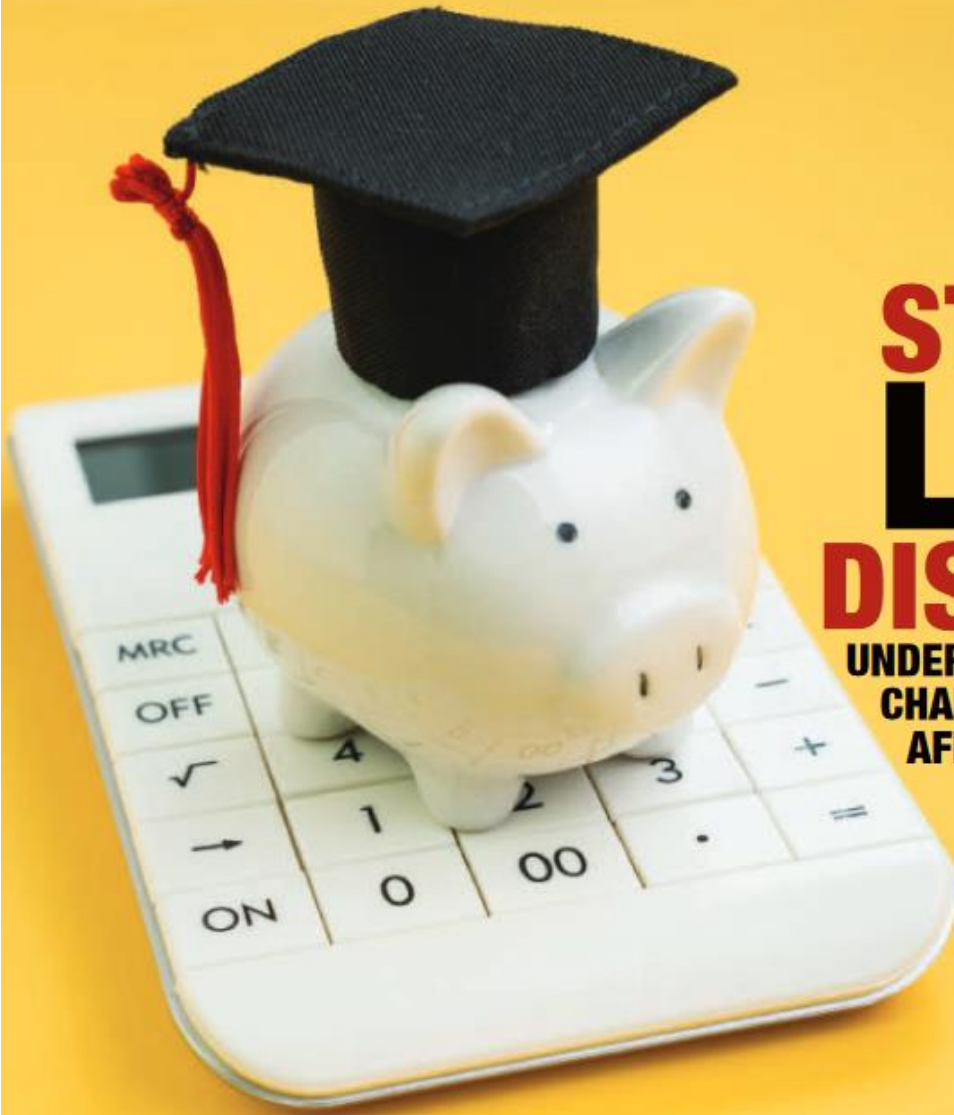


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## STUDENT LOAN DISCHARGE

**UNDERSTANDING THE LATEST  
CHANGES AND HOW THEY  
AFFECT YOUR CLIENTS**

**DOJ Clarifies the Path to  
Student Loan Discharges  
in Bankruptcy**

**How to Serve an  
Adversary Proceeding**



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# DOJ CLARIFIES the Path to Student Loan Discharges in Bankruptcy

Guidance is still new and untested, but it appears to have provided a beacon of light on the horizon.

