in favor of the State of California against Corinthian and

158. *Id.* at 8.
159. *Id.*
160. *Id.*
161. *Id.* at 9.
162. *Id.* at 6.
163. Consumer Fin. Prot. Bureau v. Corinthian Colls., Inc., No. 1:14-cv-07194, 2015 WL 10854380, at *1 (N.D. Ill. Oct. 27, 2015).
164. Complaint at 2–3, Consumer Fin. Prot. Bureau v. Corinthian Colls., Inc., No. 1:14-cv-07194 (N.D. Ill. Sept. 16, 2014), 2014 WL 5786691, ¶¶ 2–9.
165. *Id.* at 14–15, 2014 WL 5786691, ¶¶ 61–71.
166. *Id.* at 14, 2014 WL 5786691, ¶ 61.
167. *Id.* at 15, 2014 WL 5786691, ¶ 64.
168. *Id.* at 16–17, 2014 WL 5786691, ¶ 73–75.
169. *Id.* at 17–18, 2014 WL 5786691, ¶ 78.

its affiliates.[170] The judgment contained findings that placement rates posted online and provided to students in hard copy were "systematically false, misleading, erroneous and/or failed to comply with applicable state and federal regulations and/or accreditor standards"[171] and that the companies "ran millions of online and mobile ads stating that they . . . offer ultrasound technician, x-ray technician, radiology technician or dialysis technician programs, certificates, diplomas, or degrees" in California, despite the fact that no such programs existed;[172] that the schools misrepresented transferability of their credits to the California State University system;[173] and that the companies engaged in various other types of wrongdoing toward students.[174]

Corinthian's practices are probably the most publicized example of higher-education deception, but the company is hardly alone. In 2016, the year after Corinthian's collapse, ITT Technical Institutes, another large for-profit college chain, shut down amid allegations of "deceptive marketing; strong-arm recruitment tactics; misleading information about costs, courses, graduation and job placement rates; inflated enrollment numbers; bait-and-switch schemes; subpar instruction; and more."[175] Shortly thereafter, another for-profit, DeVry University, agreed to pay $100 million to resolve charges that it falsely claimed that ninety percent of its students who tried to find jobs in their field of study succeeded within six months and that its graduates earned fifteen percent more on average than those who attended other colleges or universities.[176]

In 2019, Career Education Corporation agreed in a settlement with state authorities not to try to collect $493 million in student loans its students owed based on allegations that it had improperly pressured students into enrolling,

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170. People v. Heald Coll., LLC, No. CGC-13-534793, 2016 Cal. Super. LEXIS 13746, at *1 (Mar. 23, 2016).

171. *Id.* at *9.

172. *Id.* at *11.

173. *Id.* at *16–17.

174. These included unlawfully using military seals in advertising, *id.* at *11–12, inserting unlawful waivers of rights into enrollment agreements, *id.* at *12–13, engaging in unlawful debt collection practices, *id.* at *13–14, failing to disclose the companies' role in making private loans to students, *id.* at *14–15, and misrepresenting their financial stability to students, *id.* at *17.

175. Patricia Cohen, *Downfall of ITT Technical Institutes Was a Long Time in the Making*, N.Y. TIMES (Sept. 7, 2016), https://nyti.ms/2clDAYo [https://perma.cc/6RNC-AHSY].

176. Niraj Chokshi, *DeVry University Will Pay $100 Million for Students' Loans and Tuition*, N.Y. TIMES (Dec. 15, 2016), https://www.nytimes.com/2016/12/15/business/devry-settlement-ftc.html [https://perma.cc/Q7WZ-7JH8].

misrepresented transferability of credits, and withheld tuition information,[177] as well as misrepresented the accreditation of its programs.[178] Late in that year, the University of Phoenix paid $191 million to settle FTC claims that it had falsely claimed to have special job-placement relationships with high-profile employers such as Adobe, Microsoft, and Twitter.[179]

Most of the wrongdoing just described was deceptive in nature, but some was oppressive or coercive—potentially "unfair," in the language of consumer-protection law—even if not deceptive.[180] A 2013 report of the Senate Committee on Health, Education, Labor and Pensions details further evidence of such hard-sell practices at for-profit schools. Examples include refusing to give information over the phone to induce the prospective student to come to campus for a "sales interview," controlling the enrollment conversation so that there was little opportunity to ask questions, pushing on "pain points" to overcome objections to enrolling, creating urgency to induce students to enroll on the spot, and discouraging students from contacting the financial aid department to determine available assistance before agreeing to enroll.[181] Although the line between aggressive tactics that are permissible and those that are unfair business practices may sometimes be difficult to draw, strong-arm practices have been among those alleged in lawsuits that schools have settled for large amounts of money.[182]

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177. Ian Stewart, *Nearly 180,000 Students Won't Have To Repay Loans from For-Profit Higher Ed Company*, NPR (Jan. 3, 2019, 7:17 PM), https://www.npr.org/2019/01/03/682057881/nearly-180-000-students-wont-have-to-repay-loans-from-for-profit-higher-ed-compa [https://perma.cc/VP38-WWW7].

178. Paul Fain, *Career Education Corp. Settles with States, Forgives Student Debt*, INSIDE HIGHER ED (Jan. 4, 2019), https://www.insidehighered.com/quicktakes/2019/01/04/career-education-corp-settles-states-forgives-student-debt [https://perma.cc/K2R8-GD3K]. CEC had been accused earlier of falsely claiming that students would be able to take required licensing exams after completing its programs, when in fact they could not do so because the programs were unaccredited. *See* Lisa Fleisher, *For-Profit College Agrees to $10 Million Settlement*, WALL ST. J. (Aug. 19, 2013, 5:06 PM), https://online.wsj.com/article/SB10001424127887323608504579023142047667678.html [https://perma.cc/CC29-MJDZ].

179. Aaron Glantz, *University of Phoenix Settles for Record $191 Million on Charges of Deceptive Advertising*, REVEAL (Dec. 11, 2019), https://www.revealnews.org/article/university-of-phoenix-settles-for-record-191-million-on-charges-of-deceptive-advertising/ [https://perma.cc/5XUS-MCJK].

180. *See, e.g.*, CAL. BUS. & PROF. CODE § 17200 (West 2020) (prohibiting "unlawful, unfair or fraudulent" business acts and practices).

181. *See* COMM. ON HEALTH, EDUC., LAB. & PENSIONS, 112TH CONG., *supra* note 153, at 67–75 (detailing evidence of these practices).

182. *See supra* Part II.A.

Schools also have been accused of targeting prospective students who are veterans,[183] have low incomes or other vulnerabilities,[184] or are members of structurally disadvantaged groups, such as Black and Latinx people.[185] Corinthian, for example, spent over $600,000 on two weeks of advertising on Black Entertainment Television in 2014.[186] Another now-closed for-profit institution, Vatterott College, described its target market as follows in an internal document: "Welfare Mom w/Kids. Pregnant Ladies. Recent Divorce. Low Self-Esteem. Low Income Jobs. Experienced a Recent Death. Physically/Mentally Abused. Recent Incarceration. Drug Rehabilitation. Dead-End Jobs-No Future."[187] Targeting vulnerable and disadvantaged people with deceptive messages or unfair tactics is particularly blameworthy.

B. Borrower Defense Rule—Procedural History

The Higher Education Act authorizes the Secretary of Education to create an administrative process for the discharge of federal direct loans where borrowers have defenses to repayment of the loans. Specifically, Section 455(h) of the Higher Education Act of 1965 as amended, adopted in 1993,[188] directs the Secretary of Education to "specify in regulations which acts or omissions of an institution of higher education a borrower may assert as a

183. *See* Kimberly Hefling, *Vets to Congress: Cut off For-Profit Colleges' Incentive To Recruit Student Veterans*, POLITICO (Mar. 29, 2019, 8:55 AM), https://www.politico.com/story/2019/03/29/for-profit-colleges-student-veterans-1288265 [https://perma.cc/7SLA-6UEX] (reporting that veterans groups describe GI Bill recipients as "aggressively targeted by for-profit colleges").

184. *See* Patricia Cohen, *For-Profit Colleges Accused of Fraud Still Receive U.S. Funds*, N.Y. TIMES (Oct. 12, 2015), https://nyti.ms/1GEAGmh [https://perma.cc/UH6Q-AZGC] (reporting accusations that for-profit colleges "prey[ ] on the poor, veterans and minorities").

185. *See* SUZANNE KAHN ET AL., BRIDGING PROGRESSIVE POLICY DEBATES: HOW STUDENT DEBT AND THE RACIAL WEALTH GAP REINFORCE EACH OTHER 19–20 (2019); Jiménez & Glater, *supra* note 24, at 145–49.

186. *See* Genevieve (Genzie) Bonadies, Joshua Rovenger, Eileen Connor, Brenda Shum & Toby Merrill, *For-Profit Schools' Predatory Practices and Students of Color: A Mission To Enroll Rather than Educate*, HARV. L. REV. BLOG (July 30, 2018), https://blog.harvardlawreview.org/for-profit-schools-predatory-practices-and-students-of-color-a-mission-to-enroll-rather-than-educate/ [https://perma.cc/G9D2-FQHV].

187. COMM. ON HEALTH, EDUC., LAB. & PENSIONS, 112TH CONG., *supra* note 153, at 66.

188. *See* Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, § 4021, 107 Stat. 312, 351 (codified at 20 U.S.C. § 1087a).

defense to repayment of a loan made under this part,"[189] meaning a William D. Ford Federal Direct Loan.[190]

The complex procedural history of the borrower defense rule illustrates how politically contentious the rule has been and how important the change in administrations has been to policy in the area, so it is worth reviewing in some detail. The Secretary issued two sets of regulations under this provision in 1994; the ones in effect from the end of the year forward provided, "In any proceeding to collect on a Direct Loan, the borrower may assert as a defense against repayment, any act or omission of the school attended by the student that would give rise to a cause of action against the school under applicable State law."[191]

The Department did not change the regulations until 2016,[192] when it adopted new rules in the wake of the collapse of Corinthian Colleges.[193] With minor exceptions,[194] the revised borrower defense rules were to take effect on July 1, 2017.[195]

Following a change in administration and a legal challenge to the new rules,[196] the Department changed course and adopted a policy of delaying implementation of the 2016 rules until it could develop a replacement for

189. 20 U.S.C. § 1087e(h). More generally, the Secretary has authority to "make, . . . rescind, and amend rules and regulations governing the" programs the Department administers, including the federal student loan programs. *See id.* § 1221e-3.

190. Loans made under other federal student loan programs, such as the Perkins and Federal Family Education Loan programs, can be discharged under the borrower defense rules discussed here if they are consolidated into direct loans. *See* 34 C.F.R. § 685.212(k)(2) (2020). There are some limits on the ability to recover funds already paid in such cases, different substantive standards may apply to older loans, and there may be avenues to relief other than consolidation. *See* NAT'L CONSUMER. L. CTR., STUDENT LOAN LAW § 10.6.3 (6th ed. 2019). Given that no new loans are being made under the FFEL and Perkins programs, *id.* § 1.3, this article focuses on the rules for direct loans.

191. William D. Ford Federal Direct Loan Program, 59 Fed. Reg. 61,664, 61,696 (Dec. 1, 1994) (to be codified at 34 C.F.R. § 685.206(c)(1)).

192. Direct Loan Master Promissory Notes ("MPNs") also have contained language, which has varied over time, providing for borrower defenses based on school conduct. The current MPN seems tied to the standards set forth in the regulations. *See* U.S. DEP'T EDUC., MASTER PROMISSORY NOTE 13 (2019), https://studentaid.gov/sites/default/files/Sub_Unsub_MPN_508-en-us.pdf [https://perma.cc/M2E2-L77G].

193. *See* Student Assistance General Provisions, 81 Fed. Reg. 75,926, 75,926 (Nov. 1, 2016) (to be codified at 34 C.F.R. pt. 30, 668, 674, 682, 685, 686) (noting that the Department was taking action "[i]n response to the collapse of Corinthian Colleges . . . and the flood of borrower defense claims submitted by Corinthian students stemming from the school's misconduct").

194. The exceptions provided for mandatory administrative forbearance and immediate cessation of guaranty agency collection activity upon notice of a borrower defense claim. *See id.* at 75,928, 76,079, 76,080.

195. *See id.* at 75,928.

196. *See* Cal. Ass'n of Priv. Postsecondary Schs. v. DeVos, 344 F. Supp. 3d 158, 163 (D.D.C. 2018).

them. The Department stayed the 2016 rules, first pending the legal challenge,[197] then until July 1, 2018,[198] then until July 1, 2019.[199]

The Department's decisions to delay implementation of the 2016 rules were themselves challenged in court. In September 2018, the District Court for the District of Columbia decided that the Department's delays were improper.[200] It accordingly vacated the stays, and the 2016 rules took effect in October 2018.[201] The Department, which had stopped processing claims with the change in administration, reportedly did not start processing them again until December 2019.[202]

Meanwhile, the Department worked on new rules to replace the ones it had sought to delay. After the prescribed, negotiated, rulemaking process failed to yield consensus,[203] the Department issued a notice of proposed rulemaking[204] and then, on September 23, 2019, issued a new set of borrower defense rules, which superseded the 2016 rules that had taken effect the preceding October.[205]

The House of Representatives and Senate, in January and March 2020, respectively, adopted a joint resolution invalidating the new rules under the

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197. *See* Student Assistance General Provisions, 82 Fed. Reg. 27,621, 27,622 (June 16, 2017) (to be codified at 34 C.F.R. pts. 668, 674, 682, 685).

198. *See* Student Assistance General Provisions, 82 Fed. Reg. 49,114, 49,114 (Oct. 24, 2017) (to be codified at 34 C.F.R. pts. 668, 674, 682, 685).

199. *See id.* at 49,117 (announcing intent to propose delay until July 1, 2019 "to allow for completion of the negotiated rulemaking process before regulatory changes become effective"); Student Assistance General Provisions, 82 Fed. Reg. 49,155, 49,155 (Oct. 24, 2017) (to be codified at 34 C.F.R. pts. 668, 674, 682, 685) (proposing delay until July 1, 2019); Student Assistance General Provisions, 83 Fed. Reg. 6458, 6458–59 (Feb. 14, 2018) (to be codified at 32 C.F.R. pt. 706) (final rule adopting delay until July 1, 2019).

200. *See* Bauer v. DeVos, 325 F. Supp. 3d 74, 88 (D.D.C.), *vacated*, 332 F. Supp. 3d 181 (D.D.C. 2018).

201. *See Bauer*, 332 F. Supp. at 186. In March 2019, the Department of Education issued a final rule acknowledging that "[w]ith this action by the Court" the 2016 rules "took effect." Student Assistance General Provisions, 84 Fed. Reg. 9964, 9965 (Mar. 19, 2019) (to be codified at 34 C.F.R. pt. 668, 674, 682, 685). Also, in October 2018, the court denied a preliminary injunction in a challenge to the 2016 rules, delaying implementation of some of those rules. *See Cal. Ass'n of Priv. Postsecondary Schs.*, 344 F. Supp. 3d at 164–65, 183.

202. Danielle Douglas-Gabriel, *DeVos Reaches Settlement over Stalled Student Debt Relief Claims*, WASH. POST (Apr. 10, 2020, 11:32 AM), https://www.washingtonpost.com/education/2020/04/10/devos-reaches-settlement-over-stalled-student-debt-relief-claims/ [https://perma.cc/ZK54-GMY2].

203. *See* Student Assistance General Provisions, 83 Fed. Reg. 37,242, 37,249 (July 31, 2018) (to be codified at 34 C.F.R. pt. 668, 674, 682, 685).

204. *See id.* at 37,242.

205. *See* Student Assistance General Provisions, 84 Fed. Reg. 49,788, 49,789 (Sept. 23, 2019).

