Cullen | Dykman

Student Debt Discharge in Bankruptcy: Movement Toward A Kinder and Gentler Approach

November 21, 2022

Kevin P. McDonough
Garden City – 516.357.3787

Michael H. Traison
Chicago/NYC – 312.860.4230

Dina L. Vespia
Garden City – 516.357.3726

Michael Kwiatkowski
Garden City – 516.296.9144

On November 17, 2022, the U.S. Department of Justice (DOJ), in coordination with the U.S. Department of Education (DOE), announced the adoption of a new policy and process for handling debtors in bankruptcy seeking to discharge federal student loan debt. *See* Justice Department and Department of Education Announce a Fairer and More Accessible Bankruptcy Discharge Process for Student Loan Borrowers | OPA | Department of Justice.

The announcement emphasizes a joint commitment by DOJ and DOE to creating "clearer, fairer, and more practical standards" for assessing discharge requests by student loan borrowers in bankruptcy. We discussed how the bankruptcy process works with respect to discharge of student debt in several of our prior alerts. *See* An Update on Student Loan Debt: Interpretation of the Statute is Critical; Another Bankruptcy Court Rules in Favor of Discharging Student Loan Debt; Student Loan Debt Discharged in Recent Bankruptcy Court Opinion; Student Loan Debt Discharged in Recent Illinois Bankruptcy Court Opinion; Student Loan Mediation Before Litigation Program Adopted by the United States Bankruptcy Court for the Southern District of New York.

The issuance of the new advisory on the process of responding to debtors seeking discharge of student loan debt comes amidst the Administration's attempts to use Executive Orders to forgive student loan debt which have encountered resistance from several federal courts confronting the issue. The new policy appears to recognize the inconsistency in handling the discharge issue among the courts as well as the harshness of the application of the "undue hardship" standard as it has developed under the current caselaw, including under its most common

test based on *Brunner v. New York State Higher Education Services Corp.*, 831 F.2d 395 (2d Cir. 1987).

The process of seeking discharge of student loan debt requires commencement of an adversary proceeding which is litigation which can become time intensive, emotionally stressful and economically disastrous. This new policy seeks to avoid unnecessary litigiousness and provides a process for DOJ attorneys to handle, at the outset, adversary proceedings where the debtor seeks to discharge federal student loan debt. The new policy is directed not at the Office of the United States Trustee (who rarely, if ever, appears in such matters), but at the DOE and the DOJ attorneys representing the DOE.

The new policy encourages DOJ attorneys to contact the debtor or debtor's counsel as soon as practicable after commencement of the adversary proceeding and provide them an opportunity to submit an "attestation form" which requests information about the debtor's income and expenses. The attestation form, together with information from the DOE, will assist the DOJ attorney in evaluating the relevant factors to determine whether to recommend that the student loan be discharged. The three relevant factors are (i) debtor's present ability to repay the loan; (ii) whether the debtor's inability to pay the loan is likely to persist in the future; and (iii) whether the debtor has acted in good faith in the past in attempting to repay the loan.

Upon an analysis of these factors based on information from the debtor and the DOE, the DOJ attorney will recommend to the bankruptcy court whether the debtor's federal student loan should be discharged. Ultimately, of course, the bankruptcy judge will make the final determination on whether to grant discharge. Since bankruptcy judges will still have to consider the fairly harsh *Brunner* standard in deciding whether discharge is appropriate, one questions whether DOJ's recommendation under this new policy will have significant impact beyond close cases. On the other hand, the new DOJ policy seems to provide bankruptcy judges the opportunity to be more lenient when considering whether discharge should be granted. Moreover, if bankruptcy judges take that opportunity, even if doing so may be in contravention of the existing caselaw, parties to the adversary proceeding may be unlikely to appeal those decisions. As such, the executive branch is opening up the door to a more equitable approach in the absence of revisions to the Bankruptcy Code and adverse court decisions.

Please note this is a general overview of developments in the law and does not constitute legal advice. Nothing herein creates an attorney-client relationship between the sender and recipient. If you have questions regarding this alert, please contact Kevin P. McDonough (kmcdonough@cullenllp.com) at 516.357.3787 or Michael H. Traison (mtraison@cullenllp.com) at 312.860.4240 or Dina L. Vespia (dvespia@cullenllp.com) at 516.357.3726 or Michael Kwiatkowski (mkwiatkowski@cullenllp.com) at 516.296.9144.

About Cullen and Dykman's Higher Education and Bankruptcy and Creditors' Rights Practice Areas

Our firm's Higher Education practice group is a multidisciplinary team committed to helping colleges and universities navigate the ever-changing higher education landscape. Our focus is on providing practical solutions to complex legal problems and avoiding unnecessary expenses. With our Bankruptcy and Creditors' Rights practice, we are able to offer clients a unique perspective on the issues involved in complex bankruptcy proceedings in a wide range of industries.

Practices

- Higher Education
- Bankruptcy and Creditors' Rights

Attorneys

- Kevin P. McDonough
- Michael H. Traison
- Dina L. Vespia
- Michael Kwiatkowski