BANKRUPTCY, MORALITY & STUDENT LOANS: A DECADE OF ERROR IN UNDUE HARDSHIP ANALYSIS

Linn White
Thomas Jefferson School of Law

Follow this and additional works at: https://digitalcommons.onu.edu/onu_law_review

Part of the Bankruptcy Law Commons

Recommended Citation
Available at: https://digitalcommons.onu.edu/onu_law_review/vol43/iss1/4

This Article is brought to you for free and open access by DigitalCommons@ONU. It has been accepted for inclusion in Ohio Northern University Law Review by an authorized editor of DigitalCommons@ONU. For more information, please contact digitalcommons@onu.edu.
Bankruptcy, Morality & Student Loans: A Decade of Error in Undue Hardship Analysis

LINN WHITE*

In an effort to stem perceived abuses of the bankruptcy system, Congress adopted a rule in 1976 that created a time-based conditional limitation on the discharge of federally guaranteed student loans in bankruptcy. The only means of overcoming the limitation was the showing of an “undue hardship,” which was undefined by the legislature. This gave rise to two judicially created, means-based tests that were used to determine if the debtor was attempting to abuse the bankruptcy system. By the time the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) was enacted, the time-based restriction was gone, leaving only the undue hardship exception to student debtors seeking relief against an expanded pool of protected creditors. Meanwhile, the judiciary has largely continued to apply the same two means-based tests from 1978.

However, using a detailed analysis of statutory history, statutory construction, and case law, this paper reveals deep flaws in the fundamental reasoning that underpins the current judicial rationale. Through an uncritical acceptance of specious moral arguments, coupled with the concomitant failure to objectively assess the history and plain language of BAPCPA, both the judiciary and some of the staunchest critics of the conditional discharge have failed to recognize the erroneous application of the bankruptcy regulations as envisioned by BAPCPA. However, the research also demonstrates that, with modest changes, the courts could provide a more humane, ethical, and equitable treatment of student loan debtors that not only comports with current law, but is actually mandated by it.

I. Introduction ............................................................................................ 152
II. A Brief History of Bankruptcy ............................................................. 154
    A. Bankruptcy in the Early United States........................................... 162
    B. Bankruptcy in the Modern Era....................................................... 165
III. Morality and Bankruptcy .................................................................... 169
IV. Undue Hardship .................................................................................. 182

* Linn White is an adjunct professor for the graduate program at Thomas Jefferson School of Law. The author would like to thank Mark Sage for his guidance in the writing of this article. The author would also like to thank Dr. Bridget Lynch for her kindness and support.
I. INTRODUCTION

More than 500 years before the United States came into existence, English law was already struggling with the issue of how best to deal with defaulting debtors. The early rules and regulations were largely in response to the fraudulent practices of the nascent merchant class, and as such, tended to treat the matter as a criminal offense. Accordingly, during the first few centuries of bankruptcy regulation, defaulting debtors were often subject to imprisonment, pillory, maiming, and even death. However, during the Industrial Revolution, the criminal sanctions slowly gave way to more equitable approaches. Essentially, after creditors lost the ability to imprison debtors, what followed is the struggle between the rights of creditors and debtors that persists to this day. Nonetheless, bankruptcy protection expanded during the 20th century and gradually afforded more access to greater numbers of people.

It is arguably fair to say that since the High Middle Ages, creditors have waged an unbroken fight against any softening of bankruptcy regulations and seemed to have the upper hand much of that time, although they definitely lost ground in the last century. However, that lost ground was somewhat recovered with the passage of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA). However, in a sense, the passage of BAPCPA acted more like a cap on a steady erosion of debtor rights, rather than a sudden reversal of policy for the creditors. The slow erosion of debtor rights is perhaps no more evident than it is in the realm of student loans and the debtors who carry them.

The dischargeability of student debt was already facing assault in the legislature, even before Congress liberalized the bankruptcy law with the

1. See 11 Edw. (1283), reprinted in 1 STATUTES OF THE REALM 53, 53-54 (1235-1377) [hereinafter 11 Edw.].
4. See id. at 11-12.
5. See id.
6. See id. at 26-27.
7. See id. at 7.
Bankruptcy Code of 1978. As such, by the time Congress enacted the 1978 Code, student loans in bankruptcy had already succumbed to the attack. Absent the showing of an “undue hardship,” a time-based restriction of five years conditioned the discharge of student loans. Through the years, the time-based restriction was slowly eliminated, while the pool of protected creditors was expanded. However, Congress declined to define the term “undue hardship,” instead leaving the matter up to the judiciary. The judicially constructed tests from that period largely survive untouched to this day, nearly forty years later.

This paper will first briefly explore the history of bankruptcy law, starting with the Statute of Merchants in 1283, through the most recent changes in BAPCPA. From there, the research will show that not only did the proponents of tighter restrictions on student loan discharges rely on demonstrably false assertions, but that the manner in which they used them has clouded rational discourse on the matter ever since. With that foundation established, it will be shown that the judiciary is utilizing a statutory construction that is more applicable to the old Bankruptcy Code, rather than the current law. Further, the research will demonstrate that the usage of the two predominant, judicially constructed tests for undue hardship violates both the mandate and the plain language of BAPCPA. Then, a statutory construction and undue hardship analysis that properly accords with both the current state of the law and the legislature’s intentions will be presented. Finally, it will be shown that it is the uncritical acceptance of specious moral arguments by both the courts and the critics of the conditional discharge of student loans that has led to over a decade of judicial error.

12. See id. at §§ 439(A)-440, 90 Stat. at 2141.
15. See id.
17. See infra Part II; see also infra Part II.B.
18. See infra Part III.
19. See infra Part IV.
20. See infra Part IV.
21. See infra Part IV.A.
22. See infra Part V.
II. A BRIEF HISTORY OF BANKRUPTCY

Modern bankruptcy laws in the United States could fairly, if loosely, be said to trace their origins to a series of English statutes from the latter part of the High Middle Ages. The first of these was the Statute of Merchants, which was enacted in 1283. Though not specifically naming bankruptcy, the statute codified the means by which a merchant could affect a recognizance of a debt owed. Thus, if a creditor “lent their [g]oods to divers [sic] persons, be greatly impoverished” by lack of payment, this new scheme provided a legal framework to seize the defaulting debtor’s assets. The act as fashioned was followed shortly thereafter by a second iteration of the Statute of Merchants in 1285. The former statute had provisioned for creditors to compel a sheriff to seize a delinquent debtor’s assets, and if no assets were found, they could then subsequently seize and imprison the debtor.

Apparently, many of the local sheriffs were either reluctant to, or otherwise avoided enforcement of, the provisions of the 1283 Act, which gave rise to an expanded authority within the later statute. Among other things, that expanded authority allowed the creditor to seize the debtor as the first remedy for default. Even though the text of the aforementioned acts specifically referred to merchants, it seems that many “non-merchants” also availed themselves of the remedies afforded by the legislation. Evidently, this occurred with such frequency that the practice warranted passage of Chapter XXXIII of “The New Ordinances,” which specifically limited actions under the Statute of Merchants to those “between [m]erchants and [m]erchants, and of [m]erchandises [sic] made between them . . . .” Noting that many non-merchants “do feel much aggrieved and fined by the Statute of Merchants made at Acton Burnell,” the legislators sought to try and prevent abuse of the system.