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**O**n November 17, 2022, the U.S. Department of Justice (DOJ) and Department of Education (DOE) announced new guidance (Guidance) regarding how and when the federal government will agree to discharge federal student loans in bankruptcy. This Guidance represents one of the most seismic changes in consumer bankruptcy practice since the enactment of BAPCPA in 2005. With student loans representing the second largest source of consumer debt in the U.S.<sup>1</sup>, the impact of the Guidance will be far-reaching for millions of distressed debtors who will now have a clearer path and increased likelihood to successfully discharge their federal student loans in bankruptcy.

To be clear, neither the statute (11 U.S.C. § 523 (a)(8)) requiring an “undue hardship” to discharge federal student loans nor the case law interpreting it has changed. The majority standard of review remains *Brunner v New York State Higher Education Services Corp.*, 831 F.2d 395 (2d Cir. 1987) with some courts adopting a totality-of-the-circumstances test. Under *Brunner*, the debtor must demonstrate an inability to maintain a minimum standard of living, the

circumstances must be likely to persist in the future and the debtor must have made good faith efforts to repay the student loans. The totality-of-the-circumstances, on the other hand, requires that courts broadly examine debtor’s ability to repay their loans considering relevant factors such as debtor’s past, present and likely future financial resources, reasonable living expenses for debtor and dependents, and other relevant facts.

To date, attempts by debtors to meet the “undue hardship” test have largely been ineffective and expensive.<sup>2</sup> As a result, many realistically but also mistakenly assume that student loans simply are not dischargeable in bankruptcy.

The Guidance seeks to change that by providing the objective standards through which the DOE and DOJ will review a debtor’s case—safe harbors of sorts. If the debtor can demonstrate the existence of these facts and circumstances, then the DOJ and DOE will stipulate that the student loans should be discharged. And, while an adversary proceeding will still be a necessary protocol to initiate the review, the clarity provided by the Guidance will allow debtors to more effectively evaluate their likelihood of success before even engaging in the process. Moreover, the DOE will provide its recommendation to the debtor’s counsel and then the DOJ’s decision to stipulate (when appropriate) will allow for abbreviated and less costly proceedings instead of full-blown litigation.

Another important benefit of the Guidance is that DOJ is providing transparency as to how its attorneys will evaluate critical



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To provide more information about how consumer bankruptcy attorneys can implement the new DOJ/EOD guidance to benefit both their clients and their own practices, NACBA offers an in-depth webinar, *New DOJ/ED Guidance on Undue Hardship Discharge of Student Loans in Bankruptcy* and will have a full day course with up-to-the-minute information at its Spring Conference in Washington, D.C. on April 27, 2023.

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financial information. For example, DOJ has advised that it will allow debtors to take the full amount of any expense covered by IRS National Standards, while it will look to

actual borrower expenditures for expenses covered by IRS Local Standards.<sup>3</sup> Perhaps most importantly, the DOJ has made clear that its attorneys, when determining student loan affordability, should look to the benchmark affordability of student loan payments under the Standard Repayment plan formula (normally the most expensive and least affordable plan). This is a major shift since previously, great emphasis was placed on affordability of Income-Driven Repayment plans which are normally the least expensive.

The Guidance is still new and untested so navigating student loan discharges may not be smooth sailing yet, but it appears to have provided a beacon of light on the horizon. ■

**FOOTNOTES**

1. Hanson, Melanie, "Student Loan Debt Statistics" [EducationData.org](https://educationdata.org), July 29, 2022. <https://educationdata.org/student-loan-debt-statistics>
2. Iullano, Jason, An Empirical Assessment of Student Loan Discharges and the Undue Hardship Standard (July 24, 2011), 86 American Bankruptcy Law Journal 495 (2012). Available at SSRN: <https://ssrn.com/abstract=1894445> or <http://dx.doi.org/10.2139/ssrn.1894445>
3. DOJ has also made clear that it will allow debtors to explain the need for any expenses that exceed any of the IRS Standards and its attorneys are to consider such explanations and determine if they are reasonable and warranted.



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