Congressional Review Act.[206] On May 29, 2020, President Trump vetoed the joint resolution,[207] and the new rules went into effect on July 1, 2020, as scheduled.[208]

Borrower advocacy groups challenged the new rule in a lawsuit filed in the District Court for the Southern District of New York. Both sides in the litigation have filed summary judgment motions; they completed briefing on the motions on September 5, 2020.[209] The attorneys general of 22 states and Washington, D.C. sought to invalidate the rules in a separate action filed in the Northern District of California. The Department moved to dismiss, and briefing on that motion is currently scheduled to be completed on January 27, 2021.[210]

C. Borrower Defense Rule—Substantive Provisions

The significant substantive differences between the 2016 and 2019 rules illustrate both why the battle has been so fierce and why relief through the bankruptcy system is now needed. The 2016 rules replaced the state-law cause-of-action standard from 1994 with a uniform federal standard providing that the borrower had a defense to repayment in three circumstances: if the borrower obtained a "nondefault, favorable contested

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206. *See* 166 CONG. REC. H314–15 (daily ed. Jan. 16, 2020); 166 CONG. REC. S1685 (daily ed. Mar. 11, 2020); Green & Cowley, *supra* note 49; Ali Zaslav, *Senate Democrats To Force Vote This Week To Reverse DeVos Student Loan Policy*, CNN, https://www.cnn.com/2020/03/10/politics/senate-democrats-vote-devos-student-loan-policy/index.html [https://perma.cc/X3E9-4UFT] (Mar. 10, 2020, 3:20 PM).

207. *See* 166 CONG. REC. H2361–62 (daily ed. June 1, 2020) (vetoing H.R.J. Res. 76).

208. Another contentious process, relating specifically to Corinthian borrowers who borrowed to attend programs for which Corinthian had misrepresented placement numbers, unfolded in parallel with the struggle over the general borrower defense rules. The substantive issue for the Corinthian students was whether a special process for these borrowers would provide full loan forgiveness. *See* Calvillo Manriquez v. DeVos, 345 F. Supp. 3d 1077, 1088–89, 1098–99 (N.D. Cal. 2018). The Department of Education was ultimately held in contempt for collecting from Corinthian borrowers contrary to an order directing it to stop doing so while litigation over the matter was ongoing. *See* Calvillo Manriquez v. DeVos, 411 F. Supp. 3d 535, 537 (N.D. Cal. 2019). It was reported in April 2020 that the parties had reached an agreement on the principal terms of a settlement providing for a timetable for the Department of Education to resolve borrower-defense claims. *See* Douglas-Gabriel, *supra* note 202. As of December 2, 2020, the parties were still negotiating to finalize the settlement. *See* Joint Status Report, Calvillo Manriquez v. DeVos, No. 3:17-cv-7106-SK (N.D. Cal. Dec. 2, 2020).

209. *New York Legal Assistance Group. v. DeVos (1:20-cv-01414)*, COURTLISTENER (Jan. 9, 2021, 6:12 AM), https://www.courtlistener.com/docket/16860916/new-york-legal-assistance-group-v-devos/ [https://perma.cc/5FZK-A6N5].

210. *California v. DeVos (4:20-cv-04717)*, COURTLISTENER (Jan. 9, 2021, 3:10 AM), https://www.courtlistener.com/docket/17351511/people-of-the-state-of-california-v-betsy-devos/ [https://perma.cc/HSV3-8JRK].

judgment" against the school;[211] if the school "failed to perform its obligations under the terms of a contract" with the borrower;[212] or if the school made a "substantial misrepresentation . . . that the borrower reasonably relied on to the borrower's detriment" in deciding to attend or continue attending the school or in deciding to take out a Direct Loan.[213]

"Misrepresentation" had previously been defined as a "false, erroneous or misleading statement," including a statement that "has the likelihood or tendency to deceive."[214] The 2016 rules amended the definition to include "any statement that has the likelihood or tendency to mislead under the circumstances"[215] and added a provision that "[m]isrepresentation includes any statement that omits information in such a way as to make the statement false, erroneous, or misleading."[216]

The 2019 rules narrowed the substantive bases for a borrower-defense claim. They eliminated judgments against schools[217] and schools' breaches of contract as independent grounds for borrower defense.[218] Under the 2019 rules, a borrower can succeed on a borrower-defense claim only if "the borrower establishes by a preponderance of the evidence"[219] that "the institution at which the borrower enrolled made a misrepresentation . . . of material fact upon which the borrower reasonably relied" in deciding to take

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211. Student Assistance General Provisions, 81 Fed. Reg. 75,926, 76,083 (Nov. 1, 2016) (to be codified at 34 C.F.R. § 685.222(b)).

212. *Id.* (to be codified at 34 C.F.R. § 685.222(c)).

213. *Id.* (to be codified at 34 C.F.R. § 685.222(d)).

214. 34 C.F.R. § 668.71(c) (2016).

215. Student Assistance General Provisions, 81 Fed. Reg. at 76,072 (to be codified at 34 C.F.R. § 668.71(c)).

216. *Id.*

217. *See* Student Assistance General Provisions, 84 Fed. Reg. 49,788, 49,926–27 (Sept. 23, 2019) (to be codified at 34 C.F.R. § 685.206(e)) (omitting judgment as a basis for borrower defense).

218. *See id.* The 2019 rules also exclude several other types of claims from the category of potential borrower defenses. *See id.* (codified at 34 C.F.R. § 685.206(e)(5)(ii)(A)–(H)) (excluding as potential borrower defenses claims for personal injury, sexual harassment, civil rights violations, defamation, and others). Although the rules had not previously contained these exclusions, adding them may not have reflected a change in policy. *See* Student Assistance General Provisions, 81 Fed. Reg. at 75,945 (The Department of Education has "stated consistently" that "personal injury tort claims and actions based on allegations of sexual or racial harassment" cannot be the basis for borrower-defense claims because they are "not directly related to the loan or to the provision of educational services").

219. *See* Student Assistance General Provisions, 84 Fed. Reg. at 49,926 (to be codified at 34 C.F.R. § 685.206(e)(2)). Under the 2016 rules, a borrower defense succeeds if "a preponderance of the evidence . . . show[s]" that the relevant requirements are met. Student Assistance General Provisions, 81 Fed. Reg. at 76,083 (to be codified at 34 C.F.R. § 685.222(a)(2)).

out a federal student loan;[220] that the misrepresentation "directly and clearly relates to" enrollment, continued enrollment or the provision of educational services;[221] and that "the borrower was financially harmed by the misrepresentation."[222]

The 2019 rules also narrowed the definition of "misrepresentation," in part by adding a scienter requirement. A "misrepresentation" under the 2019 rules is

> a statement, act, or omission . . . that is false, misleading, or deceptive; that was made with knowledge of its false, misleading, or deceptive nature or with a reckless disregard for the truth; and that directly and clearly relates to enrollment or continuing enrollment at the institution or the provision of educational services for which the loan was made.[223]

The scienter requirement appears to make it very difficult for a borrower to prevail, as commenters on the proposed rules pointed out.[224] To answer this objection, the Department suggested that a borrower could use the fact that a school employee's claims differed from those made in the school's marketing materials to demonstrate reckless disregard for the truth.[225] The framing of this example is misleading in that the example ignores the fact that schools have been found deceitful in their official, required disclosures, not just in statements by rogue employees.[226] More important, the Department undercut its point a few paragraphs later when it stated that "a school should not be held liable if it committed an inadvertent mistake."[227] In the Department's own unrepresentative scenario, even if a school were confronted with a discrepancy between what its employee said and what its materials said, it could simply argue that the misrepresentation was an "innocent mistake"[228]— and the burden of showing otherwise would be on the borrower.

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220. *See* Student Assistance General Provisions, 84 Fed. Reg. at 49,926 (to be codified at 34 C.F.R. § 685.206(e)(2)(i)).

221. *See id.* The 2016 rules had specified that the act or omission giving rise to borrower defense must "relate[ ] to the making of a Direct Loan for enrollment at the school or the provision of educational services for which the loan was provided." Student Assistance General Provisions, 81 Fed. Reg. at 76,083 (34 C.F.R. § 685.22(a)(5)); *see also id.* at 75,945 (citing the Department of Education's "consistent[ ]" statements that conduct giving rise to borrower defense must be "directly related" to loan or provision of educational services).

222. *See* Student Assistance General Provisions, 84 Fed. Reg. at 49,927 (to be codified at 34 C.F.R. § 685.206(e)(2)(ii)).

223. *Id.* at 49,927 (codified at 34 C.F.R. § 685.206(e)(3)).

224. *Id.* at 49,802.

225. *Id.* at 49,803.

226. *Id.* at 49,804.

227. *Id.*

228. *Id.*

Another important set of differences between the 2016 and 2019 rules relates to the procedures for bringing borrower-defense claims. The 2016 rules provided for both individual[229] and group[230] processes. The individual process provided for an application by the borrower,[231] notice to and response by the school,[232] and resolution of the claim through "a fact-finding process conducted by" a Department official,[233] whose decisions are designated as "final."[234]

As for group processes, they could be started by the Secretary (not a borrower or group of borrowers).[235] In a group proceeding, the Secretary was to designate a Department official[236] to present the group's claim to a hearing officer, who was to make a decision based on evidence presented by the Department official and the school.[237] Importantly, the rules provided for a rebuttable presumption of borrower reliance on any widely disseminated, substantial misrepresentation.[238]

The 2019 rules eliminate the provision dealing with group actions altogether. They also impose procedural requirements on individual actions that make it more difficult for a borrower to prevail.[239] The borrower must now, with the initial application for forgiveness, provide "any information relevant to assessing whether the borrower incurred financial harm, including providing documentation that the borrower actively pursued employment in the field for which the borrower's education prepared the borrower if the borrower is a recent graduate."[240] As the rules state, "failure to provide such information results in a presumption that the borrower failed to actively pursue employment in the field."[241] The rules provide for a decision based on the borrower's application, the school's response, and the borrower's reply, which "must be limited to issues and evidence raised in the school's

229. *See* Student Assistance General Provisions, 81 Fed. Reg. 75,926, 76,083–84 (Nov. 1, 2016) (to be codified at 34 C.F.R. § 685.222(e)).

230. *See id.* at 76,084–85 (to be codified at 34 C.F.R. § 685.222(f)–(h)).

231. *See id.* at 76,083 (to be codified at 34 C.F.R. § 685.222(e)(1)(i)).

232. *See id.* at 76,084 (to be codified at 34 C.F.R. § 685.222(e)(3)(i)).

233. *See id.* (to be codified at 34 C.F.R. § 685.222(e)(3)).

234. *See id.* (to be codified at 34 C.F.R. § 685.222(e)(5)).

235. *See id.* (to be codified at 34 C.F.R. § 685.222(f)(1)).

236. *See id.* (to be codified at 34 C.F.R. § 685.222(f)(2)(i)).

237. *See id.* at 76,085 (to be codified at 34 C.F.R. § 685.222(h)(1)). If the school was closed and had provided no financial protection currently available to the Secretary of Education, the hearing officer was to consider information presented by the school only "if practicable." *Id.* (to be codified at 34 C.F.R. § 685.222(g)(1)).

238. *See id.* at 76,084–85 (to be codified at 34 C.F.R. § 685.222(f)(3)).

239. *See* Student Assistance General Provisions, 84 Fed. Reg. 49,788, 49,928 (Sept. 23, 2019) (to be codified at 34 C.F.R. § 685.206(e)(8)–(10)).

240. *See id.* (to be codified at 34 C.F.R. § 685.206(e)(8)(v)).

241. *Id.*

submission and any evidence otherwise in the possession of the Secretary."[242] There is no provision for a live hearing.[243] Despite the borrower's burden to prove scienter, there is also no provision for discovery.[244]

The successive versions of the borrower rules also differ in how they treat the Secretary's recovery from schools for loan balances cancelled because of successful borrower-defense applications. The 2016 rules appeared to make collection from schools automatic upon a successful borrower-defense application,[245] while the 2019 rules provide that the Secretary has discretion to start a separate process that would lead to collection.[246]

III. SCHOOL MISCONDUCT IN STUDENT LOAN BANKRUPTCY

Part III presents and makes the case for a concrete proposal for taking school misconduct into account in evaluating undue hardship. Part III.A describes the proposal. Part III.B shows that the proposal is consistent with the text and policy of the Bankruptcy Code, properly understood, and promotes the purposes of the federal student loan programs. Part III.B also shows that courts generally can implement the proposal while following existing tests for undue hardship, although the *Brunner* test may restrict the use of school misconduct in this context to some extent. Part III.C makes use of an analogy to the FTC's Holder Rule to show that consumer-law principles support the proposal.

A. A Proposal for Considering School Misconduct in Student Loan Bankruptcy

When repayment will entail some hardship, and the student borrower has relied on a misrepresentation in deciding to pursue or continue debt-financed education or to take out a particular loan, the debt should be dischargeable at least to the extent of the difference between the cost of schooling and the value of the education the borrower actually received.[247] Reliance should be

242. *See id.* at 49,928–29 (to be codified at 34 C.F.R. § 685.206(e)(10)).

243. *See id.* (to be codified at 34 C.F.R. § 685.206(e)(8)–(11)).

244. *See id.*

245. *See* Student Assistance General Provisions, 81 Fed. Reg. 75,926, 76,089 (Nov. 1, 2016) (to be codified at 34 C.F.R. § 685.308(a)); *id.* at 76,085 (to be codified at 34 C.F.R. § 685.222(h)(5)(i)); *id.* at 75,947–48.

246. Student Assistance General Provisions, 84 Fed. Reg. at 49,933 (to be codified at 34 C.F.R. § 685.308(a)(3)); *id.* at 49,792.

247. For comparison, the 2016 rules provided that relief for misrepresentation was to be based on the cost of attendance, the value of the education the borrower received, the value of the

presumed for widely disseminated misrepresentations,[248] and the burden should be on the student loan holder to prove any value the borrower actually received from the misrepresented education.[249]

Although most school-misconduct allegations relate to deception, governmental authorities have also found that schools have engaged in high-pressure or strong-arm recruiting tactics.[250] Where recruiting or retention tactics are unfair[251] or abusive[252] practices under consumer-protection law principles or are procedurally unconscionable under contract law,[253] and the value of the education is less than its cost, courts should be willing to discharge at least the loan balance attributable to the difference between the education's cost and its value.

Finally, the school may have breached a contract with the student or the student may have a judgment against the school.[254] In such cases, the school is liable to the student, and the question is simply whether that liability implies that the student should be able to discharge the loan. Presuming that the student's claim is related to the loan or the educational services the loan was incurred to pay for and that repayment would entail hardship,[255] the

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education a "reasonable borrower in the borrower's circumstances would have received, and/or the value of the education the borrower should have expected given the information provided by the institution." 34 C.F.R. § 685.222(i)(2)(i) (2020). Under the rules, value was to be assessed "in a manner that is reasonable and practicable." *Id.*

248. *See* 34 C.F.R. § 685.222(f)(3) (providing for rebuttable presumption of reasonable reliance in the case of widely disseminated, substantial misrepresentations).

249. The burden to prove the benefit is placed on the institution to free the borrower from the task of trying to prove a negative fact. *See, e.g.*, Bank of Am. v. WestTrop Ass'n, No. 2:16-cv-1451-KJD-DJA, 2020 WL 1156116, at *5 (D. Nev. Mar. 9, 2020) ("It is difficult and unfair to require a party to prove a negative fact."); *see also* Overby v. Nat'l Ass'n of Letter Carriers, 595 F.3d 1290, 1294 (D.C. Cir. 2010) ("[I]f direct evidence of negatives were required, there would be little point in the law requiring any person to do anything as the failure to do it could rarely be proved.").

250. *See* discussion *supra* Part II.A.

251. *See, e.g.*, Am. Fin. Servs. Ass'n v. Fed. Trade Comm'n, 767 F.2d 957, 979 (D.C. Cir. 1985) (listing "high-pressure sales techniques" as one of four types of conduct that the Federal Trade Commission "has determined to be unfair").

252. *See* 12 U.S.C. § 5511(b)(2) (authorizing the Consumer Financial Protection Bureau to ensure that consumers are protected from "unfair, deceptive, or abusive acts and practices").

253. 7 TIMOTHY MURRAY ET AL., CORBIN ON CONTRACTS § 29.4 (2020) (citing Warren Elec. Supply, Inc. v. Davidson, 727 N.Y.S.2d 502, 504 (App. Div. 2001)) (noting "high pressure sales tactics" as one of the "indicia of unconscionability"); *see* 1 RICHARD A. LORD, WILLISTON ON CONTRACTS § 1:21 (4th ed. 2020) (citing State *ex rel.* Hewitt v. Kerr, 461 S.W.3d 798, 807 n.7 (Mo. 2015) (giving "high pressure sales" as an example of procedural unconscionability)).