24. See 11 Edw., supra note 1, at 53-54 (this statute was also known as the Statute of Acton-Burnell, and the title and commencement are noted as such in French in an unnumbered note at the bottom of the page).
25. See id. (alteration in original).
26. See id. (alteration in original).
27. See 13 Edw. (1285), reprinted in 1 STATUTES OF THE REALM 98 (1235-1377) [hereinafter 13 Edw.].
28. See 11 Edw., supra note 1, at 53-54.
29. See 13 Edw., supra note 27, at 98-100.
30. See id.
31. See id.
32. 5 Edw. 2 c. 33 (1311), reprinted in 1 THE STATUTES OF THE REALM 165 (1235-1377) [hereinafter 5 Edw. 2] (alteration in original).
33. See id.
To that end, the ordinance first required that “four good and lawful men” testify that the recognizance was for a mercantile debt. Second, the ordinance limited where and to whom those recognizances could be delivered and registered. While the grievances that non-merchants complained of are not detailed, it is clear that rules distinguishing commercial debtors were already being implemented. It appears that the specific designation of a “bankrupt” does not make the official record until the reign of King Henry VIII; however, author Louis Levinthal noted in 1919 that “although no laws were made against bankrupts specifically by that name prior to that time . . . laws were made against those persons who today are called bankrupts.” As such, Mr. Levinthal detailed the passage of several acts after the Statue of Merchants that are essentially the forerunners to modern laws regarding fraudulent transfers.

Levinthal went on to point out that those early statutes were limited to transfers for the debtor’s benefit and failed to account for transfers in preference of one creditor over another. It is here that the Statute of Bankrupts of 1542 attempted to fill that gap, by introducing the concept of state enforcement of both: (1) the seizure of debtors; and (2) a ratable distribution of the debtor’s assets among their various creditors. This was largely deemed preferable, because once a default seemed imminent under the previous rules, creditors had to go to the authorities in order to establish priority for their claims. Given the nature of communications at the time, these rules would have clearly left distant creditors at a disadvantage. As an aside, one might note that the rationale is quite analogous to our modern

34. See id.
35. See id.
36. See id. at 165-67.
37. Levinthal, supra note 2, at 11.
38. See id. at 11-14 (noting 50 Edw. 3 c. 6 (1326), reprinted in 1 THE STATUTES OF THE REALM 251 (1235-1377) barred collusive land and chattel transfers to friends, whereby the debtor could avoid the creditor by taking “asylum” and then living off the rents; 13 Eliz. c. 7 (1571), reprinted in 4 THE STATUTES OF THE REALM 537 (1547-1624) [hereinafter 13 Eliz.] mandated that “[f]lying to a franchise, or taking sanctuary” was an act of bankruptcy; 21 Jac. c. 15 (1623), reprinted in 4 THE STATUTES OF THE REALM 1228 (1547-1624) [hereinafter 21 Jac.] (alteration in original) barred transfers of property to non-creditors, even if accompanied by valuable consideration; 2 Rich. 2 c. 3 (1377), reprinted in THE STATUTES OF THE REALM 1 (1377-1504) instituted a remedy, where after a debtor had secreted themselves away in a “privileged place” (i.e., asylum) for a term of five weeks or more, the creditor was allowed to give notice at the gate of the privileged place via the Sheriff. If the debtor still refused to come out, the creditor could then seize the debtor’s assets.).
39. See id. at 14.
40. See 34 & 35 Hen. 8 c. 4 (1542), reprinted in 4 THE STATUTES OF THE REALM 893, 899-901 (1509-1545) [hereinafter 34 & 35 Hen. 8] (“The machinery for enforcing individual debts was available in the King’s Courts from the thirteenth century onwards. It is unlikely that any customary process would have sufficed to restrain the individual creditor from stealing a march upon his fellows.”).
41. See id. at 13.
bankruptcy statutes regarding so-called preference transfers within the United States.43 The Supreme Court of the United States summarized the modern scheme in *Union Bank v. Wolas*44, writing:

Any creditor that received a greater payment than others of his class is required to disgorge so that all may share equally. The operation of the preference section to deter ‘the race of diligence’ of creditors to dismember the debtor before bankruptcy furthers the second goal of the preference section—that of equality of distribution.45

Returning to the matter at hand, as one can see, the Statute of Bankrupts was more akin to a criminal sanction, and as such, the Act was decidedly both pro-creditor and anti-fraud in nature, as might be gleaned from the opening paragraph.46 While the depth of the fraud complained of could reasonably be ascertained by a cursory reading of the Act, the discerning reader might notice that any underlying circumstances that could innocently lead one to default are markedly absent.47 Rather, in place of any attempt to determine causation, a presumption of abuse is clearly evident.48 Even still, less than thirty years later, “[t]he Act of 13 Elizabeth, c.7 complains that despite the Act of 34 and 35 Henry VIII, c. 4, fraudulent bankrupts had much increased . . . .”49

Along with the Fraudulent Conveyances Act of 1571, 13 Elizabeth further codified the means of dealing with a defaulting debtor’s assets.50

---

46. 34 & 35 Hen. 8, *supra* note 40, at 899-901. The original text reads:

Where divers and soondrye persones craftelye obtenying into theyre handes greate substaunce of other mennes goods doo sodenlie flee to partes unknowne or kepe theyre houses, not mynding to paye or restor to any theyre debts or duties, but at theyre owne willes and pleasures consume the substaunce obtyened by credyte of other men, for theyre owne pleasures and delicate lyving, againste all reasone quytie and good conscience [sic] . . . .

*Id.* When the text is modernized for clarity, it reads:

Where diverse and sundry persons craftily obtaining into their hands great substance of other men’s goods do suddenly flee to parts unknown or keep their houses, not minding to pay or restore to any their debts or duties, but at their own pleasures consume the substance obtained by credit of other men, for their own pleasures and delicate living, against all reason, equity, and good conscience . . . .

*See id.*

47. *See id.* at 899.
50. See 13 Eliz., *supra* note 38, at 537-38.
Interestingly, the underlying logic of these rules is still visible in the right of the modern bankruptcy trustee or debtor in possession to avoid many pre-petition transfers. The years following 13 Elizabeth and leading up to the American Revolution saw some softening of the bankruptcy statutes in England. Of this, Levinthal noted that the Acts of Anne in 1705 and 1711 "permit[ted] an allowance for maintenance to be made to a bankrupt who surrenders, and, even more important, grant him a 'discharge' from all debts owing at the commencement of his bankruptcy." Of this, Levinthal noted that the Acts of Anne in 1705 and 1711 “permit[ted] an allowance for maintenance to be made to a bankrupt who surrenders, and, even more important, grant him a 'discharge' from all debts owing at the commencement of his bankruptcy.”

Germane to the broader discussion at hand, regarding the Acts of Anne, Levinthal said:

This provision was probably the consequence not only of pity, but also of the feeling that mercantile credit is given in the interest of the creditor as well as of the debtor; that the giving of credit necessarily involves some risk; that it should be the business of the trader to insure against this loss by adding on a percentage for the credit which he advances; and that all the debtor ought to pledge is his estate, not his future earnings, and certainly not his personal liberty.

With that, one can see the gradual acceptance of both the idea of merchant debt as a necessity, as well as the notion that a merchant creditor must also bear some responsibility for mitigating the effects of commercial losses. Of course, the legislation discussed thus far has dealt almost solely with debts incurred between merchants and traders. While the treatment of those defaulting debtors could scarcely be called gentle, one must recall that the genesis of those laws was to encourage trade. Tracing back to the Statute of Merchants in 1283, apparently after having “lent goods to divers persons” at a loss and without recourse, it seems that, quite predictably, many foreign traders simply stopped coming to England. While the

52. See Levinthal, supra note 2, at 17-18 (citing 21 Jac., supra note 38, at 1228) (though it should be said that prior to that “softening,” on the previous page, Levinthal made note of a particularly stiff punishment, which stated that, “pillory and loss of an ear should be the penalty imposed upon debtor who failed to show that bankruptcy was due solely to misfortune.”).
53. Id. at 18.
54. See id. at 19 n.67 (noting that subsequent legislation “seems to hint” that it was enacted to combat abusive practices by debtors under the Statutes of Anne). But see Tabb, supra note 3, at 18-19.
55. See id. at 19.
56. See 11 Edw., supra note 1, at 53-54; 13 Edw., supra note 27, at 98; 34 & 35 Hen. 8, supra note 40, at 899.
57. See 34 & 35 Hen. 8, supra note 40, at 899-901.
58. See 11 Edw., supra note 1, at 53-54 (noting that because of the lack of “speedy” remedies at law against fraudulent debtors, “and by reason hereof many Merchants [sic] [have withdrawn to come] into this Realm [sic] with their Merchandises [sic], [sic] to the Damage [sic] as well of the Merchants [sic] as of the whole Realm . . . .”).
encouragement of trade might not necessarily justify some of the treatments that were meted out, it does at least provide a frame of reference for a clearer understanding of the underlying rationale that drove the formation of these laws.\textsuperscript{59}

However, the disdain for the non-merchant debtor is not as readily apparent.\textsuperscript{60} Of traders, Sir William Blackstone noted rather oddly in 1765 that England gives “the benefit of the laws of bankruptcy to none but actual traders; since that set of men are, generally speaking, the only persons liable to accidental losses, and to an inability of paying their debts, without any fault of their own.”\textsuperscript{61} This statement is odd, because the assertion clearly defies both common experience and logic. Nevertheless, Blackstone subsequently goes to some length to distinguish the criteria for what constitutes an “actual” trader, noting that the law has expanded the definition through the years to include bankers and the like, as well as stockbrokers and others.\textsuperscript{62} However, the tradesman’s designation was withheld from those who engaged in “handicraft” occupations, as well as from innkeepers and even farmers—even though they all ostensibly engaged in trade.\textsuperscript{63} Perhaps more tellingly, Blackstone says of the non-mercantile class that “subjecting them to the laws of bankruptcy might be a means of defeating their landlords of the security which the law has given them above all others, for the payment of their reserved rents . . . .”\textsuperscript{64}

With that said, one can see early on that defaulting merchant debtors were largely looked upon with distaste.\textsuperscript{65} That distaste did not necessarily

\textsuperscript{59} See Levinthal, supra note 2, at 18-19.
\textsuperscript{61} Id. at 473.
\textsuperscript{62} Id. at 475.
\textsuperscript{63} Blackstone says:

But by the same act, no farmer, grazier, or drover, shall (as such) be liable to be deemed a bankrupt: for, though they buy and sell corn, and hay, and beasts, in the course of husbandry, yet trade is not their principal, but only a collateral, object; their chief concern being to manure and till the ground, and make the best advantage of it’s (sic) produce.

\textsuperscript{64} Id. One can see that Blackstone’s analysis is clearly deficient, unless of course the farmers in question were solely raising crops for their own sustenance. Id. However, a freeholding subsistence farmer would not comport with Blackstone’s concern about non-merchants being able to defeat a landlord’s rent receipts via bankruptcy. Id. Further, it is both an observable reality and common sense that a farmer’s “chief concern” in raising crops does not necessarily impute a lack of means or desire to trade the result of that effort for profit or gain. Id. Put another way, it would be just as absurd to posit that Ford’s “chief concern” is to build cars and that selling those cars is but a collateral reason for building them. See id. As such, it would seem that the assertion above is more likely an attempt to buttress class distinctions than a conscientious effort to craft a legal doctrine. See id.

\textsuperscript{65} Id.
arise solely from notions of the inherent immorality of debt.66 Rather, it would seem that the law was more concerned with curtailing the perceived fraudulent practices of the native merchant class in England in order to encourage foreign trade and investment.67 However, as trade grew in volume and importance (perhaps as a consequence of the statutes), one can see what appears to be a corresponding shift in the legislation’s tone.68 Blackstone noted that “in this extrajudicial method of proceeding, which is allowed merely for the benefit of commerce, the law is extremely watchful to detect a man, whose circumstances are declining.”69 He then went on to list several statutorily enumerated acts that constitute an act of bankruptcy.70 However, Blackstone then pointed out that if the bankrupt could prove that their loss was due to innocent misfortune—and could gain creditor approval—they would be entitled to a certificate that gave them a sort of general indemnity.71

With that certificate in hand, the debtor merchant was also “entitled to a decent and reasonable allowance out of his effects, for his future support and maintenance, and to put him in a way of honest industry.”72 Further, the debtor was given a discharge of all debts, and “[t]hus the bankrupt becomes a clear man again; and, by the assistance of his allowance and his own industry, may become a useful member of the [C]ommonwealth.”73 Obviously, with the deck somewhat stacked in the creditor’s favor, approval was not always forthcoming.74 Likely in recognition of this fact, subsequent statutes removed the need for creditor approval, making the discharge a judicial act.75 However, because the bankruptcy statutes did not apply to non-merchants, those debtors were barred from receiving the benefit of the certificate and the corresponding “fresh start.”76 This was attributed to the notion that:

If persons in other situations of life run in debt without the power of payment, they must take the consequences of their own indiscretion, even though they meet with sudden accidents that may reduce their fortunes: for the law holds it to be an unjustifiable practice, for any

66. See id. at 474, 478-79.
67. Id. at 474.
68. Id. at 477.
69. Id.
70. BLACKSTONE, supra note 60, at 477-79 (noting eleven different means by which a debtor might seek to fraudulently hide assets or otherwise deprive creditors).
71. Id. at 483.
72. Id.
73. Id. at 484 (alteration in original).
74. See id.
75. See Levinthal, supra note 2, at 19-20.
76. BLACKSTONE, supra note 60, at 473.
person but a trader to encumber himself with debts of any considerable value. 77

Blackstone failed to address why the practice is unjustifiable for one party and not the other, though one might presume from the certitude by which it is expressed that such views were likely common at the time. 78 Commentaries does briefly touch on insolvency, “which is an occasional act, frequently passed by the legislature; whereby all persons whatsoever, who are either in too low a way of dealing to become bankrupts, or not being in a mercantile state of life . . . are discharged from all suits and imprisonment.” 79 Note that, even though freed from prison, there is no mention of debt relief for the insolvent debtor. 80 The debtor’s release from prison by insolvency was only good “upon delivering up all their estate and effects to their creditors upon oath,” with the further admonishment that any fraud or perjury would be punished by death. 81 Unfortunately for the debtor, many times their property was only sufficient to affect their release, leaving the debt intact, whereby “creditors could still use collection devices other than imprisonment” to come after the debtor. 82