254. *See* 34 C.F.R. § 685.222(b)–(c) (2020) (providing for borrower defense in these cases).

255. *See* Student Assistance General Provisions, 81 Fed. Reg. 75,926, 75,945 (Nov. 1, 2016) (to be codified at 34 C.F.R. pt. 30, 668, 674, 682, 685, 686) (asserting that since 1995, borrower defense has been available only for causes of action "directly related to the loan or to the provision of educational services").

answer is yes. As argued in Part III.C, principles underlying the FTC Holder Rule dictate that the federal government is better positioned to bear school-misconduct losses than student borrowers.

Some degree of hardship in repaying is a statutory requirement for bankruptcy discharge of student loans.[256] As this author has argued elsewhere, the term "hardship" in Section 523(a)(8) can be understood as the inability to maintain a middle-class standard of living.[257] Cases of school misconduct in particular call for such a generous interpretation of "hardship,"[258] although precedent may not permit the middle-class standard in some jurisdictions.[259]

Because bankruptcy courts apply the open-ended undue-hardship standard, they are free to act to protect bankrupt student borrowers without regard to constraints on consumer-protection law that have been imposed in some contexts. For example, under a policy statement adopted in 1980 that Congress codified into law in 1994,[260] the FTC may not prohibit an act or practice as unfair without engaging in a cost–benefit analysis that considers "countervailing benefits to consumers or to competition."[261] Presumably, it would be difficult for most bankrupt student borrowers to present such an analysis. However, most state consumer-protection laws apparently do not require such a showing,[262] and neither should bankruptcy courts.

When deception or unfair practices contributed to a borrower's decision to enroll in the school in the first place, the borrower arguably should not have to pay for the schooling at all. When a contract is avoided for misrepresentation, the avoiding party must return property received under the contract but is not obligated to account for services provided.[263] There is generally no requirement to pay for benefits that the recipient should have

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256. *See* 11 U.S.C. § 523(a)(8).

257. *See* Hunt, *Purpose*, *supra* note 29, at 22–30 (explaining and defending proposal to define hardship this way). Precedent may obstruct immediate adoption of this standard in some jurisdictions.

258. *See* discussion *infra* Part III.B.4.

259. *See* discussion *infra* Part III.B.4.

260. David L. Belt, *Should the FTC's Current Criteria for Determining "Unfair Act and Practices" Be Applied to State "Little FTC Acts"?*, ANTITRUST SOURCE, June 2010, at 1–4.

261. 15 U.S.C. § 45(n).

262. *See* Belt, *supra* note 260, at 6 (reporting that of twenty-eight states with "Little FTC Acts," only four apply the test of Section 45(n)).

263. *See* RESTATEMENT (SECOND) OF CONTRACTS § 376 (AM. L. INST. 1981) (stating that party avoiding contract must return property "under the rule stated in § 384"); *id.* § 384(1) (requiring the return of property received in most cases but imposing no comparable requirement for services received); *see also* RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 13 cmt. b (AM. L. INST. 2011) (stating the rules on restitution for fraud "are intended to be fully consistent with the rules stated in Restatement Second, Contracts § . . . 376").

been free to refuse, even if they are valuable.[264] If deceit or coercion undermined the borrower's assent to the exchange of money for schooling, the borrower arguably has been deprived of freedom to refuse and should be relieved of an obligation to pay.[265] If a school targeted deceptive or unfair practices at low-income students or students from structurally disadvantaged racial or ethnic groups such as Black, Latinx and Native students,[266] its behavior is even more culpable, further justifying full relief for the victim. Particularly in targeting cases,[267] courts should consider granting full discharge without an offset for the value of services rendered.

This article focuses on school conduct that is deceptive or that is unfair, abusive or unconscionable under consumer-protection or contract-law principles. However, the interpretation of "undue hardship" proposed here can support other efforts to combat school behavior that falls short of reasonable standards. For example, offering poor-quality education can harm students even without deception or "unfairness," at least as the latter term is sometimes applied in consumer law.[268] As Professor Glater has pointed out, the Department has not tried to supervise educational quality directly.[269] Conceiving of undue hardship as unjustified hardship bolsters the argument that bankruptcy courts should mitigate student harm from poor educational quality by considering whether the student actually benefited from the program, as some courts have done in the past,[270] and as this author[271] and other scholars[272] have advocated.

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264. *See* RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 2(4) (AM. L. INST. 2011) ("Liability in restitution may not subject an innocent recipient to . . . an obligation to pay for a benefit that the recipient should have been free to refuse.").

265. *Cf. id.* § 13 cmt. a, illus.1 (stating that a fraud perpetrator is liable in restitution to victim even where victim received fair market value for what they gave up in the fraud-contaminated exchange).

266. *See* discussion *supra* Part II.A.

267. Targeting might be difficult for an individual borrower to prove in a bankruptcy case, but the findings of government investigations or class actions could be helpful in making the showing. *See* discussion *infra* Part IV.C.2.

268. *See* Maura Dundon, *Students or Consumers? For-Profit Colleges and the Practical and Theoretical Role of Consumer Protection*, 9 HARV. L. & POL'Y REV. 375, 390–91 (2015) (explaining difficulties of proving practices are "unfair" under current consumer protection law).

269. *See* Jonathan D. Glater, *Law and the Conundrum of Higher Education Quality*, 51 U.C. DAVIS L. REV. 1211, 1245–46 (2018).

270. *See* Hunt, *supra* note 23, at 778–79 (collecting cases).

271. *See id.* at 778–83 (arguing that net debtor benefit from education should be considered in undue-hardship determinations).

272. *See* Jiménez & Glater, *supra* note 24, at 186–87.

B. Bankruptcy Law and Policy Support Adoption of the Article's Proposal

Courts have only very rarely considered school misconduct in deciding whether to discharge student loans, but they should be willing to do so. The Code's text and underlying policy, as well as courts' treatment of creditor-side misconduct in analogous situations, all support this article's proposal. Judicial precedent on the meaning of "undue hardship" does not prohibit courts from considering school wrongdoing, although it may constrict the inquiry in some jurisdictions.

Despite the many findings that schools have deceived and abused students, and the enormous controversy over the borrower defense rule, it appears that a borrower has asserted school misconduct as a basis for discharge in only one reported case.[273] In that case, *Gumpher v. Educational Credit Management Corporation* (*In re Gumpher*), the joint debtor–borrowers sought to discharge loans held by ECMC that they had taken out to attend the culinary school Le Cordon Bleu.[274] They alleged that the school "used inflated job statistics to mislead the Plaintiff(s) into thinking they would secure jobs after graduation."[275] The court dismissed the adversary proceeding against ECMC because the plaintiffs failed to plead any specific misrepresentation Le Cordon Bleu made[276] or to plead facts connecting ECMC to any wrongdoing by Le Cordon Bleu.[277] The court held that the borrowers had not alleged facts supporting an inference that ECMC "is in any way liable for the alleged misconduct of the culinary school."[278] Although this statement might be taken to indicate that the court required that a lender or servicer be "liable for" the school's improper behavior in order for the borrower to get bankruptcy relief, the court did not analyze the issue. The scanty nature of the complaint in *Gumpher* makes it difficult to draw any larger meaning from the case.

Three older bankruptcy court decisions that granted partial or total discharge of student loans acknowledged the problem of school

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273. The statement in the text is based on the following search in Westlaw's "All Federal Cases" database, conducted May 27, 2020: "undue hardship" and ("student loan" or "education! loan") and bankrupt! and ((misconduct or malfeasance or impropriety or misbehavior or wrongdoing) /s (school or university or institution)).

274. Gumpher v. Educ. Credit Mgmt. Corp. (*In re* Gumpher), No. 16-31183, 2017 WL 187547, at *1 (Bankr. N.D. Ohio Jan. 17, 2017).

275. *Id.* at *3.

276. *See id.* at *4.

277. *See id.*

278. *Id.*

misconduct,[279] and one even stated that whether the student was "inveigled into obtaining the loan . . . when the college authorities should have known that . . . the student had little chance of obtaining employment in that field" should be a "substantial factor" in determining dischargeability.[280] However, in none of these cases did the court clearly rely on school misconduct in deciding to grant discharge.[281]

1. School Misconduct Is Relevant to "Undue Hardship" Under the Bankruptcy Code

Schools' behavior is relevant to evaluating undue hardship under Section 523(a)(8). Hardship endured to pay a student loan that arises from the school's deception or unfair coercion is unjustified and therefore "undue."

As discussed, dictionary definitions of "undue" from when bankruptcy nondischargeability of student loans was enacted define the word as "inappropriate,"[282] "improper,"[283] "excessive,"[284] "unreasonable"[285] and "unjustifiable."[286] This article uses the term "unjustifiable" to sum up all these concepts, given that they all entail exceeding or transgressing some standard or norm. In fact, judicial opinions commonly equate "undue" and "unjustified."[287] Unjustified hardship is undue hardship.

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279. *See* Vazquez v. United Student Aid Funds, Inc. (*In re* Vazquez), 194 B.R. 677, 680 (Bankr. S.D. Fla. 1996) ("The Court is aware of many scams where profit-hungry solicitors enroll people into educational programs which provide nothing of practical value to the student and from which the 'graduates' are able to achieve little if anything."); Correll v. Union Nat'l Bank of Pittsburgh (*In re* Correll), 105 B.R. 302, 307 (Bankr. W.D. Pa. 1989) ("[F]ar too many school operators are exploiting America's neediest people and their dreams for a new start in life."); Littell v. Oregon (*In re* Littell), 6 B.R. 85, 88 (Bankr. D. Or. 1980) ("There is thus great pressure and temptation on the part of college authorities to encourage students to apply for loans . . . when in effect it is not a sound economic thing to do.").

280. *In re Littell*, 6 B.R. at 88.

281. In *In re Vazquez*, the court could not determine whether the debtors were in fact the victims of a scam. 194 B.R. at 680. In *In re Correll*, although the court determined that the debtor was victimized by a profit-hungry operator, it did not explain how this fact figured into its analysis. 105 B.R. at 307–08. In *In re Littell*, the court did not find that the debtor's school in particular was exploitative, perhaps because the debtors did not raise the issue. 6 B.R. at 88–89.

282. *See supra* notes 80–81, 83–84.

283. *See supra* notes 80–85, 87.

284. *See supra* notes 80–84.

285. *See supra* notes 82–84.

286. *See supra* notes 80.

287. For examples from federal appellate courts, see Spartan Concrete Prods., LLC v. Argos USVI Corp., 929 F.3d 107, 115 (3d Cir. 2019) ("Undue delay is 'protracted and unjustified.'") (quoting Mullin v. Balicki, 875 F.3d 140, 151 (3d Cir. 2017)); DeGruy v. Wade, 586 F. App'x 652, 656 (5th Cir. 2014) (equating "unjustifiable delay" with "undue delay and dilatory motive");

This notion applies to the case of school misconduct. Any hardship a borrower endures in repaying loans that they were tricked or unfairly pressured into incurring and for which they have not received corresponding educational value is unjustified and therefore undue. Such loans should be discharged.

Courts already ask whether a debtor's hardship is unjustified in some respects. In evaluating the debtor's efforts to repay, they scrutinize aspects of debtor conduct, such as the decision to have children,[288] that are not strictly related to the degree of hardship that repayment would entail.[289] Discharge is denied when the debtor's hardship arises from debtor conduct of which the court does not approve. This article advocates applying the concept of justified hardship in an even-handed manner that takes account of the seller's fault as well as the buyer's.

No matter how unjustifiable it would be to make a borrower repay, discharge is available under the Code only if repayment entails some degree of hardship. Courts should require only a minimal showing of "undue hardship" in school-wrongdoing cases because the fact that the borrower's consent to the loan resulted from deception or unfairness goes a long way toward making discharge appropriate. The text of the statute itself imposes little constraint on courts' generosity; hardship can mean simply something that is "hard to bear."[290] Bankrupt borrowers are likely to face some difficulty

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In re Engle Cases, 767 F.3d 1082, 1099 (11th Cir. 2014); McNeil v. Anderson, 258 F. App'x 205, 207 (10th Cir. 2007); United States v. Lopez, 443 F.3d 1280, 1286 (10th Cir. 2006); United States v. Squillacote, 221 F.3d 542, 558 (4th Cir. 2000) (noting that an "undue burden" is one that is "unjustifiable under the circumstances"); Town of Norwood v. Fed. Energy Regul. Comm'n, 202 F.3d 392, 402 (1st Cir. 2000); Griffin v. Strong, 983 F.2d 1544, 1547–48 (10th Cir. 1993); Cody v. Henderson, 936 F.2d 715, 718 (2d Cir. 1991); Sweetheart Plastics, Inc. v. Detroit Forming, Inc., 743 F.2d 1039, 1043 & n.2 (4th Cir. 1984) (equating "undue delay" and "unjustified delay").

288. *See* Ward v. United States (*In re* Ward), Ch. 7 Case No. 02-34594-H4-7, Adv. No. 02-3483, slip op. at 6–7 (Bankr. S.D. Tex. May 25, 2004) (denying discharge in part because debtor decided "to have children and start a family").

289. Courts tend to consider such issues in connection with the *Brunner* test's requirement that the debtor have made good-faith efforts to repay the loans. *See, e.g.*, Trudel v. U.S. Dep't of Educ. (*In re* Trudel), 514 B.R. 219, 229 (B.A.P. 6th Cir. 2014) ("Good faith, in this context, is essentially an inquiry into whether . . . there is some justification for the debtor's default and ongoing inability to repay the loan.") (quoting Crawley v. Educ. Credit Mgmt. Corp. (*In re* Crawley), 460 B.R. 421, 444 (Bankr. E.D. Pa. 2011)). Courts have denied discharge based at least in part on judgments that the debtor should have tried to find a higher-paying job outside the field for which their education prepared them, *see, e.g.*, U.S. Dep't of Educ. v. Gerhardt (*In re* Gerhardt), 348 F.3d 89, 93 (5th Cir. 2003), should have moved to find a job making more money, *see, e.g.*, *In re* Mallinckrodt, 274 B.R. 560, 568 (S.D. Fla. 2002), and should have paid more on the loans out of an annual income of $11,000 than the $774 the debtor did pay, *see* Stitt v. U.S. Dep't of Educ. (*In re* Stitt), 532 B.R. 638, 644 (D. Md. 2015).

290. *Hardship*, OXFORD ENGLISH DICTIONARY, *supra* note 80 ("1. The quality of being hard to bear.").

repaying their student loans, so it usually will be at least arguable that this requirement is met. As argued elsewhere, hardship can even be plausibly understood as the inability to maintain a middle-class lifestyle.[291]

2. Bankruptcy Policy Supports the Article's Proposal

"Undue hardship" under Section 523(a)(8) should be interpreted to promote the provision's underlying policies, and discharging loans arising from school misconduct is not only consistent with the specific policy goals behind conditional nondischargeability but also promotes the larger goals of the Bankruptcy Code when it is seen in the proper context.

The primary purpose of nondischargeability is to deter abuse of the bankruptcy system during the first five years of repayment; a secondary purpose is to recover funds from borrowers.[292] Borrowers at least arguably abuse bankruptcy when they have freely chosen to borrow for school and have received valuable education, only to seek bankruptcy relief because they decide they simply do not want to repay their loans.[293] Indeed, judicial decisions interpreting "undue hardship" often assume that the decision to borrow for education was a freely chosen, voluntarily incurred risk[294] or that the student borrower benefited from the education they received.[295]

When the borrower relied on a misrepresentation in deciding to pursue the program for which they borrowed or was subjected to unfair high-pressure sales tactics, such assumptions are not warranted. A borrower who seeks to be released from an obligation to pay for a worthless program they were tricked into pursuing is not abusing the system. Even assuming such a borrower should pay for all or some of any value they did receive,[296] that objection can be met in many, if not most, jurisdictions by granting a partial discharge.[297]

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291. *See* Hunt, *Purpose*, *supra* note 29, at 22–30.

292. *See* Hunt, *Help*, *supra* note 29, at 1310–12.

293. *See id.* at 1310–11.

294. *See* Pa. Higher Educ. Assistance Auth. v. Faish (*In re* Faish), 72 F.3d 298, 305 (3d Cir. 1995) (quoting *In re* Roberson, 999 F.2d 1132, 1137 (7th Cir. 1993)) ("[T]he decision of whether or not to borrow for a college education lies with the individual . . . ."); *In re Roberson*, 999 F.2d at 1137 ("The government is not twisting the arms of potential students. The decision of whether or not to borrow for a college education lies with the individual . . . .").