The divide between merchant and non-merchant debtors continued well into the 19th century in both England and the United States. 83 In England, economic historian Paul Johnson notes that “[w]hat really distinguished the defendants in bankruptcy and small debt proceedings was their social status, and this mattered because of assumptions made by judges about the economic motivations of people of different social class.” 84 Mr. Johnson goes on to outline some opinions put forth by judges at the time that seem to reveal a strong, anti-working class bias. 85 The gist of the assertions

77. Id.
78. Id. at 473-74.
79. Id. at 484 (citing 32 Geo. 2 c. 28; 1 Geo. 3 c. 17; 5 Geo. 3 c. 41; 9 Geo. 3 c. 26).
80. Id. at 484-85.
81. BLACKSTONE, supra note 60, at 484.
82. WARREN & WESTBROOK, supra note 51, at 101.
83. Id.
85. See id. at 501-02. One of the more pernicious examples is taken from a letter written by Judge Johnes of the Caernarvon County Court in 1854 that reads:

Take a common case—a young man, without family, earning high wages as a miner or mechanic, contracts a debt of a few pounds with a small tradesman, who sues him and obtains judgement. To take out execution against the goods is futile because, though in one sense wealthy, the defendant probably has none worth levying on. His high wages are possibly squandered in taverns or secreted in such a way that they cannot be reached by the creditor . . . . The defendants who thus evade and defy their creditors, are commonly men who are, in a pecuniary sense, much better off than the great majority of the professional men of this
revolved around the idea that working class debtors intentionally squandered their wages in lieu of repayment of their debts. Further, it appears that they were often discriminated against simply by the types of goods they bought. Of the latter, Johnson remarks that “[i]t was also asserted that many of the initial purchases, particularly from itinerant traders or tallymen, were unnecessary fripperies, so the debtor was doubly unworthy.”

The negative estimation of working class debtors is noted as that of the majority, but apparently, that view was not universally held. A prominent Victorian era legal publication is quoted as being “adamant that fraudulent debtors constituted ‘an insignificant minority’ of cases” that were heard at the time. It was further asserted that “[t]he majority of debtors were ‘poor persons to whom credit is often recklessly given, who benefit little by it, to whom debt is a calamity, whose ‘means’ are so shadowy that evidence of them is most difficult to present in any satisfactory shape to a judicial tribunal.” It bears mentioning that all of these notions are strikingly similar to many popular sentiments one might hear today, nearly 200 years later. If nothing else, the disparity of views expressed highlights the enduring nature of the conflict.

country—the wages they receive being commonly higher than the average remuneration of professional men, especially when we take into account the less refined mode in which they live . . . On the other hand, the creditors, whose confidence they abuse, generally belong to the poorest and most necessitous class of small retail dealers, a class who have no superfluous funds to spend in dubious litigation with knaves, and to whom legal redress, unless it be really cheap and accessible, is a mockery.

Id. Johnson correctly sums this by noting, “Here we see, combined in one short comment, moral judgments about the fecklessness of manual workers and the integrity of small traders, together with a gross misrepresentation of the economic circumstances of working-class life.” Id.

86. See id.
87. See id. at 502.
88. Id.
89. See Johnson, supra note 84, at 502.
90. Id.
91. Id. at 502-03.
92. Cf. Bankruptcy Reform: Hearing Before the Subcomm. on the Judiciary, 109th Cong. 248 (2005) (statement of Todd Zywicki, Visiting Professor of Law, Georgetown University Law Center) [hereinafter Bankruptcy Reform Hearing] (“Smaller businesses and small creditors suffer the most from a runaway bankruptcy system, as they tend to have the narrowest margins and the least ability to spread those losses among their customers.”); UNITED STATES PUBLIC INTEREST RESEARCH GROUP, THE CREDIT CARD TRAP: HOW TO SPOT IT, HOW TO AVOID IT 1 (2001), http://www.uspirg.org/sites/pirg/files/reports/Credit_Card_Trap_2001_USPIRG.pdf [hereinafter U.S. PIRG] (The report makes note of “aggressive marketing and misleading tactics,” “outrageous interest rates,” and “bigger profits than ever.” It also notes that industry proposed legislation to curtail bankruptcies will “encourage credit card companies to be more predatory in lending, because the risk of issuing cards to higher-risk consumers such as students and those with low incomes will decline.”). 93. Cf. Bankruptcy Reform Hearing, supra note 92, at 248 (statement of Todd Zywicki, Visiting Professor of Law, Georgetown University Law Center); U.S. PIRG, supra note 92, at 1.
A. Bankruptcy in the Early United States

While much of the underlying rationale for bankruptcy administration carried over from English jurisprudence, the post-Revolutionary War political and economic environment of the United States created a very different backdrop for the application of that rationale. First, large-scale debt financing of the war had caused widespread distortions in the nascent U.S. economy. As noted in a 2009 book by Bruce H. Mann, “[t]he Revolution, like all wars, was fought on credit in the form of direct loans and, more important, of paper currency and scrip issued by the Continental Congress and state governments.” This, coupled with wartime demand for goods, created a vicious circle of inflation, with a concomitant need for the continual debasement of the various paper currencies in circulation at the time. Mann also notes the sharp increase in both debt and business speculation after the war as another factor that drove shifting perceptions of bankruptcy in the United States.

Of the time, he says, “[t]he brief postwar boom...triggered a rush of merchants and traders to ports like Philadelphia, all eager to profit in the commercial frenzy, and all capitalized—and often undercapitalized—on credit.” After the post-war economy contracted, the rate of business failures increased commensurately, which “made failure the potential common fate of all merchants.” However, similar to Blackstone’s assertions, there was a perceptual divide between those who speculated in agriculture and those who speculated in other areas, such as bank stock or securities. While “[f]armers and planters borrowed for current needs or wants with the expectation of repaying after the harvest,” the ability to repay the debt accumulated by merchants and financial speculators seems to have rested largely upon the simple hope that their investments would pan out. As more of the latter sought capital, they “drove up the interest rates they had to offer to investors, which in turn attracted investments from ever-widening circles, both demographically and geographically.”

The net effect of this was to exacerbate the magnitude of the losses when the schemes failed, and with the expanded reach of those failures,

---

95. See id. at 170.
96. Id. at 169.
97. See id. at 169-70.
98. See id. at 175.
99. Mann, supra note 94, at 177.
100. Id.
101. See id. at 190.
102. See id.
103. Id. at 191.
more and more people found themselves imprisoned for debt. As such, it is not surprising to find a corresponding increase in the number of people wishing to adopt more forgiving methods of dealing with defaulted debts. While there had been several attempts at the state level, the United States’ first national bankruptcy law came into effect in 1800, of which the Supreme Court made brief mention in *Wood v. Owings*, stating that:

> On the 4th of April, 1800, [C]ongress passed an act to establish an uniform system of bankruptcy throughout the United States, which declares, among other things, that any merchant. . .with intent unlawfully to [sic] delay or defraud his creditors, make or cause to be made any fraudulent conveyance of his lands or chattels, shall be deemed and adjudged a bankrupt.

Beyond *Wood*, there is scant case law on the scheme, which is not surprising considering that the law was repealed three years after its passage. As one can see from the text above, the gist of the law was essentially the same as its English contemporary. In the wake of the failed 1800 bankruptcy act, state law again attempted to fill the gap, though as author Charles Jordan Tabb points out, due to the unique characteristics of the federal system, individual states had limited authority to discharge debts—especially those that originated beyond their respective borders. Tabb further notes the gradual decline and eventual abolishment of imprisonment for debt in the years after the 1800 act was repealed. However, debtors still “lacked any means to discharge preexisting debts during the first four decades of the nineteenth century,” which also gave rise to various stopgap measures at the state level.

After a financial crisis struck the United States economy, a new bankruptcy scheme was enacted in 1841. It is here that bankruptcy relief became available to all debtors in the United States, regardless of merchant status. Tabb says the Act “was a coordinated, simple, and short act of only seventeen sections” that was apparently a boon to struggling debtors, but “from the viewpoint of creditors, the 1841 Act, like its 1800
predecessor, was a dismal failure.” 114 This Act was also repealed very shortly after its passage and was not replaced until 1867 after yet another financial calamity, this one largely attributable to the American Civil War. 115 The procedures envisioned by the 1867 Act proved unappealing to both debtors and creditors for various reasons—so much so that it was repealed in 1878. 116 However, that Act provided the framework for the debtor to choose either state or federal non-bankruptcy property exemptions. 117 Debtor choice of exemptions was a novel concept at the time, and once the idea passed constitutional muster, the essence became part of the fabric of bankruptcy regulation that persists to this day. 118

After another twenty years and much compromise, Congress passed the Bankruptcy Act of 1898. 119 In its infancy, this legislation also looked as if it might be short lived, but with a series of compromises between debtors and creditors in 1903, “the first enduring American bankruptcy law took shape.” 120 However, the Act was not without its detractors, and with a strong push “similar to those launched by the credit industry in the 1960s, 1980s, and 1990s,” creditors sought to place payment conditions on “those debtors with some ability to pay as a condition” of discharge. 121 While those changes did not occur, the 1898 Act was amended extensively by the 1938 Chandler Act, which was passed in the aftermath of the Great Depression. 122 The bulk of the amendments revolved around issues that pertained to merchant debtors, yet the changes did introduce a new debt reorganization scheme for “wage earners” and other non-merchants under Chapter XIII. 123

Regarding the impetus for Chapter XIII, the author of the Chandler Act said, “[a] number of states had debt composition statutes, and section 74 of the Bankruptcy Act was already in existence. But those various enactments failed to prevent repeated garnishment proceedings at heavy costs, sheriffs’ fees, and unconscionable judgments against those unable to be represented by counsel.” 124 This was a significant addition, because with this, “Chapter

115. See id. at 18-19.
117. See Tabb, supra note 3, at 20.
118. See id. at 16.
119. See WARREN & WESTBROOK, supra note 51, at 102.
120. Id. at 103.
121. Tabb, supra note 3, at 27.
122. See WARREN & WESTBROOK, supra note 51, at 103.
123. See id. at 104.
124. Walter Chandler, The Wage Earners’ Plan: Its Purpose, 15 VAND. L. REV. 169, 169 (1962). It should be noted that debt compositions are arrangements for valuable consideration among debtors and creditors, as well as between the creditors themselves. The scheme provides a reduced payment for the debtor with the creditors taking a pro-rata share. See generally Comment, A Survey of Sections 74
XIII effectively introduced into consumer bankruptcy the debt compositions and extensions of state law, coupled with the unique powers of bankruptcy law, such as the discharge of remaining debt once the debtor completed the repayment plan.  

B. Bankruptcy in the Modern Era

A major overhaul of the bankruptcy system occurred again in 1978, when Congress adopted a bankruptcy bill that was birthed via a ponderous process that spanned the better part of a decade. While not critical to the present discussion, two provisions—Chapter 7 and Chapter 13—shall be outlined briefly, as both touch on consumer bankruptcies. Warren et al. characterize Chapter 7 as the “classic ‘straight’ bankruptcy liquidation...” This scheme essentially involves the sale of a debtor’s assets that are not subject to an exemption, with the proceeds going to the creditors, and allows a complete discharge of obligations for the debtor. Chapter 13 allows the debtor to keep his or her property while making reduced payments over time, and calls for a discharge of remaining debt at the end of the plan.

Unsurprisingly, the consumer credit industry balked at the passage of the 1978 bill, though it is arguably fair to say that the credit industry has balked at every turn since the passage of the 1898 Act. In fact, one might

and 75 of the Bankruptcy Act in Actual Operation, 43 YALE L.J. 1285 (1934) (detailing a broad, empirical assessment of debt composition arrangements preceding the Chandler Act).

125. Warren & Westbrook, supra note 51, at 104.


127. See infra Part II.B.


131. See Tabb, supra note 3, at 26-27 (noting a strong push for bankruptcy reform in the 1920s and 1930s after the passage of the 1898 Bankruptcy Act); see also Vern Countryman, Bankruptcy and the Individual Debtor—And a Modest Proposal to Return to the Seventeenth Century, 32 CATH. U. L. REV. 809, 818, 821 (1983) (citing H.R. 12,784, 88th Cong. (1964); H.R. 292, 89th Cong. (1965); S. 615, 89th Cong. (1965); H.R. 1057, 90th Cong. (1967); H.R. 5771, 90th Cong. (1967)) (noting effective lobbying efforts at the state level that were not achievable by debtors and an attempt by the credit industry to enact legislation that mirrored a disfavored “conditional or suspended discharge” from English practice).
even go so far as to argue that such behavior is their corporate duty when confronted with legislation such as this.\textsuperscript{132} Leaving that debate aside, the 1978 bankruptcy law also incorporated language regarding student loans that was first codified in a 1976 amendment to the Higher Education Act of 1965 (HEA).\textsuperscript{133} The text of the amendment came from a report made by a congressional bankruptcy committee formed in 1970.\textsuperscript{134} The essence of the rule was to restrict the discharge of federally funded or insured student loans in bankruptcy for a period of five years after the first payment came due, unless continuing repayment would cause an “undue hardship” for the debtor.\textsuperscript{135}

Apparently, the original sponsors of the bankruptcy code disfavored the addition of the conditional discharge language as applied to student loans.\textsuperscript{136} However, there was a strong voice of dissent from House member Allen E. Ertel, who decried the bill “for its failure to preserve the conditional[] discharge[]” for student loans in bankruptcy.\textsuperscript{137} In the end, Ertel’s argument rang loudest, and the amendment was added to both the HEA and the 1978 Bankruptcy Code.\textsuperscript{138} Congress made several amendments to the Code in the years following its passage.\textsuperscript{139} In 1990, under the Crime Control Act of 1990, Congress extended the five-year restriction on discharging student loans in bankruptcy to seven years, which is of particular concern to the

\textsuperscript{132} See ALAN R. PALMITER, CORPORATIONS: EXAMPLES AND EXPLANATIONS 216 (6th ed. 2009) (alteration in original) ("[M]any courts and commentators assert that fiduciary rules do (and should) proceed from a theory of shareholder wealth maximization[,]" which would seem to logically extend to trying to suppress unfavorable legislation if possible.).