295. *See* Educ. Credit Mgmt. Corp. v. Frushour (*In re* Frushour), 433 F.3d 393, 399 (4th Cir. 2005) ("Debtors receive valuable benefits from congressionally authorized loans . . . .").

296. This proposition is debatable. *See supra* notes 263–267 and accompanying text.

297. The Courts of Appeals for the Sixth and Ninth Circuits have held that bankruptcy courts have the authority to grant a partial discharge of student loans, and the Court of Appeals for the Fourth Circuit has affirmed a grant of partial discharge. *See* Hedlund v. Educ. Res. Inst. (*In re*

The second goal of nondischargeability, that of collecting funds from borrowers, typically will be less pressing in cases of school misconduct. To begin with, there arguably is no legitimate interest in collecting funds from victims of deceptive or unfair practices. In addition, the Department has ample authority to collect the funds from the perpetrators rather than the victims.[298] Solvent institutions are more likely to be able to pay than bankrupt student borrowers, and the Department has authority to protect itself against insolvency by requiring institutions to provide letters of credit or other financial protection.[299]

Even granting the debatable proposition that deceived borrowers should pay for value actually received, victimized students typically will not be promising targets for cost-effective loan collection efforts. Students who attended colleges that have been investigated or sued for fraud or related matters tend to have poor economic outcomes.[300] Moreover, apart from reluctance to repay arising specifically from the fact of being deceived or

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Hedlund), 718 F.3d 848, 856 (9th Cir. 2013); Saxman v. Educ. Credit Mgmt. BJR Corp. (*In re* Saxman), 325 F.3d 1168, 1170, 1173–74 (9th Cir. 2003); Tenn. Student Assistance Corp. v. Hornsby (*In re* Hornsby), 144 F.3d 433, 438–39 (6th Cir. 1998); Ammirati v. Nellie Mae (*In re* Ammirati), 85 F.3d 615, 615 (4th Cir. 1996) (per curiam). The Court of Appeals for the Eleventh Circuit has suggested that the Code does not authorize partial discharge, although it has not said so explicitly. *See* Hemar Ins. Corp. of Am. v. Cox (*In re* Cox), 338 F.3d 1238, 1243 (11th Cir. 2003). District and bankruptcy courts have split on the issue, with a majority apparently finding that partial discharge is possible. *See* NAT'L CONSUMER. L. CTR., *supra* note 190, § 11.5 nn.433 & 445 (collecting cases).

298. The Department asserted authority to recover for borrower-defense losses in 1994. *See* William D. Ford Federal Direct Loan Program, 59 Fed. Reg. 61,664, 61,696 (Dec. 1, 1994) (to be codified at 34 C.F.R. § 685.206(c)(3)) (providing that the Secretary may "initiate an appropriate proceeding" to recover borrower-defense losses from "the school whose act or omission resulted in the borrower's successful defense against repayment"). In addition to providing for recovery from institutions in individual cases, *see* Student Assistance General Provisions, 81 Fed. Reg. 75,926, 76,084 (Nov. 1, 2016) (to be codified at 34 C.F.R. § 685.222(e)(7)), the 2016 rules provided for recovery from institutions for the Secretary's recovery of losses under the new group process for borrower-defense claims. *See id.* at 76,085 (to be codified at 34 C.F.R. § 685.222(h)(5)(i)). An association of institutions challenged the recoupment provisions of the 2016 rules, and the District Court for the District of Columbia denied the association's request for a preliminary injunction without reaching the merits. *See* Cal. Ass'n of Priv. Postsecondary Schs. v. DeVos, 344 F. Supp. 3d 158, 180 (D.D.C. 2018). The 2019 rules eliminated the group process but not the provision for recovery from institutions on individual claims. *See* Student Assistance General Provisions, 84 Fed. Reg. 49,788, 49,929 (Sept. 23, 2019) (to be codified at 34 C.F.R. § 685.206(e)(16)).

299. *See* 20 U.S.C. § 1099c(c)(1)(C) (directing the Secretary to assess whether institutions have the financial responsibility required to participate in student loan programs, including whether the "institution is able . . . to meet all of its financial obligations, including (but not limited to) . . . repayments to the Secretary for liabilities . . . incurred in programs administered by the Secretary"); 34 C.F.R. § 668.175(c) (2020) (requiring letter of credit or other financial protection if institution fails to meet financial responsibility standards).

300. *See* discussion *infra* Part IV.C.1.

coerced, debtors in a position to benefit from the article's proposal would, by hypothesis, have shown that payment entails hardship and thus would have shown some degree of inability to pay.[301]

Discharging loans arising from school misconduct is more than just consistent with policies relevant to interpreting "undue hardship." It affirmatively advances the goals of the federal student loan programs, which are relevant to interpreting the undue-hardship provision.[302] Student loan bankruptcy nondischargeability entered the law through an amendment to the Higher Education Act, which governs federal student loan programs, and the nondischargeability provision affects primarily loans made under federal programs.[303] When it comes to Section 523(a)(8), student loan policy is bankruptcy policy.

The goals of the federal student loan programs include equalizing access to education,[304] creating an educated population,[305] promoting freedom of career choice,[306] and providing a benefit to students.[307] Discharge helps achieve the first three goals by giving the borrower a chance to pursue an education that is actually valuable without the burden of debt. Discharge even more clearly advances the last goal: To the extent student loans finance payments for schooling that result in no equivalent value to the borrower,[308] they harm students rather than aiding them. Moreover, the fact of being victimized or coerced is a form of student harm, as is giving up time and earnings to attend a program that one would not have voluntarily chosen with full and accurate information. Bankruptcy can alleviate all these harms.

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301. *Cf.* Bruckner et al., *supra* note 29, at 191 (arguing that when debtors meet certain defined criteria indicating inability to pay, government consent to discharge "would be more cost-effective for the taxpayer" than contesting discharge).

302. *See* Hunt, *supra* note 23, at 763–66 (arguing that "undue hardship" must be interpreted to advance the goals of the student loan programs on the ground that related statutes are to be construed together).

303. *See* Hunt, *Help*, *supra* note 29, at 1302–04.

304. *See* Hunt, *supra* note 23, at 732–36.

305. *See id.* at 736–38.

306. *See id.* at 738–40.

307. *See id.* at 740–42.

308. This condition could exist even if the schooling is of some value. If the borrower paid $30,000 for education worth $10,000, $20,000 of the price would not be exchanged for equivalent value. As discussed, the borrower arguably should not have to repay even $10,000 in this case. *See* discussion *supra* Part III.A.

3. Creditor-Side Conduct Is Considered in Applying Other Nondischargeability Provisions

Courts' application of provisions analogous to Section 523(a)(8) further confirms that they can consider school conduct in evaluating claims of undue hardship. The requirement to show undue hardship as a condition of getting a discharge is unique to student loans. However, the Code contains several other provisions that broadly have to do with whether the debtor "deserves" a discharge. The text of these statutory provisions focuses squarely on the debtor's conduct (or misconduct) and does not address creditors at all, but when courts apply the provisions, they nevertheless consider whether creditors have behaved equitably.

In the typical student loan case, the creditor is the federal government and not the school. It might be argued that showing that creditor conduct is relevant to discharge does not show that school conduct is relevant. However, Part III.C explains why the government as lender is better positioned than student borrowers to prevent and absorb the costs of school wrongdoing.

Several provisions of Section 523 of the Bankruptcy Code render certain debts nondischargeable because of debtor misconduct. For example, many fraudulently incurred debts are nondischargeable,[309] as are debts arising from the debtor's embezzlement or related activity,[310] or from the debtor's infliction of "willful and malicious injury."[311] When a creditor seeks to have the court find a debt nondischargeable under these provisions, the debtor frequently argues that the creditor's own unclean hands bar the effort.[312]

The leading view appears to be that the unclean-hands defense is available in such nondischargeability proceedings: At least two federal courts of appeals have held that it is,[313] and the author has located no case clearly to

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309. *See* 11 U.S.C. § 523(a)(2) (providing that debts "for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by–(A) false pretenses, a false representation, or actual fraud" are nondischargeable). Special rules apply to fraud relating to the debtor's financial condition. *Id.* § 523(a)(2)(B)(ii).

310. *See id.* § 523(a)(4) (providing that debts for "fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny" are not dischargeable).

311. *See id.* § 523(a)(6).

312. *See infra* notes 313–317 and accompanying text.

313. *See* Northbay Wellness Grp., Inc. v. Beyries, 789 F.3d 956, 959 (9th Cir. 2015) ("[A] plaintiff deemed to have unclean hands cannot obtain a judgment of nondischargeability."); Republic of Rwanda v. Uwimana (*In re* Uwimana), 274 F.3d 806, 810 (4th Cir. 2001) ("A plaintiff with 'unclean hands' is 'not entitled to relief from a court of equity in the form of an order denying the dischargeability of debt.'") (quoting Hutchinson v. Bromley, 126 B.R. 220, 223 (Bankr. D. Md. 1991)), *abrogated on other grounds by* Bullock v. BankChampaign, N.A., 569 U.S. 267 (2013). The U.S. Court of Appeals for the Sixth Circuit found that the Bankruptcy Appellate Panel for that circuit "correctly analyzed and decided the issues before it" when the panel found that

the contrary.[314] This is so even though there is no textual provision that, in so many words, authorizes courts to consider unclean hands in nondischargeability proceedings. Instead, the courts that have found the defense available have located their authority to do so in bankruptcy courts' status as courts of equity.[315]

To be sure, in most reported decisions, courts have found that the specific facts of the cases before them do not support the debtor's unclean-hands defense.[316] But the unclean-hands defense does sometimes succeed.[317] Cases

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unclean hands is not available as a defense in nondischargeability proceedings under Section 727(a),

> noting that unlike an inquiry under a dischargeability proceeding under § 523, which seeks to vindicate only a single creditor's debt, the inquiry in a proceeding under § 727(a) is directed toward protecting the integrity of the bankruptcy system by denying discharge to debtors who engage in objectionable conduct that is . . . broader and more pervasive than a fraud on a single creditor.

Giant Eagle, Inc. v. Monus (*In re* Monus), 167 F. App'x 494, 496 (6th Cir. 2006).

314. The Court of Appeals for the Eleventh Circuit stated that the "propriety of the [creditor's] actions is not a basis" for finding a debt dischargeable. Bullock v. BankChampaign, N.A. (*In re* Bullock), 670 F.3d 1160, 1167 (11th Cir. 2012), *vacated and remanded on other grounds*, 569 U.S. 267 (2013). However, the court did not analyze the issue, stating only that the debtor had cited no case supporting its position. *Id.* The court also noted that the issue of the creditor's misconduct could be more fairly litigated in another forum, *id.* at 1167–68, suggesting that it was not making a categorical determination that the unclean-hands defense was not available.

315. *Northbay Wellness*, 789 F.3d at 959 (holding unclean-hands defense available "[b]ecause bankruptcy courts are courts of equity"); *In re Uwimana*, 274 F.3d at 810 ("[E]quitable powers of bankruptcy courts are 'available only to . . . creditors with clean hands . . . .'" (quoting Carolin Corp. v. Miller, 886 F.2d 693, 698 (4th Cir. 1989)). At least one court has expressed "qualms" about applying the doctrine to nondischargeability claims, noting that such claims are "statutory, not simply equitable." *See* Bello Paradiso, LLC v. Hatch (*In re* Hatch), 465 B.R. 479, 494 (Bankr. W.D. Mich. 2012).

316. *See, e.g.*, Ins. Co. of N. Am. v. Cohn (*In re* Cohn), 54 F.3d 1108, 1117 n.3 (3d Cir. 1995) (finding that debtor did not show creditor's acts were bad enough to activate defense); *In re Uwimana*, 274 F.3d at 810–11 (finding that creditor's wrongdoing was not tied closely enough to the debt in question); *Northbay Wellness*, 789 F.3d at 961 (finding that debtor's conduct was worse than creditor's); Kaye v. Schack (*In re* Schack), No. 16-24794-B-7, 2018 WL 2059804, at *4 (Bankr. E.D. Cal. May 1, 2018) (same).

317. *See* Baek v. Halvorson (*In re* Halvorson), 581 B.R. 610, 637–40 (Bankr. C.D. Cal. 2018), *vacated on other grounds*, No. 8:18-cv-00525 JVS, 2018 WL 6728484 (C.D. Cal. Dec. 21, 2018) (finding that creditor's conduct undermined court-ordered mediation); Greene v. Shaw (*In re* Shaw), No. AP-11-1101-BAH, 2016 WL 1690706, at *8 (Bankr. D.N.H. Apr. 25, 2016) (finding that creditor's decedent was equally culpable with debtor in submitting potentially fraudulent loan application to a third party); Hopper v. Everett (*In re* Everett), 364 B.R. 711, 723 (Bankr. D. Ariz. 2007) (finding that creditors seeking to block discharge of debts incurred for investments in debtors' company had falsely stated to banks that they had received a large equity stake in the company in exchange for their investment).

where it has done so show that bankruptcy courts, as courts of equity, are reluctant to reward culpable creditors with a judgment of nondischargeability, even if the debtor's conduct would otherwise justify such a judgment.

Another debtor-centric requirement for getting a discharge is the rule that the debtor must act in good faith in relation to the bankruptcy.[318] There is at least one recent instance in which a bankruptcy court weighed creditor misconduct in evaluating a challenge to the debtor's good faith, although the debtor's discharge was not directly at issue.[319] As with the use of the unclean-hands defense in the nondischargeability context, there is no explicit statutory authorization for considering the creditor's wrongdoing in this setting; again the court relied on the proposition that "bankruptcy courts . . . are courts of equity and 'apply the principles and rules of equity jurisprudence'" for its authority to do so.[320]

This argument here is that these precedents support a court's consideration of school misconduct in an undue-hardship proceeding, not that a debtor can directly invoke the doctrine of unclean hands to get a discharge of federal direct student loans. Unclean hands is typically applied as a defense, and the student loan debtor in an undue-hardship proceeding is at least arguably more akin to a plaintiff pressing a cause of action.[321] Moreover, it is not clear that the doctrine can be invoked against the government at all, although cases holding that it cannot be so used often involve enforcement actions in the public interest rather than situations where the government is merely a creditor.[322]

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318. *See* 11 U.S.C. § 707(b)(1), (b)(3)(A) (requiring courts, when deciding whether to dismiss a debtor's Chapter 7 for "abuse," to consider "whether the debtor filed the petition in bad faith"); *id.* § 1129(a)(3) (requiring that courts only confirm Chapter 11 plans when "proposed in good faith"); *id.* § 1325(a)(3), (a)(7) (requiring good faith in Chapter 13 petitions and plans).

319. *See In re* Mabone, 471 B.R. 534, 536, 538–39 (Bankr. E.D. Mich. 2012) (denying secured car lender's claim of debtor's bad faith on the basis of unclean hands where secured creditor had intentionally disabled repossessed car before returning it to debtor).

320. *Id.* at 538 (quoting Young v. United States, 535 U.S. 43, 50 (2002)).

321. To discharge a student loan, the debtor must initiate an adversary proceeding by serving a summons and complaint. *See* United Student Aid Funds, Inc. v. Espinosa, 559 U.S. 260, 263 (2010). The debtor has the burden of proving undue hardship. *See* Nichols v. Align W. States Learning Corp. (*In re* Nichols), 605 F. App'x 660, 661 (9th Cir. 2015) (citing Rifino v. United States (*In re* Rifino), 245 F.3d 1083, 1087–88 (9th Cir. 2001)).

322. *See* Bartko v. Sec. Exch. Comm'n, 845 F.3d 1217, 1227 (D.C. Cir. 2017) ("[T]he Supreme Court has left open the question of whether there exists a 'flat rule that [unclean hands] may not in any circumstances run against the Government . . . .'" (quoting Heckler v. Cmty. Health Servs., 467 U.S. 51, 60 (1984)); United States v. DynCorp Int'l LLC, 282 F. Supp. 3d 51, 58 (D.D.C. 2017) ("The unclean hands doctrine 'may not be invoked against a governmental agency which is attempting to enforce a congressional mandate in the public interest.'" (quoting Sec. Exch. Comm'n v. Gulf & W. Indus., Inc., 502 F. Supp. 343, 348 (D.D.C. 1980)).