\textsuperscript{133} Compare § 439(a), 90 Stat. 2081, 2141 (alteration in original):

\begin{quote}
A debt which is a loan insured or guaranteed under the [relevant] authority . . . may be released by a discharge in bankruptcy under the Bankruptcy Act only if such discharge is granted after the five-year period . . . beginning on the date of commencement of the repayment period of such loan, except that prior to the expiration of that five-year period, such loan may be released only if the court in which the proceeding is pending determines that payment from future income or other wealth will impose an undue hardship on the debtor or his dependents.
\end{quote}

\textsuperscript{134} with § 523(a)(8)(A)-(B), 92 Stat. 2549, 2590 (alteration in original):

\begin{quote}
A discharge under [relevant authority] does not discharge an individual debtor from any debt . . . to a governmental unit, or a nonprofit institution of higher education, for an educational loan, unless—(A) such loan first became due before five years before the date of the filing of the petition; or (B) excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor’s dependents.
\end{quote}

\textsuperscript{135} See Pardo & Lacey, supra note 14, at 419-20.

\textsuperscript{136} See § 523(b)(A)-(B).

\textsuperscript{137} See Pardo & Lacey, supra note 14, at 420-23.

\textsuperscript{138} Id. at 423-24.

\textsuperscript{139} See WARREN & WESTBROOK, supra note 51, at 105.
student loan analysis.\textsuperscript{140} Just a few years later in 1998, Congress removed the time-based restriction entirely, leaving “undue hardship” as the sole means of affecting a discharge by the bankrupt student debtor—a condition that persists to this day.\textsuperscript{141}

It has been said that the 1978 Bankruptcy Code was “the first bankruptcy law in [United States] history not adopted in the immediate aftermath of a great economic debacle.”\textsuperscript{142} It would seem then that, as a corollary to this, Congress enacted the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), which appears to be the first bankruptcy law in American history that was enacted in the middle of an economic boom.\textsuperscript{143} Whether or not that had an effect on its passage is hard to say; though given the broad economic calamity that arrived very shortly after its enactment, the timing of BAPCPA was seemingly quite fortuitous for the credit industry.\textsuperscript{144} At any rate, one of the stated objectives of the legislation was “to improve bankruptcy law and practice by restoring personal responsibility and integrity in the bankruptcy system.”\textsuperscript{145} To that end, the legislative branch determined that consumer (i.e., non-merchant) debtors should be required to overcome a presumption of abuse before they may discharge their debt under Chapter 7.\textsuperscript{146} Apparently, the “personal responsibility and integrity” of business debtors required no restoration, as the same presumption of abuse does not apply to merchant debtors seeking Chapter 7 bankruptcy relief.\textsuperscript{147}

The dismissal of a consumer bankruptcy petition for abuse was not a new concept; almost twenty years prior to the passage of BAPCPA, Congress made provisions for a court to dismiss a case on its own motion “if it finds that the granting of relief would be a substantial abuse” of Chapter 7.\textsuperscript{148} However, the presumption at that time in favor of granting relief for the debtor, as noted above, was flipped 180 degrees to a

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{142} Warren & Westbrook, supra note 51, at 104.
\item \textsuperscript{143} See, e.g., Adam J. Levitin & Susan M. Wachter, Explaining the Housing Bubble, 100 Geo. L.J. 1177, 1192-94 (2012) (demonstrating a substantial increase in profits from securitized mortgage products around 2005, as part of the so-called “housing boom”).
\item \textsuperscript{146} See 11 U.S.C.S. § 707(b) (LEXIS through Pub. L. No. 114-219).
\item \textsuperscript{147} See § 707(b) (1) (LEXIS) (noting that provision only applies to debts that are “primarily consumer debts”).
\end{itemize}
\end{footnotesize}
presumption of abuse with the passage of BAPCPA. With that change, this new legislative scheme, in a sense, revived the split between merchants and non-merchants in bankruptcy that had lain dormant for the better part of two centuries. Nevertheless, BAPCPA did clarify “substantial abuse” by employing a relatively straightforward means test based on a debtor’s income and expenses. The system is arguably preferable to the previous method of case-by-case determinations by the judiciary, provided, of course, that one accepts the relative merits of combating “substantial abuse” in the first place.

As this brief historical journey comes to a close, it is worth noting that much as in Blackstone’s time, efforts to distinguish “consumer” debt from “business” debt have not always produced the most satisfactory results. In fact, some of the decisions on the issue have resulted in oddly drawn distinctions requiring leaps in logic not dissimilar to Blackstone’s “non-merchant” farmer noted above. For example, it has been ruled that an individual who ran up $119,486 in personal credit card debt to buy stocks was not a consumer debtor. Nor was a personal loan on a credit card, made from a father to a daughter to pay for airline tickets, considered a consumer debt. Obviously, there is selective use here, but the point is that, if the previously mentioned debts cannot necessarily be qualified as de facto consumer debts, it would seem that, at the very least, the notion requires a little more thought. Put another way, imagine if someone used a personal credit card to buy $25,000 worth of stocks on Monday, sold them for a $100 profit on Tuesday, and then used the money to take a cruise.

149. See id.
150. See Tabb, supra note 3, at 16-17 (noting the end of the distinction between different classes of debtors around 1840).
151. See § 707(b)(2) (LEXIS) (authorizing dismissal or conversion of case to chapter 13 if debts are “primarily consumer debts” and debtor fails to meet criteria set forth in detailed means test at (2)(I) of that section).
152. See supra Part II.B.
153. See supra Part II.B.
154. See BLACKSTONE, supra note 60 and accompanying text.
155. See In re Almendinger, 56 B.R. 97, 99 (Bankr. N.D. Ohio 1985). It is noteworthy that, in spite of taking over $100,000 worth of cash advances on the debtor’s personal credit cards in an attempt to recoup stock market losses, the court here still stated, “Ironic though it may sound, [the debtor] testified that he didn’t use his credit cards for ‘frivolous purchases,’ such as vacations.” Id (alteration in original). The Court then, relying in part on that testimony, decided to bar the dismissal. Of course, as noted above, the presumption at the time was in favor of granting a discharge, but bear in mind that, in today’s dollars, this debtor’s cash advances would have amounted to over $250,000. See Samuel H. Williamson, Seven Ways to Compute the Relative Value of a U.S. Dollar Amount, 1774 to Present, MEASURINGWORTH (2015), http://www.measuringworth.com/uscompare/index.php (last visited Feb. 28, 2016). With that said, from a creditor’s perspective, it would seem awfully hard to swallow the idea that squandering $250,000 on stock market speculation is somehow less “frivolous” than if the debtor had taken an expensive cruise.
157. See infra Part II.B.
around the world on Wednesday. If the debtor only made minimum payments on the credit card for a couple of years and then filed for Chapter 7 bankruptcy relief, would this then be a “business” debt? There is a fair amount of case law indicating that the answer would be “yes,” despite the obvious absurdity of such a result.158

Leaving that aside, one can hopefully see that, within the history of bankruptcy, a couple of patterns emerge.159 First, it is clear that there has been a consistent effort to draw distinctions between debts incurred by merchants from those incurred by non-merchants.160 Yet, the rationale behind such distinctions is often lacking upon analysis.161 The apparent underlying cause for this leads to the second discernible pattern in the development of bankruptcy law—morality and bankruptcy.162

III. MORALITY AND BANKRUPTCY

While the underlying rationale for drawing distinctions between merchant and non-merchant debtors is not always clear, what this section will show is the consistent application of moral arguments by the opponents of non-merchant access to debt relief.163 However, it will also be shown that critics rarely challenge those same moral arguments, nor do courts apply them in any meaningful sense to merchant debtors.164 Deconstructing issues of morality, especially in a historical context, would necessarily entail far more analysis than could be reasonably accomplished in this space. However, we need not retreat to the days of Blackstone to see the practical effect of leveraging morality in discussions about default and debt.165

With that said, and pertinent to the discussion at hand, let us begin by focusing on the student loan amendments made to the Higher Education

158. See In re Booth, 858 F.2d 1051, 1054-55 (5th Cir. 1988). Adopting the “profit-motive” standard, this court stated: Cases decided under the Truth in Lending Act indicate that when the credit transaction involves a profit motive, it is outside the definition of consumer credit. After noting the similarities between the definitions in the Truth in Lending Act and the Bankruptcy Code, the court in Almendinger adopted the profit motive definition when applying section 707(b). Because we believe that the profit motive definition is a correct standard in light of the plain meaning of the statute and its legislative history, we also adopt that standard.