The argument for considering creditor misconduct in student loan bankruptcies is stronger in at least two respects than the case for considering such wrongdoing in the debtor-fraud and debtor-good-faith contexts just discussed. First, the statutory authorization is clearer. The unclean-hands cases involve provisions that are triggered by the debtor's fraud or bad faith, not the creditor's. Although the test of Section 523(a)(8) focuses on the debtor's undue hardship, the qualifier "undue" opens the analysis up to factors other than the debtor's conduct.[323]

Second, in the cases just discussed, the court decided that the creditor's unclean hands barred the creditor's claim even assuming the debtor engaged in serious misconduct such as fraud or bad-faith filing. In the typical student loan case, there is no comparable assumption of wrongdoing on the debtor's part.

The argument for considering school misconduct in student loan bankruptcy is weaker than the argument for considering creditor misconduct in the cases above in one respect. In the cases just discussed, the creditor was more culpable than the government creditor typically is in student loan cases.[324] However, alleged school wrongdoing has been on a par with the creditor wrongdoing in the unclean-hands cases, and Part III.C argues that the losses from school misconduct should fall on the government rather than the student debtor. Moreover, the cases show that the comparative severity of the debtor's and the creditor's bad behavior is relevant.[325] In the typical student loan case, the debtor has done nothing wrong other than perhaps failing to pay debts on time. Drawing an analogy to the unclean-hands doctrine, the threshold for considering creditor misconduct should be correspondingly lower in such a case.[326]

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323. *See* discussion *supra* Part I.

324. *See* Baek v. Halvorson (*In re* Halvorson), 581 B.R. 610, 637 (Bankr. C.D. Cal. 2018), *vacated on other grounds*, No. 8:18-cv-00525 JVS, 2018 WL 6728484 (C.D. Cal. Dec. 21, 2018) ("The purpose of the unclean hands doctrine is not to protect the defendant—it is to protect the courts from becoming an aider and abettor of iniquity.").

325. *See supra* notes 316–317 and accompanying text.

326. The nexus between the misconduct alleged and the debt in issue is also relevant in applying the unclean-hands doctrine. Relief was denied when a debtor who had misappropriated funds from a creditor tried to invoke unclean-hands by alleging that the creditor had hidden the funds from a third party. Bruinsma v. Wigger (*In re* Wigger), 595 B.R. 236, 259–60 (Bankr. W.D. Mich. 2018). The nexus between a school's wrongdoing and a student's debt would be strong in the cases of deceptive or unfair enrollment practices covered by the article's proposal. The nexus between a school and the government direct student loan creditor is also strong. *See infra* Part III.C.2.

4. Existing Judicial Tests for "Undue Hardship" Permit Courts To Consider School Misconduct

Part III.B.2 explained how the text of the Bankruptcy Code, properly understood, supports this article's proposal. The Supreme Court or a court of appeals sitting en banc could simply adopt the article's suggestion. But most courts adjudicating student loan bankruptcies must follow authoritative precedents interpreting the Code. This section argues that these existing judicial tests do not foreclose consideration of school misconduct. The majority *Brunner* test may, however, unnecessarily crab the inquiry by deeming school wrongdoing relevant only insofar as it affects the borrower's "good faith."

It seems straightforward that the totality-of-the-circumstances test does not exclude consideration of creditor-side conduct.[327] As mentioned, the most recent appellate decision from the Eighth Circuit explaining the test states, "[C]ourts must consider . . . 'any . . . relevant facts and circumstances.'"[328] School conduct thus can be considered if it is "relevant" to whether the debtor should receive a discharge. This article demonstrates that relevance. The fact that the borrower was deceived or strong-armed is an important circumstance tending to justify discharge, and that circumstance can be incorporated directly into the test.

The majority *Brunner* test requires the debtor to prove "good faith efforts to repay the loan[ ]."[329] In applying this element of the test, courts evaluate whether borrower efforts to repay were adequate.[330] When the debtor has not paid as the repayment plan requires, the good-faith-efforts analysis takes account of the debtor's reasons for not paying more.[331] Debtors frequently get

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327. *See* Jiménez & Glater, *supra* note 24, at 186 (recommending that courts consider the possibility of exploitative school misconduct under the totality-of-the-circumstances test).

328. Educ. Credit Mgmt. Corp. v. Jesperson (*In re* Jesperson), 571 F.3d 775, 779 (8th Cir. 2009) (quoting Long v. Educ. Credit Mgmt. Corp. (*In re* Long), 322 F.3d 549, 554 (8th Cir. 2003)). The Bankruptcy Appellate Panel for the First Circuit adopted a similar formulation. *See* Bronsdon v. Educ. Credit Mgmt. Corp. (*In re* Bronsdon), 435 B.R. 791, 798 (B.A.P. 1st Cir. 2010) (citing and quoting Lorenz v. Am. Educ. Servs. (*In re* Lorenz), 337 B.R. 423, 430 (B.A.P. 1st Cir. 2006)) (allowing the court to consider "other relevant facts or circumstances unique to the case" under the totality-of-the-circumstances test). Although the word "unique" might suggest that only idiosyncratic factors pertaining uniquely to the individual debtor are relevant under the test, the court did not apply the test that way. *See id.* at 801–02 (considering generally available IDR programs as part of the "other relevant facts and circumstances" inquiry).

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

330. *See, e.g.*, Educ. Credit Mgmt. Corp. v. Mason (*In re* Mason) 464 F.3d 878, 885 (9th Cir. 2006) (reversing grant of partial discharge because debtor's "inadequate" efforts to find employment and negotiate a repayment plan constituted a lack of good-faith effort to repay).

331. *See* Trudel v. U.S. Dep't of Educ. (*In re* Trudel), 514 B.R. 219, 229 (B.A.P. 6th Cir. 2014).

discharges without making significant, or even any,[332] payments when they have good reasons for not doing so. Such reasons include health problems,[333] the need to care for children or other family members with disabilities,[334] the need to spend a tax refund on necessities such as car repair and medical needs rather than student loan repayment,[335] and so forth.

If student loans are at least in part a product of deception or unfair pressure by the school, that is another justification for not repaying more of them. Neither the text of the test nor any opinion affirmatively excludes such misconduct from the analysis of good faith.

The *Brunner* framework, as established by the actual wording of the test, is rather flexible and has been applied in some cases with great severity[336] and in others more leniently.[337] The opinion in *Brunner* stated in dicta that its rule "may seem draconian" in effect and defended that result on the ground that the outcome "plainly serves the purposes of the guaranteed student loan program."[338]

Specifically, the court found that "strip[ping borrowers] of the refuge of bankruptcy in all but extreme circumstances" was a "quid pro quo" that the government exacted in return for giving students loans without regard to creditworthiness.[339] The court cited no sources supporting its determination that the government strikes such a harsh bargain.[340] Instead, the court's conception of the exchange apparently stemmed from its conviction that imposing onerous bankruptcy terms was fair because students could analyze the deal for themselves: "This is a bargain each student loan borrower strikes

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332. *See* NAT'L CONSUMER L. CTR., *supra* note 190, § 11.4.2.3.1 n.288 (collecting cases).

333. *See* Williams v. Nat'l Collegiate Student Loan Tr. 2004-1 (*In re* Williams), No. 16-10625-CMA, 2017 WL 665050, at *3–4 (Bankr. W.D. Wash. Feb. 17, 2017).

334. *See* Murphy v. United States (*In re* Murphy), No. 15-11240-j7, 2018 WL 2670455, at *8–9 (Bankr. D.N.M. June 1, 2018); *see also* Coplin v. U.S. Dep't of Educ., No. 13-46108, 2017 WL 6061580, at *1–2, *12 (Bankr. W.D. Wash. Dec. 6, 2017).

335. *See* Lamento v. U.S. Dep't of Educ. (*In re* Lamento), 520 B.R. 667, 678 (Bankr. N.D. Ohio 2014) (explaining that the refund was spent on "children's medical needs, school needs, and to repair the 11 year old car").

336. *See* Thomas v. Dep't of Educ. (*In re* Thomas), 931 F.3d 449, 450–51, 455 (5th Cir. 2019) (denying discharge to sixty-two-year-old debtor with incurable diabetic neuropathy that made it impossible to stand, who had not been able to find work in over a year due to her condition, and whose income was $194 per month in food stamps as compared to monthly expenses of $640).

337. *See* Rosenberg v. N.Y. State Higher Educ. Servs. Corp. (*In re* Rosenberg), 610 B.R. 454, 457, 462 (Bankr. S.D.N.Y. 2020) (granting discharge of over $220,000 in student debt).

338. Brunner v. N.Y. State Higher Educ. Servs. Corp. (*In re* Brunner), 46 B.R. 752, 756 (S.D.N.Y. 1985). The reasoning underlying the *Brunner* test is set forth in the district court's opinion in the case. The appellate opinion adopted the district court's test "[f]or the reasons set forth in the district court's order." Brunner v. N.Y. State Higher Educ. Servs. Corp., 831 F.2d 395, 396 (2d Cir. 1987).

339. *In re Brunner*, 46 B.R. at 756.

340. *Id.*

with the government. Like all bargains, it entails risk. It is for each student individually to decide whether the risks of future hardship outweigh the potential benefits of a deferred-payment education."[341]

For two reasons, courts in school-wrongdoing cases should not follow the *Brunner* dicta to the effect that the test should be harshly applied. First, the actual, not imagined, purposes of the student loan programs support consideration of school misconduct.[342] Second, borrowers whose schools recruited them through deceptive or unfair means were deprived of their ability "individually to decide whether the risks of future hardship outweigh the potential benefits of a deferred-payment education."[343] The assumption underlying the hypothetical bargain that *Brunner* imagined is not met in the case of school misconduct—a case the court did not address. Thus, in such a case, courts should apply *Brunner* leniently, specifically by weighing the school's wrongdoing.

Even so, the *Brunner* test may obstruct giving due weight to school misconduct. If school misconduct affects analysis only of the borrower's good-faith efforts to repay, it might be relevant only insofar as it helps justify a questionable repayment record.[344] Borrowers with strong repayment records thus might not be able to use school wrongdoing to their advantage in proving undue hardship.

It is not clear that school misconduct is directly relevant to the other two elements of the *Brunner* test, which go to the existence and duration of the hardship that repayment would inflict on the borrower.[345] It would, however, be reasonable to relax these requirements in school-misconduct cases, given the unfairness involved in making borrowers pay for schooling when they were induced to purchase it by deception or unfair coercion. It does not make sense to require as much suffering for discharge of such debts as is required for discharge of fairly induced ones. Courts in *Brunner* jurisdictions should employ a sliding scale, under which a strong showing of good faith (bolstered by school misconduct) could justify relief on a lesser showing of hardship.

Precedent may be an obstacle here in some cases. The demands of some courts, discussed in Part I, that hardship be more severe than is usual for bankrupt debtors could obstruct use of a sliding scale in a minority of jurisdictions by imposing a uniform, high bar on the required showing of

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341. *Id.*

342. *See* discussion *supra* Part III.B.2.

343. *In re Brunner*, 46 B.R. at 756.

344. *See* Pa. Higher Educ. Assistance Agency v. Faish (*In re* Faish), 72 F.3d 298, 306 (3d Cir. 1995) ("Equitable concerns or other extraneous factors not contemplated by the *Brunner* framework may not be imported into the court's analysis to support a finding of dischargeability.").

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

hardship. However, these decisions need not be so interpreted.[346] A few other decisions state that the three elements of *Brunner* are to be applied "individually."[347] "Individually" might imply "independently," i.e., without a sliding scale. But the terms are not necessarily equivalent, and the cases have not equated them.

C. Consumer Policy Supports the Article's Proposal

The preceding section argued that school deception or coercion reduces the borrower's responsibility to repay and that actual financial losses from discharge are likely to be less than the face amount of the discharged debt because borrowers facing hardship are unlikely ever to repay in full. Even granting one or both of these propositions, the question remains why the federal government should absorb any financial losses that discharge does cause.

Arguably, the fact that a bad actor (the school) victimized an innocent party (the student) is not a reason to impose the resulting loss on another innocent party (the government). Senator Lamar Alexander made the point succinctly in explaining his vote against the joint resolution that would have repealed the 2019 borrower defense rule: "If your car is a lemon, you don't sue the bank—you sue the dealer."[348]

1. The FTC Holder Rule

But Senator Alexander was wrong or at least made the point too broadly. Since 1976,[349] the FTC's Holder Rule[350] has required that consumer credit contracts contain language making holders of the contracts "subject to all claims and defenses which the debtor could assert against the seller of goods or services."[351] As Professor (later Dean and Associate Provost) Julia Patterson Forrester has noted, "The FTC sought, with this Rule, to shift risks of seller misconduct to creditors who could either absorb the costs of

346. *See* discussion *supra* note 73 and accompanying text.

347. *See, e.g.*, *In re Faish*, 72 F.3d at 306; Tinsley v. U.S. Dep't of Educ. (*In re* Tinsley), No. 17-28611-ABA, 2018 WL 6819515, at *5 (Bankr. D.N.J. Dec. 26, 2018); Regan v. U.S. Dep't of Educ. (*In re* Regan), 590 B.R. 567, 574 n.8 (Bankr. D.N.M. 2018); Belcher v. Columbia Univ. (*In re* Belcher), 287 B.R. 839, 844 (Bankr. N.D. Ga. 2001); Hollister v. Univ. of N.D. (*In re* Hollister), 247 B.R. 485, 490 (Bankr. W.D. Okla. 2000).

348. *See* Green & Cowley, *supra* note 49.

349. *See* Promulgation of Trade Regulation Rule and Statement of Basis and Purpose, 40 Fed. Reg. 53,506, 53,506 (Nov. 18, 1975) (providing for 1976 effective date).

350. *See* 16 C.F.R. pt. 433 (2020).

351. *See* § 433.2.

misconduct or return the costs to sellers."[352] At least forty states reportedly have analogous statutes.[353]

A "[c]onsumer credit contract" under the Rule includes a "[p]urchase money loan,"[354] which in turn includes "[a] cash advance which is received by a consumer" that is applied "in whole or substantial part, to a purchase of goods or services from a seller who (1) refers consumers to the creditor or (2) is affiliated with the creditor by common control, contract, or business arrangement."[355] This language appears to cover cases where a school refers students to a lender that issues loans that the students use to pay the school.

Courts have applied the Holder Rule to loans made under the older Federal Family Education Loan program to fund attendance at proprietary institutions,[356] and Department staff has acknowledged that the Holder Rule applies to such loans.[357] The Holder Rule also would seem to apply directly to private loans arranged by the school, at least if the school is a for-profit institution.[358] However, there appears to be no published case in which a party argued that the Rule applies to federal direct loans.[359] The FTC's jurisdiction

352. Julia Patterson Forrester, *Constructing a New Theoretical Framework for Home Improvement Financing*, 75 OR. L. REV. 1095, 1107–08 (1996).

353. *See* NAT'L CONSUMER L. CTR., *supra* note 190, § 10.6.4.4.4.

354. *See* 16 C.F.R. § 433.1(i) (2020).

355. *See id.* § 433.1(d).

356. *See, e.g.*, Morgan v. Markerdowne Corp., 976 F. Supp. 301, 310–12 (D.N.J. 1997); Jackson v. Culinary Sch. of Wash., 788 F. Supp. 1233, 1248–51 (D.D.C. 1992). *But see, e.g.*, Armstrong v. Accrediting Council for Continuing Educ. & Training, Inc., 168 F.3d 1362, 1368 (D.C. Cir. 1999) (declining to apply Holder Rule to a loan that originated during period when FTC was not enforcing Holder Rule as to guaranteed student loans). The question of the Holder Rule's direct applicability to loans issued under the federal guaranteed student loan program became less urgent in 1994 because the Department adopted, for for-profit institutions in the program, a promissory note that included a notice very similar to that required under the Holder Rule. *Id.* at 1365, 1367–68. The Department issued a rule requiring all institutions to include Holder-Rule-like language in 2007. *See* Federal Perkins Loan Program, 72 Fed. Reg. 61,960, 61,977–78, 62,001 (Nov. 1, 2007) (to be codified at 34 C.F.R. pt. 674, 682, 685).

357. U.S. Dep't of Educ., Opinion Letter, Overview: Federal Trade Commission (FTC) Holder Rule (July 2, 1993), https://library.nclc.org/sites/default/files/DOE_Holder.pdf [https://perma.cc/W8TM-ZVE2].

358. The Holder Rule may not apply to loans to finance attendance at private nonprofit or public institutions. The rule regulates "sellers," § 433.2, and a "seller" is defined as a type of "person." *See id.* § 433.1(j). A "person" in turn is defined as "[a]n individual, corporation, or any other business organization." *Id.* § 433.1(a). For private loans arranged by for-profit institutions, the fact that the Holder Rule covers them supports consideration of school wrongdoing in bankruptcy, as Part III.C.2 argues.

359. The statement in the text is based on the following search in Westlaw's "All Cases" database, conducted May 20, 2020: "holder rule" and "student loan."

probably does not extend to loans made by the government,[360] and in any event, the borrower defense rule in effect until 2018 was substantively similar to the Holder Rule.[361]

Even assuming the Holder Rule does not apply by its terms to federal direct student loans, the FTC's explanation of the Rule articulates policies relevant to evaluating undue hardship in bankruptcy. Starting from the proposition that "[c]onsumers are generally not in a position to evaluate the likelihood of seller misconduct in a particular transaction"[362] so that "[m]isconduct costs are not incorporated in the price of the goods or services"[363] or in financing terms, the FTC decided to "reallocat[e]" and "internalize" the costs of seller wrongdoing.[364] Specifically, because lenders were "in a better position than the buyer to return seller misconduct costs to sellers, the guilty party,"[365] making lenders responsible for the wrongdoing of related sellers would "reduce the costs of seller misconduct in the marketplace."[366] Where it was not economical for the lender to return the costs to the seller, the FTC determined that the lender should "absorb" the cost.[367] Accordingly, the FTC found that "it is an unfair practice for a seller to employ procedures in . . . the financing of a consumer sale which separate the buyer's duty to pay . . . from the seller's reciprocal duty to perform as promised."[368]

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360. The FTC is authorized to regulate the practices of "persons, partnerships, or corporations." 15 U.S.C. § 45(a)(2). There is a "longstanding interpretive presumption" in statutory interpretation "that 'person' does not include the sovereign." Vt. Agency of Nat. Res. v. United States *ex rel.* Stevens, 529 U.S. 765, 780 (2000).

361. Until the 2016 borrower defense rule went into effect by court order in late 2018, *see supra* note 201 and accompanying text, the rule provided for a borrower defense based on "any act or omission of the school attended by the student that would give rise to a cause of action against the school under applicable State law." Student Assistance General Provisions, 81 Fed. Reg. 75,926, 76,080 (Nov. 1, 2016) (to be codified at 34 C.F.R. pt. 685). This appears similar to the Holder Rule's provision that a lender and its assigns are "subject to all claims and defenses which the debtor could assert against the seller of goods or services." *See supra* note 351 and accompanying text.

362. Promulgation of Trade Regulation Rule and Statement of Basis and Purpose, 40 Fed. Reg. 53,506, 53,522 (Nov. 18, 1975).

363. *Id.*

364. *Id.* at 53,523.

365. *Id.*

366. *Id.*

367. *Id.*

368. *Id.* at 53,522.

2. Holder Rule Principles and School Misconduct

The Holder Rule thus recognizes that when a seller refers a borrower to a lender, the costs of the seller's misconduct against the borrower should fall in the first instance on the lender and not the borrower. The basic premise of the Holder Rule—that the lender is better able than buyers to return misconduct costs to sellers—is satisfied in the case of federal direct loans.

From the beginning, the borrower defense rule has provided for federal recovery from institutions of losses resulting from its application.[369] Recovery is through an administrative proceeding the Department itself administers.[370] A student loan borrower, by contrast, must successfully sue a school in order to make the school pay the costs of its misconduct. Many commenters have pointed out the deficiencies in this approach.[371]

Probably more important, the Department has the power to police schools' behavior by limiting or terminating the school's eligibility for federal loan funds. Substantial misrepresentations to students are not just a basis for borrower defense; they are also forbidden by Department regulations.[372] After an administrative process, the Department can impose fines of up to $58,328 per violation.[373] More significantly, the Department can limit or terminate an institution's participation in the federal student loan programs if the

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369. *See* William D. Ford Federal Direct Loan Program, 59 Fed. Reg. 61,664, 61,696 (Dec. 1, 1994) (to be codified at 34 C.F.R. § 685.206(c)(3)) (authorizing Secretary to "initiate an appropriate proceeding" to recover borrower-defense losses from "the school whose act or omission resulted in the borrower's successful defense against repayment").

370. *See* 34 C.F.R. § 668.81(a)(5) (2020) (providing that 34 C.F.R. pt. 668 subpart G furnishes the rules for Department recovery on borrower-defense claims); *id.* § 668.87 (setting forth procedures applicable specifically to Department's recovery of borrower-defense losses from institutions); *id.* §§ 668.88–668.92 (setting forth general administrative procedures that apply to proceedings to recover borrower defense losses from institutions).

371. *See, e.g.*, Blake Shinoda, *Enabling Class Litigation as an Approach to Regulating For-Profit Colleges*, 87 S. CAL. L. REV. 1085, 1109 (2014) (noting that "several commentators have highlighted the weaknesses inherent in defrauded student lawsuits"); Rebecca E. Reif, Note, *Knowledge Is Power: Reform of For-Profit Educational Institutions on an Individual and Institutional Level*, 61 DRAKE L. REV. 251, 254 (2012) (referring to the "ultimate failure[ ] of individuals who invoke traditional state tort and contract causes of action such as educational malpractice, fraudulent misrepresentation, and negligent misrepresentation for individual recovery"); Aaron N. Taylor, *"Your Results May Vary": Protecting Students and Taxpayers Through Tighter Regulation of Proprietary School Representations*, 62 ADMIN. L. REV. 729, 763–68 (2010) (reviewing cases and concluding that contract and tort law "provide only narrow paths to recovery in cases where misrepresentation or fraud is alleged"); Patrick F. Linehan, *Dreams Protected: A New Approach to Policing Proprietary Schools' Misrepresentations*, 89 GEO. L.J. 753, 754 (2001) ("Unfortunately, existing legal doctrine and regulatory regimes are ill-suited to protect proprietary school students from such predatory marketing practices.").

372. *See* § 668.71(a).

373. *See id.* § 668.84(a)(1).

institution "substantially misrepresents the nature of . . . its educational program, its financial charges, or the employability of its graduates."[374]

In addition, the Department probably has the legal authority to adopt rules that would terminate institutions' participation in the federal student loan program based not just on deception but on a broader range of misconduct, including unfair business practices.[375] Higher education institutions, especially for-profit ones, rely heavily on such funds,[376] so such termination is likely to be a death sentence in many cases.[377] Individual student borrowers have no analogous power to discipline institutions.

In addition to being better situated than individual borrowers to prevent school-misconduct losses, the federal government is better able to "absorb" such losses when they do occur. Bankruptcy scholars have long argued that parties that can diversify risks are better positioned to bear them.[378] The

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374. *See id.* § 668.86(a)(1)(ii).

375. *See* 20 U.S.C. § 1221e-3 (conferring on Secretary authority to make "rules and regulations" "in order to carry out functions otherwise vested in the Secretary"); *id.* § 3474 (granting the 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"). The student loan program under Title IV of the Higher Education Act is a program that the Secretary "carr[ies] out," as relevant to the cited provisions. *See* Ass'n of Priv. Sector Colls. & Univs. v. Duncan, 110 F. Supp. 3d 176, 201 (D.D.C. 2015), *aff'd*, 640 F. App'x 5 (D.C. Cir. 2016). These grants of authority seem to authorize the Secretary to forbid a wide array of school misconduct by regulation, and the Secretary is expressly authorized to limit, suspend, or terminate schools' participation in student loan programs if they violate regulations. *See* 20 U.S.C. § 1094(c)(1)(F). A possible counterargument is that the express authorization to limit, suspend, or terminate participation for substantial misrepresentations in the specified categories listed in the current regulations, *see id.* § 1094(c)(3)(A), acts to limit the Secretary's authority to sanction institutions for other misrepresentations.

376. *See* Robert Kelchen, *How Much Do For-Profit Colleges Rely on Federal Funds?*, BROOKINGS: BROWN CENTER CHALKBOARD (Jan. 11, 2017), https://www.brookings.edu/blog/brown-center-chalkboard/2017/01/11/how-much-do-for-profit-colleges-rely-on-federal-funds/ [https://perma.cc/XCT8-VP3N] ("[A] sizable percentage of for-profit colleges get between 80 percent and 90 percent of their revenue from federal financial aid."). One analysis of 2016–17 NCES data indicates that the for-profit sector may be as much as eighty percent funded by federal student loans. *See* Jee Whan (James) Youn, Research Findings on Federal Student Loans in Post-Secondary Education (2020) (unpublished manuscript) (on file with author).

377. *See* Bruckner, *supra* note 27, at 252 ("[T]erminating access to Title IV funds is a death sentence for most [institutions of higher education]."); Dundon, *supra* note 268, at 393 (describing cutoff from federal dollars as "the higher education death penalty").

378. *See, e.g.*, Elizabeth Warren & Jay Lawrence Westbrook, *Contracting Out of Bankruptcy: An Empirical Intervention*, 118 HARV. L. REV. 1197, 1232 (2005) (arguing against shifting bankruptcy risks to employees because "although most creditors have the option of spreading their risks by extending credit to several customers, this option is not available to employees, who are unlikely to work for more than a single employer"); Steven Kropp, *Collective Bargaining in Bankruptcy: Toward an Analytical Framework for Section 1113*, 66 TEMP. L. REV.

government can spread borrower-defense costs over millions of student loans, while each student borrower is likely to attend only one or a few schools. Comparing the federal government to an individual borrower, the federal government is much more likely to suffer *some* borrower-defense losses under this article's proposal. But the government's loss as a percentage of its total student loan outlay is in effect certain to be smaller and more predictable than the individual's loss as a percentage of their education spending.[379] This risk-spreading argument is separate from another defensible claim: that the federal government, with its vast resources,[380] is simply better able to afford losses than individual bankrupt borrowers.

Finally, schools' relationships with federal student loans appears, if anything, closer than the "referral" relationship that triggers the Holder Rule.[381] Under the program participation agreement that institutions enter in order to receive federal direct student loan funds, the institution agrees to "originate" loans made under the program,[382] as contemplated by the Higher Education Act.[383] The Department has explained that "[a]s a loan 'originator' for the Department, the school is the authorized agent of the Department."[384] Origination, where the school actually carries out part of the process of

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697, 706–07 (1993); Elizabeth Warren, *Bankruptcy Policy*, 54 U. CHI. L. REV. 775, 790 (1987); Douglas Bordewieck & Vern Countryman, *The Rejection of Collective Bargaining Agreements by Chapter 11 Debtors*, 58 AM. BANKR. L.J. 293, 312–13 (1983). Scholars have also supported placing risks on the parties best able to bear them in discussing other commercial contexts. *See* Jim Hawkins, *Protecting Consumers as Sellers*, 94 IND. L.J. 1407, 1439 (2019) (arguing that sellers are better positioned to bear risks than buyers "because they can spread the cost of the risk over numerous other deals"); Larry T. Garvin, *Small Business and the False Dichotomies of Contract Law*, 40 WAKE FOREST L. REV. 295, 304–05 (2005) ("[S]elf-insurance is not nearly as good an option for an individual as for a business. With fewer transactions, the consumer cannot assume that routine fluctuations will average smoothly.").

379. For an account of diversification's ability to reduce the probability of a relatively large loss while increasing the probability of a smaller loss, and to make losses more predictable, see JONATHAN BERK & PETER DEMARZO, CORPORATE FINANCE 341–43 (5th ed. 2020).

380. *See* CONG. BUDGET OFF., TABLE 1: CBO'S MARCH 2020 BASELINE BUDGET PROJECTIONS, BY CATEGORY, https://www.cbo.gov/about/products/budget-economic-data#2 [https://perma.cc/PMU8-FPZW] (select "Mar 2020" under "10 Year Budget Projections") (reflecting federal government revenues of $3.463 trillion and outlays of $4.447 trillion for 2019).

381. The Department has indicated that a referral relationship exists where the school "recommends" a lender to its students with the lender's knowledge. *See* U.S. Dep't of Educ., *supra* note 357.

382. *See* Student Assistance General Provisions, 81 Fed. Reg. 39,330, 39,358 (June 16, 2016) (notice of proposed rulemaking).

383. *See* 20 U.S.C. § 1087d(b)(3) (providing that agreement between the Department and school for origination of federal direct loans shall "provide that the institution . . . will originate loans to eligible students and parents in accordance with this part").

384. Student Assistance General Provisions, 81 Fed. Reg. 75,926, 75,931 (Nov. 1, 2016) (to be codified at 34 C.F.R. pt. 668, 682, 685) (providing for July 1, 2020 effective date).

making the loan, is an even stronger basis for holding the lender responsible for school misconduct than is referral.[385]

Regulations confirm the close relationship between the Department and schools in making federal direct loans. They provide that when a school "originate[s]"[386] direct loans, it is responsible for ascertaining and "provid[ing] to the Secretary"[387] information including "[t]he borrower's eligibility for a loan,"[388] "[t]he student's loan amount,"[389] and "[t]he anticipated and actual disbursement date or dates and disbursement amounts."[390] Regulations also prescribe sixteen topics that required entrance counseling must cover.[391] An "Origination Process Overview" on the Department's website spells the origination process out in even more detail.[392]

And the Department and institutions are even more deeply entwined than the agency relationship created by schools' role as originators might suggest. The Department has explained that "the scope of the . . . Direct Loan Program . . . extends far beyond the simple act of originating the loan on behalf of the Department; the HEA [Higher Education Act] itself regulates a broad range of school actions *as they relate to Direct Loan participation*."[393]

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385. Even before the Department concluded in 1994 that a referral relationship triggered lender liability under the Holder Rule, it had determined that an origination relationship, defined as one in which the school performs "substantial functions or responsibilities normally performed by lenders," was sufficient to make the lender responsible for the school's loan-related acts and omissions. NAT'L CONSUMER L. CTR., *supra* note 190, § 10.6.4.4.2; 34 C.F.R. § 682.604(f)(2)(iii) (1993).

386. 34 C.F.R. § 685.301(a)(1) (2020).

387. *Id.* § 685.301(a)(2).

388. *Id.* § 685.301(a)(2)(i).

389. *Id.* § 685.301(a)(2)(ii).

390. *Id.* § 685.301(a)(2)(iii).

391. *See id.* § 685.304(a)(6)(i)–(xvi).

392. U.S. DEP'T OF EDUC., ORIGINATION PROCESS OVERVIEW 1 (2016), https://ifap.ed.gov/sites/default/files/attachments/2019-07/FSDLProcOriginationProcOverview.pdf [https://perma.cc/3AGZ-UWQG] ("Direct Loan Origination is the process through which your school will determine a student's or parent's eligibility for a William D. Ford Federal Direct Loan (Direct Loan) Program loan and inform the U.S. Department of Education's (the Department's) Common Origination and Disbursement (COD) System of eligibility and loan information."). As part of the origination process, the school "must complete" actions including "[c]onfirm[ing] all student or parent eligibility factors," "[e]valuat[ing] need and determin[ing] Direct Loan [award and] amount," notification of "Master Promissory Note" and "entrance counseling" completion, and "complet[ing] and submit[ting] loan origination information to the COD System." *Id.* Removing any doubt, the document states "your school must . . . ensure that the student or parent has actually completed the MPN [Master Promissory Note] and/or entrance counseling." *Id.* at 4.

393. Student Assistance General Provisions, 81 Fed. Reg. 75,926, 76,023 (Nov. 1, 2016).

To be sure, federal direct student loans differ in their purpose[394] from the for-profit lending that occasioned the Holder Rule.[395] The federal government does not make federal student loans primarily to earn a profit,[396] although the direct loan program has been profitable by the government's official yardstick until recently.[397] But the logic of the Holder Rule does not rest on an assumption of the lender's profit motive. Instead, the critical assumptions about the lender are that it wishes to make loans and that it wishes to avoid losses on those loans, so that it has an incentive to police seller behavior. These assumptions apply to the Department, which is obligated to make direct loans[398] and sees itself as obligated to try to collect them.[399]

IV. WHY BANKRUPTCY?

Part IV considers three issues that fall under the heading of institutional appropriateness. Part IV.A argues that bankruptcy courts have the institutional competence to adjudicate claims of school unfairness. Part IV.B argues that the existence of the administrative borrower-defense discharge does not foreclose bankruptcy relief. Part IV.C argues that bankruptcy can be a practical and effective solution for some victimized borrowers.