159. See infra Part II.B.

160. See WARREN & WESTBROOK, supra note 51, at 104.

161. See infra Part II.B, Part III.

162. See infra Part III.

163. See infra Part III.

164. See infra Part III.

165. See infra Part III.
As discussed above, prior to the passage of the 1978 Bankruptcy Code, the conditional discharge of student loans in bankruptcy was first codified in the HEA. One of the more noteworthy aspects of the discussion surrounding the conditional student loan discharge is the language that Representative Ertel employed to argue for its retention. Rep. Ertel is quoted as saying:

At a time when political, business, and social morality are major issues, it is dangerous to enact a law that is almost specifically designed to encourage fraud. For example, as a student leaves college to find a job, that student would have two options: (1) repay a substantial loan at a time when that student’s financial situation is probably at its lowest, or (2) discharge the debt in bankruptcy, having received the benefit of a free education. If Student A elects to repay the loan, honoring the legal and moral obligation that was incurred, he begins his career with a substantial debt and the accompanying financial pressure. Meanwhile, Student B (who chooses to declare bankruptcy) can begin with a clean slate. . . . [thus] Student B is rewarded for refusing to honor a legal obligation. The lesson that Students A and B have learned is that it ‘does not pay’ to honor one’s debts or other legal obligations.

While much has been made of this in academic literature, perhaps the most pernicious aspect of this short comment is the introduction of morality into the discussion. To clarify that point, imagine if Rep. Ertel had instead said:

At a time when political, business, and social morality are major issues, it is dangerous to enact a law that is almost specifically designed to encourage fraud. For example, as a small business owner establishes their business, that owner would have two options: (1) repay a substantial business loan at a time when the financial situation of their business is probably at its lowest; or (2) discharge the debt in bankruptcy, having received the benefit of a free business start-up.

---

166. See § 439(a), 90 Stat. 2081, 2141.
167. Id.; see § 523(a)(8)(A)-(B), 92 Stat. 2549, 2590-91.
170. See, e.g., Pardo & Lacey, supra note 14, at 424.
Of course, it is entirely possible that business people do indeed assess capital loans in this fashion. Regardless, it should be evident that this simple substitution engenders a decidedly different innate response—the original example rings of self-evidence, while the latter carries a tone of absurdity. As touched on earlier, the original sponsors of the Bankruptcy Code objected to the inclusion of the conditional language regarding student loans in the HEA and the Bankruptcy Code. Authors Pardo and Lacey noted that the sponsors actually delayed the law’s implementation until a requested General Accounting Office (GAO) study on student loan discharges in bankruptcy could be evaluated. Further, in a 2006 paper, author John A.E. Pottow said of the GAO report that, “[u]nfortunately, those empirical data, like many empirical data gathered in Washington, fell on deaf ears. The evidence of a lower than 1% discharge rate of federally insured student loans in bankruptcy did not block the nondischargeability provision from entering the Bankruptcy Code.”

Rather inconveniently though, Rep. Ertel had countered with some data of his own, demonstrating that “[d]uring the four years from 1972 to 1976, defaults and delinquencies in federal student loan programs have increased by more than 300%.” He also mentioned the apparent collapse of a student loan guarantee program administered by the City of Washington D.C. that “was discontinued when defaults exceeded $2 million (more than the city had allocated to cover those loans)” to further buttress his argument. The point of this is not to give weight to Rep. Ertel’s numbers or assertions—for casting doubt on Rep. Ertel’s figures would have been but a simple matter. Rather, this is to call attention to an important

171. See id. at 421-25.
172. See id. at 422.
173. Pottow, supra note 10, at 249.
175. Id.
176. See Arthur F. Burns, The Per Jacobsson Found., The 1979 Per Jacobsson Lecture: The Anguish of Central Banking 8-9 (Sept. 30, 1979), http://www.perjacobsson.org/lectures/1979.pdf. The period between 1972 and 1976 saw a substantial increase in inflation in the United States. In addition to the “loose financing of the war in Viet Nam [sic],” the cause of high inflation was also attributed to:

the devaluations of the dollar in 1971 and 1973, the worldwide economic boom of 1972-73, the crop failures and resulting surge in world food prices in 1973-74, the extraordinary increases in oil prices that became effective in 1974, and the sharp deceleration of productivity growth from the late 1960s onward.

Id. at 9 (alteration in original). Of course, this information does not materially alter Rep. Ertel’s assertion. However, the thrust of Rep. Ertel’s argument was that opportunistic student debtors were taking advantage of an overly permissive bankruptcy system. With that in mind, it should be clear that, at the very least, there were numerous economic factors that could have also been driving the increase in filings. Further, it should also be clear that a reasonable inference might also attribute some of those same factors to the failure of the Washington D.C. student loan guarantee program.
distinction. As authors Pardo and Lacey stated in their very thoughtful paper cited above, Rep. Ertel “couched his dissent in inflammatory terms, resorting to politics of fear.” However, this characterization quickly loses its impact, as just a few pages later, Pardo and Lacey all but endorse Rep. Ertel’s position by stating:

As a general matter, a debtor who borrows money from a creditor knows (1) whether or not he intends to repay the debt, and (2) what circumstances exist or may come into being that reduce the likelihood of repayment . . . to the extent that the debtor’s intentions cannot be (or are too costly to be) unearthed by the creditor, that knowledge is private information unavailable to the creditor. In a legal regime that discharges debtors from personal liability for past debts, private information creates a moral hazard. A debtor who knows that he can obtain a discharge has an incentive to obtain the extension of credit, use the credit, default on his repayment obligation, and ultimately file for bankruptcy to discharge the debt.

As one can see, the latter half of this statement is essentially what Rep. Ertel stated about “Student B” above, minus the social prefacing. For, isn’t the “moral hazard” as outlined by Pardo and Lacey exactly what Rep. Ertel cautioned against when he said that Student B could “discharge the debt in bankruptcy, having received the benefit of a free education” and “begin with a clean slate?” Doesn’t that necessarily take into account Student B operating off his own “private information” in choosing not to repay? Pardo and Lacey continued their analysis by stating that “[t]wo reasons occur to us why moral hazard should be deemed an inappropriate justification for the conditionally dischargeable status of educational debt.” Those two reasons can be roughly summed as: (1) even though the moral hazard exists, debtors did not take advantage of it; and (2) there are already rules in place to deal with people that do take advantage. However, this reasoning essentially relegates the topic to a debate about the best way to deal with moral hazard, when the discussion really should
address whether or not the whole notion can be reduced to moral absolutes in the first place.\textsuperscript{185}

To wit, if Pardo’s and Lacey’s “economic principle” is true “as a general matter,” then why, for example, would an employee ever work for an employer without being paid up front?\textsuperscript{186} Providing labor in exchange for payment at a later date is, in a practical sense, an extension of credit from employee to employer.\textsuperscript{187} In such a case, only the employer knows (1) whether or not she intends to pay the employee; and (2) what circumstances exist or may come into being that reduce the likelihood of payment.\textsuperscript{188} For that matter, does it not logically follow that “private information” and the concomitant “moral hazard” would also be present in a small business loan transaction?\textsuperscript{189} Or in a contract for goods to be delivered with payment due at a later date?\textsuperscript{190} With those questions in mind, at the very least it should be obvious that those “economic principles” outlined above are not necessarily applicable “as a general matter.”\textsuperscript{191} In other words, something else is clearly afoot.