A. Institutional Competence

There should be no serious question of bankruptcy courts' basic institutional competence to address questions of school misconduct.

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394. *See* Hunt, *supra* note 23, at 731–42 (discussing the purposes of the federal student loan programs, including providing equality of access to higher education, educating the population for the benefit of the country, enabling free choice of career, and providing a benefit to students).

395. *See* Promulgation of Trade Regulation Rule and Statement of Basis and Purpose, 40 Fed. Reg. 53,506, 53,507 (Nov. 18, 1975) (giving background for rule and mentioning only private lenders).

396. *See* Jonathan D. Glater, *The Narrative and Rhetoric of Student Debt*, 2018 UTAH L. REV. 885, 891 ("The goal of extending [student] loans is to promote access, not repayment.").

397. *See* Emily Wilkins, *Student-Loan Outlook Is Reversed, Showing $31 Billion U.S. Cost*, BLOOMBERG GOV'T (May 7, 2019, 12:00 AM), https://about.bgov.com/news/student-loan-outlook-is-reversed-showing-31-billion-cost/ [https://perma.cc/H8NN-V6ZA] (stating that the Congressional Budget Office (CBO), in 2018, forecast that the student loan program would make an $8.7 billion profit for the federal government over the next ten years, but that in 2019 the CBO forecast a $31 billion loss over the following decade).

398. *See* 20 U.S.C. § 1087b(a) (stating that "The Secretary shall provide . . . funds for student and parent loans" under the direct loan program).

399. *See, e.g.*, Letter from Lynn Mahaffie, *supra* note 61, at 1 (referencing Department's "obligation to collect debts").

Although the undue-hardship test typically has focused on the debtor's conduct, bankruptcy courts routinely address wrongdoing by creditors.

The very recent bankruptcy court case of *In re Beal*, in which the court applied the Holder Rule to reduce a creditor's claim,[400] illustrates the point. In *Beal*, the debtors traded in a vehicle at a dealership and financed the rest of the cost of their new vehicle, thus becoming indebted to Santander Consumer USA.[401] But the dealer breached its contract with the debtors by failing to apply part of the trade-in value to pay off the $3,900 loan on the old vehicle, so that the debtors improperly ended up owing that sum to their original lender.[402] Noting that the debtors' contract with the dealership contained the Holder Rule language making the financier and assignees liable for claims against the seller, the court reduced Santander's claim by the $3,900 the dealer failed to pay off on the old loan.[403] In a deceptive-school case, the school would be analogous to the dealership, the Department to Santander, and the student debtor to the Beals.[404]

The seller's liability in *Beal* arose from breach of contract rather than deception, but bankruptcy courts also regularly adjudicate debtor-side claims of deceptive and unfair practices. They adjudicate such claims against creditors of the debtor and their agents;[405] the Department would be such a

400. No. 19-50053-rlj13, 2019 WL 5057942 (Bankr. N.D. Tex. Oct. 8, 2019).

401. *Id.* at *2.

402. *Id.*

403. *Id.*

404. The Department's responsibility in a student loan case is even clearer than in *Beal* because in *Beal* the dealer merely sold an installment sale contract to Santander, which did not itself make the loan. *Id.* at *2. In the case of a federal direct student loan, the Department is, if anything, more directly tied to any deceptive or unfair practices of the school because the Department makes the loan to the student and disburses the funds directly to the school. *See Disbursements and Receiving Aid*, FED. STUDENT AID OFF., https://studentaidhelp.ed.gov/app/answers/detail/a_id/2102/~/disbursements-and-receiving-aid [https://perma.cc/PBF6-NPHR]. Although the functional difference between the contract-sale and direct-loan methods of financing may not be large, the difference does cut in favor of Department responsibility.

405. Many bankruptcy courts have found that creditors' actual or alleged conduct toward debtors violated state statutes forbidding unfair and deceptive acts and practices (state UDAP statutes). *See, e.g.*, Field v. Bank of Am. (*In re* Gibbs), 522 B.R. 282, 285, 287–88 (Bankr. D. Haw. 2014) (Hawaii statute); *In re* Porter, 498 B.R. 609, 660–61 (Bankr. E.D. La. 2013) (Louisiana statute); McClendon v. Walter Home Mortg. (*In re* McClendon), 488 B.R. 876, 894–95 (Bankr. E.D.N.C. 2013) (North Carolina statute); Bryce v. Lawrence (*In re* Bryce), 491 B.R. 157, 184–86 (Bankr. W.D. Wash. 2013) (Washington statute); Hinson v. Countrywide Home Loans, Inc. (*In re* Hinson), 481 B.R. 364, 376–77 (Bankr. E.D.N.C. 2012) (North Carolina statute); 201 Forest St. LLC v. LBM Fin. LLC (*In re* 201 Forest Street LLC), 409 B.R. 543, 554, 597–98 (Bankr. D. Mass. 2009) (Massachusetts statute); Anderson v. Brokers, Inc. (*In re* Brokers, Inc.), 396 B.R. 146, 160–64 (Bankr. M.D.N.C. 2008) (North Carolina statute); Balko v. Carnegie

creditor in a deceptive-school case. Bankruptcy courts also hear claims of unfair and deceptive practices against parties such as sellers of services[406] that had dealings with the debtor.[407] In a deceptive-school case, the school is such a seller of services.

B. The Borrower Defense Rule Does Not Foreclose Bankruptcy Relief

No matter how strong the normative justification for providing bankruptcy relief to students who were deceived or subjected to strong-arm tactics, courts might be reluctant to do so if granting discharge on this basis runs counter to policies of the Department's borrower defense rule itself. This section argues that the conflict between this article's proposal and the articulated policies of the borrower defense rules is quite limited, and that courts generally have—with good reason—rejected arguments that the Department's administrative relief schemes foreclose bankruptcy relief.

1. No Conflict with Borrower Defense Rule Policies

Bankruptcy relief based on a school's misconduct is compatible with the policies underpinning both the 2016 and 2019 borrower defense rules. Both sets of rules recognize that borrowers may be harmed by institutions' misrepresentations and that such harm is a valid basis for relieving borrowers

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Fin. Grp. Inc. (*In re* Balko), 382 B.R. 717, 719, 725 (Bankr. W.D. Pa. 2008) (Pennsylvania statute); Patterson v. Chrysler Fin. Co. (*In re* Patterson), 263 B.R. 82, 98 (Bankr. E.D. Pa. 2001) (Pennsylvania statute). In some cases, bankruptcy courts' findings that creditors violated UDAP statutes have been reversed on the merits with no allegation that it was improper for the bankruptcy court to hear the consumer-protection claims in the first place. *See, e.g.*, Meyer v. U.S. Bank N.A. (*In re* Meyer), 506 B.R. 533, 549–52 (Bankr. W.D. Wash. 2014) (Washington statute), *rev'd sub nom.* 530 B.R. 767, 776–83 (W.D. Wash. 2015), *aff'd sub nom.* Meyer v. Nw. Tr. Servs. Inc., 712 F. App'x 619 (9th Cir. 2017); Kekauoha-Alisa v. Ameriquest Mortg. Co. (*In re* Kekauoha-Alisa), 394 B.R. 507, 517–18 (Bankr. D. Haw. 2008), *rev'd in relevant part* 407 B.R. 442 (B.A.P. 9th Cir. 2009), *aff'd in part*, *vacated in part* 674 F.3d 1083 (9th Cir. 2012).

406. *See* Goldsmith v. Marsh USA, Inc. (*In re* Glasshouse Techs., Inc.), 604 B.R. 600, 638 (Bankr. D. Mass. 2019) (debtor's insurance broker and risk management consultant); NC & VA Warranty Co. v. Fidelity Bank (*In re* NC & VA Warranty Co.), 554 B.R. 110, 128–30 (Bankr. M.D.N.C. 2016) (debtor's reinsurer); *In re Porter*, 498 B.R. at 620–21 (debtor musical artists' personal manager); Teraforce Tech. Corp. v. Vista Controls, Inc. (*In re* Teraforce Tech. Corp.), 379 B.R. 626, 631, 642–43 (Bankr. N.D. Tex. 2007) (party that had contracted to advertise, market, and sell debtor's products).

407. *See* Adler v. Smith (*In re* Thundervision, L.L.C.), No. 09-11145, 2014 WL 468224, at *7–8 (Bankr. E.D. La. Feb. 5, 2014) (managing member of L.L.C. debtor); Bender v. Saint Felix (*In re* Miller), 418 B.R. 406, 408, 411–12 (Bankr. N.D. Fla. 2009) (purchaser of real property from debtor); *In re Brokers, Inc.*, 396 B.R. at 155, 160–64 (former president of debtor corporation).

from the obligation to repay in some circumstances.[408] The rules differ, however, in the degree of institutional culpability needed for a borrower-defense claim. The 2016 rules provide for borrower defense even for innocent or negligent misrepresentations, stressing that "[w]e believe that an institution is responsible for the harm to borrowers caused by its misrepresentations, even if such misrepresentations cannot be attributed to institutional intent or knowledge and are the result of inadvertent or innocent mistakes."[409] The 2019 rules, however, impose a strict scienter requirement, permitting borrower defense only if the institution acts "with knowledge of its false, misleading, or deceptive nature or with a reckless disregard for the truth."[410]

The 2019 rules acknowledge that a key reason for heightening the institutional culpability needed for borrower defense is protecting schools.[411] Critically, the Department can recover from institutions on borrower-defense claims,[412] and the Department described schools whose students asserted successful borrower-defense claims as being "held liable."[413] There is no

408. *See* Student Assistance General Provisions, 84 Fed. Reg. 49,788, 49,792 (Sept. 23, 2019) ("[W]e have revised the rules to provide a fairer and more equitable process for borrowers to seek relief when institutions have committed acts or omissions that constitute a misrepresentation and cause financial harm to students."); Student Assistance General Provisions, 81 Fed. Reg. 39,330, 39,330 (June 16, 2016) ("The purpose of the borrower defense regulation is to protect student loan borrowers from misleading, deceitful, and predatory practices of, and failures to fulfill contractual promises by, institutions participating in the Department's student aid programs.").

409. Student Assistance General Provisions, 81 Fed. Reg. 75,926, 75,947 (Nov. 1, 2016).

410. Student Assistance General Provisions, 84 Fed. Reg. at 49,927 (to be codified at 34 C.F.R. § 685.206(e)(3)).

411. *See id.* at 49,804 ("We agree with the commenters who argued that a school should not be held liable if it committed an inadvertent mistake . . . . Treating innocent mistakes in the same manner as acts or omissions made with knowledge of their false, misleading, or deceptive nature, places well-performing schools at risk unnecessarily . . . ."); *id.* at 49,804–05 ("The Department has now concluded that the 2016 final regulations' inclusion of misrepresentations that 'cannot be attributed to institutional intent or knowledge and are the result of inadvertent or innocent mistakes' is inappropriate for these final regulations and had the potential to result in vastly increased administrative burden and financial risk to schools and, when the burden proves too great, to the taxpayer. In such a case, a mere mathematical error could lead to devastating consequences to the institution and potentially to its current students . . . ."); *id.* at 49,805 (arguing that including a scienter requirement "better guards the interests of . . . an institution acting in good faith"); *id.* ("We also believe it would be improper to subject an institution . . . to liability and reputational harm for innocent or inadvertent misstatements.").

412. *See id.* at 49,792 ("The Department . . . has a process to recover the losses the Department sustains from institutions as a result of granting borrower defense to repayment discharges.").

413. *Id.* at 49,804.

comparable right to recover in the case of bankruptcy discharge.[414] Thus, concerns about unfairness to institutions are much less important in bankruptcy, where the institutions' funds are not directly at risk. In other words, to the extent there is an interest in protecting students while honoring the Department's inclination not to be too hard on institutions, bankruptcy relief serves that interest.

2. Administrative Discharge Schemes Do Not Foreclose Bankruptcy Relief

Even apart from any actual explicit policy conflict, it might be argued that granting bankruptcy relief based on institutional wrongdoing where the Department has declined to make relief available end-runs the Department's judgment about when discharge for this reason is appropriate. Courts most commonly have rejected such arguments in analogous contexts, however, and rightly so.

For example, student debtors are allowed to seek an administrative discharge from the Department of Education if they have become "permanently and totally disabled,"[415] and the Department has issued regulations defining a total and permanent disability in this context.[416] Nevertheless, the debtor's disability is a recognized consideration under both the *Brunner*[417] and totality-of-the-circumstances tests for bankruptcy discharge.[418] Indeed, empirical studies indicate that poor debtor health is one of the few factors reliably associated with greater likelihood of getting a

414. *See generally* 34 C.F.R. pt. 685 (2020) (regulations governing the Ford Direct Loan Program). The regulations do not provide for recovery from institutions in the event of borrower bankruptcy. The Department could recover through a separate proceeding based on the school's substantial misrepresentation, *see supra* Part III.C.2, but bankruptcy relief itself would not trigger this right.

415. 20 U.S.C. § 1087(a)(1) (FFEL program loans). There appears to be no specific statutory authorization for disability discharge of federal direct student loans, but presumably the general provision that federal direct loans "shall have the same terms, conditions, and benefits" as FFEL loans covers disability discharge. *See id.* § 1087e(a)(1).

416. *See* 34 C.F.R. § 685.102(b) (2020) (defining "totally and permanently disabled"); *id.* § 685.213(a)(1) (applying definition from § 685.102(b) to federal direct loan program).

417. *See, e.g.*, McCoy v. United States (*In re* McCoy), 810 F. App'x 315, 316–17 (5th Cir. 2020) (noting that additional circumstances indicating debtor's inability to repay that are likely to persist, as required by second element of *Brunner* test, "may include illness, disability" (quoting *In re* Oyler, 397 F.3d 382, 386 (6th Cir. 2005))).

418. *See, e.g.*, Educ. Credit Mgmt. Corp. v. Jesperson, 571 F.3d 775, 783 (8th Cir. 2009) (Smith, J., concurring) (noting that factors considered in applying the totality-of-the-circumstances test "include . . . whether there is permanent or long-term disability of the debtor" (quoting McLaughlin v. U.S. Funds (*In re* McLaughlin), 359 B.R. 746, 750 (Bankr. W.D. Mo. 2007))).

discharge.[419] Recent cases confirm that courts frequently point to debtor disability when granting discharge.[420]

The author has located no case in which a student loan holder has been so bold as to claim that the availability of administrative discharge absolutely forecloses the bankruptcy court from considering the debtor's health-related issues. Holders do, however, argue with some frequency that student borrowers must exhaust administrative remedies before seeking discharge or that an undue-hardship proceeding is not ripe until administrative relief has been denied.

Such arguments generally have failed.[421] Courts have recognized that administrative relief is "completely separate and distinct from,"[422] and "does

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419. *See* Jason Iuliano, *An Empirical Assessment of Student Loan Discharges and the Undue Hardship Standard*, 86 AM. BANKR. L.J. 495, 525 (2012) (reporting that people who received discharges differed from those who did not in that they "were more likely to have a medical hardship"); Rafael I. Pardo & Michelle R. Lacey, *The Real Student-Loan Scandal: Undue Hardship Discharge Litigation*, 83 AM. BANKR. L.J. 179, 216 (2009) (recognizing that "the debtor or a debtor's dependent suffering from a medical condition" is significantly associated with amount of debt discharged); 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, 485 tbl.8 (2005) (reporting that debtors who were granted discharge were more likely to be unhealthy than debtors denied discharge).

420. *See* Skelly v. U.S. Dep't of Educ., No. 19-cv-1812-GPC-BLM, 2019 WL 6840398, at *1, *3–5 (S.D. Cal. Dec. 16, 2019) (explaining that plaintiff who alleged she received Social Security disability benefits but had been denied a disability discharge stated a claim of undue hardship based in part on "deteriorating health"); Smith v. U.S. Dep't of Educ. (*In re* Smith), 608 B.R. 236, 240, 244 (Bankr. D. Or. 2019) (granting discharge to debtor with persistent atrial fibrillation, anxiety and depressive disorders, and asthma because "[t]he caselaw does not require a debtor to exhaust all treatment options before discharging a student loan because of an established illness or disability"); Hill v. Educ. Credit Mgmt. Corp., (*In re* Hill), 598 B.R. 907, 917 (Bankr. N.D. Ga. 2019); Pierson v. Navient (*In re* Pierson), No. 17-31687, 2018 WL 4849658 (Bankr. N.D. Ohio Oct. 4, 2018); Smith v. U.S. Dep't of Educ. (*In re* Smith), 582 B.R. 556, 568 (Bankr. D. Mass. 2018).

421. *See* Educ. Credit Mgmt. Corp. v. Mosley (*In re* Mosley), 494 F.3d 1320, 1327 (11th Cir. 2007) (rejecting argument that *Brunner*'s good-faith element required debtor to pursue IDR "or seek an administrative discharge based on disability" before seeking bankruptcy relief from student loans); Nash v. Conn. Student Loan Found. (*In re* Nash), 446 F.3d 188, 193–94 (1st Cir. 2006) (evaluating debtor's claim of undue hardship on the merits despite fact that debtor was potentially eligible for and had not sought administrative discharge); *In re Hill*, 598 B.R. at 920. Other courts have held that the failure to pursue administrative discharge is relevant to the debtor's good faith without finding that the debtor was required to exhaust administrative remedies. *See* Lagueux v. U.S. Dep't of Educ. (*In re* Lagueux), 604 B.R. 249, 251 (Bankr. D.S.C. 2019) ("[A] debtor is not precluded from seeking a discharge under § 523(a)(8) solely because he or she did not first pursue an administrative option."); Miraglia v. U.S. Dep't of Educ. (*In re* Miraglia), 559 B.R. 481, 489 (Bankr. N.D. Ohio 2016); Dorsey v. U.S. Dep't of Educ., 528 B.R. 137, 146 (E.D. La. 2015); Cagle v. Educ. Credit Mgmt. Corp. (*In re* Cagle), 462 B.R. 829, 832 (D. Kan. 2011).

422. *Dorsey*, 528 B.R. at 143–44; *In re Lagueux*, 604 B.R. at 251; *In re Cagle*, 462 B.R. at 831.

not equate with"[423] bankruptcy relief, and that the Department's regulations separately provide for both types of relief.[424] One court observed that Congress reenacted the undue-hardship provision without qualification while the administrative disability discharge regulation was on the books.[425] All these observations apply to the relationship between the borrower defense rule and bankruptcy.[426] On the other side of the ledger, the only court to have found that exhaustion of remedies is generally required in a disability case stated only that the Department "ha[d] the right to evaluate [the debtor's] financial circumstances and apply [its] regulatory procedures," without further explanation.[427]

Without finding that seeking an administrative disability discharge is a prerequisite for bankruptcy relief, most courts that have addressed the issue have found that pursuing such an administrative discharge where it may be available helps the borrower show a good-faith effort to repay.[428] Even so, courts have granted discharge while expressly acknowledging that the borrower failed to pursue administrative relief.[429] This underscores the point that pursuing such remedies is not required.

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423. *Dorsey*, 528 B.R. at 145; *In re Cagle*, 462 B.R. at 832.

424. *Dorsey*, 528 B.R. at 144; *In re Lagueux*, 604 B.R. at 251; *In re Cagle*, 462 B.R. at 831.

425. *Dorsey*, 528 B.R. at 145.

426. Bankruptcy is separate and distinct from the borrower defense rule, just as it is from the disability discharge regulations. Department regulations provide for both borrower defense, *see* discussion *supra* Part II.B, and for bankruptcy relief, *see* 34 C.F.R. § 682.402 (2020); *id.* § 674.49. The undue-hardship exception to nondischargeability was reenacted as recently as 2005, *see* Pub. L. No. 109-8, § 220, 119 Stat. 23, 59 (2005) (amending Section 523(a)(8) of the Bankruptcy Code and retaining the undue-hardship exception), and a borrower defense rule has been on the books since 1994, *see* discussion *supra* Part II.B.

427. *See* VerMaas v. Student Loans of N.D. (*In re* VerMaas), 302 B.R. 650, 660 (Bankr. D. Neb. 2003). In another case, the court held that where the debtor had already received a conditional administrative discharge that would become final if the debtor remained disabled for three years, the debtor's undue-hardship claim was not ripe for decision. *See* Furrow v. U.S. Dep't of Educ., No. 02-33740DRD, 2005 WL 1397156, at *1–2 (Bankr. W.D. Mo. May 24, 2005). The court relied on the finding that denying immediate relief would not harm the debtor because his debt would be discharged after three years absent a change in circumstance, and he did not incur interest charges or have to make payments during that period. *Id.* These circumstances generally will not be present in borrower-defense cases.

428. *See In re Lagueux*, 604 B.R. at 251; Miraglia v. U.S. Dep't of Educ. (*In re* Miraglia), 559 B.R. 481, 489 (Bankr. N.D. Ohio 2016); *Dorsey*, 528 B.R. at 146–47; *In re Cagle*, 462 B.R. at 832.

429. *See* Educ. Credit Mgmt. Corp. v. Mosley (*In re* Mosley), 494 F.3d 1320, 1327 (11th Cir. 2007); Hill v. Educ. Credit Mgmt. Corp., (*In re* Hill), 598 B.R. 907, 922 (Bankr. N.D. Ga. 2019). Debtors who did not pursue administrative relief have also won in procedural contexts where grant of discharge was not directly in issue. *See Dorsey*, 528 B.R. at 150 (reversing dismissal of debtor's case); *In re Lagueux*¸ 604 B.R. at 252 (denying creditor summary judgment); *In re Cagle*, 462 B.R. at 832 (denying creditor's motion to dismiss).

Where an administrative discharge is not a "realistic" solution to student debt, courts have not held the failure to seek one against the borrower.[430] That reasoning applies in the school-deception context, where a major problem with seeking an administrative discharge is the difficulty of showing that the school acted with the scienter required under the 2019 rules.[431] Where the student borrower knows they were deceived but does not have evidence of the school's state of mind, recourse to an administrative remedy would be unrealistic or futile. Even in contexts outside student loan bankruptcy, where exhaustion of administrative remedies is generally required, an exception applies where pursuing the administrative remedy would be futile.[432]

Holders have also argued that the availability of another form of administrative remedy, an IDR plan, blocks bankruptcy relief. Seven courts of appeals have considered the relationship between IDR plans and bankruptcy, and none has endorsed this theory.[433] Although courts generally do find IDR relevant to good faith,[434] the futility of seeking administrative relief under the 2019 borrower defense rule again suggests that the borrower's failure to seek a borrower-defense discharge should not be considered in the school-misconduct context. In any event, several courts of appeals have found that the debtor demonstrated good faith in the case before the court despite not participating in IDR.[435]

The Department itself has abjured any role in defining the bankruptcy term "undue hardship."[436] This disavowal further undermines any claim that considering schools' wrongdoing in interpreting the term would trench upon the Department's authority.

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430. *See In re Mosley*, 494 F.3d at 1327 (noting that debtor was not required to pursue administrative remedies where the bankruptcy court "had sufficient evidence . . . to conclude that these options would not have provided [debtor] a realistic solution to his inability to pay").

431. *See* discussion *supra* Part II.C.

432. *See* CHARLES H. KOCH & RICHARD MURPHY, 4 ADMIN. L. & PRAC. § 12:21 & n.40 (3d ed. 2020) (collecting cases).

433. *See* Hedlund v. Educ. Res. Inst., Inc., 718 F.3d 848, 855 (9th Cir. 2013); Krieger v. Educ. Credit Mgmt. Corp., 713 F.3d 882, 883–84 (7th Cir. 2013); Coco v. N.J. Higher Educ. Student Assistance (*In re* Coco), 335 F. App'x 224, 227–28 (3d Cir. 2009); Roe v. Coll. Access Network (*In re* Roe), 295 F. App'x 927, 931 (10th Cir. 2008); *In re Mosley*, 494 F.3d at 1327; Barrett v. Educ. Credit Mgmt. Corp. (*In re* Barrett), 487 F.3d 353, 363–64 (6th Cir. 2007); Educ. Credit Mgmt. Corp. v. Frushour (*In re* Frushour), 433 F.3d 393, 402–03 (4th Cir. 2005).

434. *See In re Lagueux*¸ 604 B.R. at 251; Miraglia v. U.S. Dep't of Educ. (*In re* Miraglia), 559 B.R. 481, 489 (Bankr. N.D. Ohio 2016); *Dorsey*, 528 B.R. at 146–47; *In re Cagle*, 462 B.R. at 832.

435. *See Hedlund*, 718 F.3d at 855; *Krieger*, 713 F.3d at 883–84; *In re Coco*, 335 F. App'x at 227–28; *In re Mosley*, 494 F.3d at 1327; *In re Barrett*, 487 F.3d at 363–64.

436. *See* Letter from Lynn Mahaffie, *supra* note 61, at 3.

C. Bankruptcy as a Practical Solution for Victimized Borrowers

Another objection is simply that bankruptcy might not be a good solution for many defrauded student loan borrowers. In some respects, however, bankruptcy may actually offer a better solution than even a strong borrower defense rule. For example, bankruptcy may have tax advantages. The Internal Revenue Code provides that bankruptcy discharge of debt does not result in taxable income.[437] There is no comparable provision covering borrower-defense discharge, although the IRS currently provides administrative relief in such cases.[438] Moreover, some victimized borrowers would seek bankruptcy protection even if courts did not consider school wrongdoing; if courts do consider school wrongdoing, they will help borrowers in this group. Nevertheless, it is worth addressing the objection that bankruptcy is not very helpful to victimized borrowers as a class.

1. Attractiveness of Bankruptcy to Victimized Borrowers

Not all victimized student borrowers will be good candidates for bankruptcy. Deciding whether bankruptcy is the right solution for an individual student debtor can involve a complex analysis of student and non-student debt, property, income, willingness to undergo litigation and potential social stigma, and other factors. But the aggregate picture for students at for-profit schools that have been sued or investigated appears bleak, suggesting that bankruptcy could help many such borrowers. According to a 2018 report from the Center for American Progress, the median of such schools' five-year default rates was thirty-one percent.[439] When borrowers who were ninety days delinquent or were not making loan payments for reasons other than further education or military service are included, the median rate of distress is fifty percent.[440]

Chapter 7 bankruptcy involves liquidation of nonexempt property[441] and thus is generally more likely to be advantageous for those with little wealth. Data on for-profit students' wealth does not appear to be available. However,

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437. *See* I.R.C. § 108(a)(1)(A).

438. *See* Rev. Proc. 2020-11, 2020-6 I.R.B. 406 (providing that the IRS "will not assert" that borrowers receiving relief under the borrower defense rule "must recognize gross income as a result of the discharge").

439. *See* Ben Miller, *The Cost of Insufficient Student Loan Accountability*, CTR. FOR AM. PROGRESS (Aug. 30, 2018, 9:53 AM), https://www.americanprogress.org/issues/education-postsecondary/news/2018/08/30/457302/cost-insufficient-student-loan-accountability/ [https://perma.cc/WY6R-GVGG] (median calculation by author).

440. *Id.* (median calculation by author).

441. *See* 11 U.S.C. § 541(a)(1) (providing debtor's property enters bankruptcy estate upon bankruptcy); *id.* § 704(a)(1) (providing for liquidation of estate property in Chapter 7).

for-profit college students earn less[442] and are less likely to be employed[443] than students at public institutions, and for-profit college students are drawn disproportionately from poorer families. Thirteen percent of postsecondary students from the lowest family-income quintile attend for-profit schools, compared with two percent of students from the highest quintile.[444] This data, combined with the loan distress data, suggests that many for-profit students do not accumulate wealth rapidly, making bankruptcy more attractive. Indeed, the IRS has suggested that many such students are likely to be insolvent.[445]

2. Proving Deception and Unfairness

It might be difficult for borrowers to prove some of the types of misrepresentations that have attracted the most attention. For example, the typical bankrupt student loan debtor might not be able to fund significant discovery efforts, so it might be difficult for such a borrower to learn a school's true job placement rates and prove that the school misrepresented these numbers.[446]

Borrowers are, however, in a good position to know of many types of misrepresentations because their own experiences would be contrary to what they were told. Such misrepresentations include those about the nature and cost of the program, whether the program has the necessary accreditation for students to obtain certain licenses, and whether credits are transferable to other institutions.[447] Borrowers who have undergone strong-arm recruiting tactics that might amount to unfair trade practices will know of and be able to testify to them.[448]

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442. *See For Profit Colleges by the Numbers*, CTR. FOR ANALYSIS OF POSTSECONDARY EDUC. & EMP., https://capseecenter.org/research/by-the-numbers/for-profit-college-infographic/ [https://perma.cc/QC3Q-YZZM] (Feb. 2018).

443. *See id.*

444. *See* Paul Fain, *Wealth's Influence on Enrollment and Completion*, INSIDE HIGHER ED (May 23, 2019), https://www.insidehighered.com/news/2019/05/23/feds-release-broader-data-socioeconomic-status-and-college-enrollment-and-completion [https://perma.cc/AU9S-8XP2].

445. *See* Rev. Proc. 2020-11.08, 2020-6 I.R.B. 406 ("[T]he Treasury Department and the IRS believe that most . . . borrowers would be able to exclude from gross income . . . the discharged amounts based on the insolvency exclusion under section 108(a)(1)(B) of the Code; fraudulent or material misrepresentations made by such . . . schools . . . ; or other tax law authority.").

446. *See supra* Part II.A (discussing alleged misrepresentation of employment numbers).

447. *See supra* Part II.A (discussing alleged misrepresentations by schools).

448. *See supra* Part II.A (discussing potentially unfair strong-arm recruiting practices).

Even for subjects such as placement rates, borrowers may be able to adduce[449] findings from investigations by the Department,[450] the CFPB,[451] state attorneys general,[452] or other entities. Consumer class actions also may turn up information about schools' practices.[453]

Borrowers should not be put to the task of proving school misconduct on an individual basis, which is a reason that the Department's group adjudication process was so important. Nevertheless, being able to rely on school misconduct to obtain a bankruptcy discharge should help a significant number of student debtors.

CONCLUSION

The Department's 2019 rules have left victimized student borrowers stranded, with no realistic prospect of administrative relief. Bankruptcy courts should allow such borrowers to discharge their student loans if they show that repayment would entail some hardship and that they were induced to incur the loan through deceptive, unfair, abusive, or unconscionable acts or practices. This suggestion could lead to some losses for the federal government. But with its extensive supervisory powers and diversified portfolio, the government is better able to prevent and absorb losses than are individual student borrowers.

Bankruptcy cannot provide a complete substitute for a robust borrower defense rule. Not all borrowers will want to liquidate their nonexempt property, undergo social stigma, or go through the adversarial process needed to discharge student loans. But many will seek bankruptcy protection, impelled by student debts arising from school misconduct, by other debts, or by a combination. This article's proposal can help these borrowers, who have been left with nowhere else to turn.

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449. *See* FED. R. EVID. 803(8)(A)(iii) (providing exception to hearsay rule for a "record or statement of a public office" that "sets out . . . in a civil case . . . factual findings from a legally authorized investigation"). This rule has been applied in bankruptcy proceedings. *See, e.g.*, Lightsway Litig. Servs., LLC v. Wimar Tahoe Corp. (*In re* Tropicana Ent., LLC), 613 B.R. 587, 592 (Bankr. D. Del. 2020) (admitting administrative report and opinion).

450. *See supra* Part II.A (discussing Department investigation).

451. *See supra* Part II.A (discussing CFPB investigation).

452. *See supra* Part II.A (discussing investigations by state attorneys general).

453. *See, e.g.*, Makaeff v. Trump Univ., LLC, No. 3:10-cv-0940-GPC-WVG, 2014 WL 688164, at *20–21 (S.D. Cal. Feb. 21, 2014) (granting class certification after discovery revealed that the defendant had made similar misrepresentations to a large group of people). Even if a consumer class action brings valuable information to light, it may not result in complete relief for borrowers, so bankruptcy relief would still be useful.