Returning to the student loan amendments, bear in mind that Pardo and Lacey were fairly critical in their article of the conditional discharge provision.\textsuperscript{192} Yet, the arguments they put forward against it are not materially different from those employed by the legislators that sponsored the bill.\textsuperscript{193} Further, they also noted that the bill’s sponsors had the “unanimous support of the Subcommittee on Civil and Constitutional Rights of the House Committee on the Judiciary[,] and the near-unanimous support of the House Judiciary Committee” to repeal a provision that “addressed a perceived, rather than real abuse.”\textsuperscript{194} So, given that these lawmakers: (1) had the near-unanimous support of their peers—information that directly contradicted Rep. Ertel’s; and (2) were otherwise not inclined

\begin{footnotes}
\item[186] See Pardo & Lacey, \textit{supra} note 14, at 429.
\item[187] See Debbie Zatzman, \textit{The Unpaid Employee as Creditor: Case Comment on Homeplan Realty}, 6 \textit{Dalhousie L.J.} 148, 148 (1981) (noting a hypothetical situation in which an unpaid employee becomes a creditor to the employer for her unpaid labor).
\item[188] See Pardo & Lacey, \textit{supra} note 14, at 429.
\item[189] See \textit{id.} at 429-30.
\item[190] See \textit{id.}
\item[191] See \textit{id.} at 429.
\item[192] See \textit{generally id.}
\item[193] See Pardo & Lacey, \textit{supra} note 14, at 430 \& n.126 (citing an argument made by the Bankruptcy Commission in support of its first argument against moral hazard); \textit{see also id.} at 430 \& n.127 (citing a code section that the Committee likely either wrote, or ostensibly had a hand in writing, in support of their second argument against moral hazard).
\item[194] \textit{Id.} at 423.
\end{footnotes}
to include the conditional language, how is it that it was included anyway?\textsuperscript{195}

This speaks to the pernicious aspect of the moral language that Rep. Ertel employed, for once the conditional discharge was established as the correct moral choice, then pressing for its repeal becomes, in effect, inferential support for an immoral position.\textsuperscript{196} Of course, one could never know for certain the mental state of the legislators that voted either for or against the measure.\textsuperscript{197} However, if the “moral hazard” analysis above is taken as true, then what other incentive would be left for the bill’s sponsors to stand firm on the issue of allowing student loan discharges in bankruptcy?\textsuperscript{198} An overriding desire for fairness? The question becomes even more specious if those sponsors had, like Pardo and Lacey, already knowingly or otherwise accepted the underlying rationale supporting the moral hazard argument.\textsuperscript{199} Regardless, what is clear is that, despite the GAO report that demonstrated a “less than one percent” discharge rate for student loans in bankruptcy, a factually isolated statement noting a 300% increase in defaults coupled with a naked assertion of moral hazard was, at least in part, enough to keep the conditional language in the bill.\textsuperscript{200}

Given its seeming effectiveness, it should come as no surprise that moral language again makes an appearance in the run up to the passage of BAPCPA.\textsuperscript{201} The opening text of a 2005 congressional report to recommend passage of the Act is illustrative, where an increase in

\textsuperscript{195} Pardo and Lacey argue:

\texttt{Id. at 425.}

\textsuperscript{196} \textit{See} ROBERT JAY LIFTON, THOUGHT REFORM AND THE PSYCHOLOGY OF TOTALISM: A STUDY OF “BRAINWASHING” IN CHINA 429 (Univ. of North Carolina Press 1989) (1961), for further discussion and analysis to this effect, provided of course that one adopts the premise of Rep. Ertel’s conclusory statement. However, as noted below, statements such as the one made by Rep. Ertel can surreptitiously affect rational thought.

\textsuperscript{197} \textit{See} Pardo & Lacey, \textit{ supra} note 14, at 425.

\textsuperscript{198} \textit{See id.} at 423, 429.


\textsuperscript{201} \textit{See H.R. REP. NO. 109-31, at 2, \textit{reprinted in} 2005 U.S.C.C.A.N. at 88-89 (stating that the purpose of the Bankruptcy Abuse Prevention and Consumer Protection Act is to restore “personal responsibility and integrity in the bankruptcy system . . . .”).}
bankruptcy filings is partially attributed to a “lack of personal financial accountability.” In support of this argument, the report approvingly cites the following quote:

[S]hoplifting is wrong; bankruptcy is also a moral act. Bankruptcy is a moral as well as an economic act. There is a conscious decision not to keep one’s promises. It is a decision not to reciprocate a benefit received, a good deed done on the promise that you will reciprocate. Promise-keeping and reciprocity are the foundation of an economy and healthy civil society.

Disregarding the clumsy association of the criminal act of shoplifting with bankruptcy, the quoted passage, much like Rep. Ertel’s from 1976, cannot be necessarily held as an absolute, for if it is unequivocally true, then it must necessarily apply to business bankruptcies as well. So, then, by what rationale would it be acceptable for a bankruptcy estate or debtor-in-possession to avoid preferential payments under Chapter 11? Under that scheme, the debtor must prove by a preponderance of the evidence that they were already insolvent when they made the preferential payment. Thus, in a practical sense, the debtor must know that he or she is insolvent, then make a payment to a creditor, all the while knowing full well that the creditor will be forced to disgorge the payment in the future when the debtor files for bankruptcy protection. In other words, the only way to trigger the avoidance power is if the business receives the benefit of a “good deed done” on a promise that it knew to be false when it made it. What should be made of this “moral, as well as economic act?”

Further still, why should it be acceptable for a business to reorganize at all under Chapter 11, where the defaulting debtor can “[i]n a sense then . . . force[] the creditors to finance the reorganization venture and to bear the

206. See id. at 439 (“The trustee or other person attacking a transfer as preferential has the burden of establishing that the transfer involved all six elements of a § 547(b) preference. This burden of proof is met by a preponderance of the evidence.” (citations omitted)); see also 11 U.S.C.S. § 547(b) (LEXIS through Pub. L. No. 114-219).
207. See SCARBERRY ET AL., supra note 205, at 439-40 (This example demonstrates an avoidable payment from a hypothetical company. A corporation paid the hypothetical to satisfy a “one-year old, unsecured debt” to a trade creditor that was critical to the operation of the company. The authors note that even though the payment would have been “unassailable under state law,” § 547(b) would still be triggered.).
risk of losses from it”? In such a case, not only has the debtor consciously decided to “not keep one’s promise,” but that debtor can go even further and subordinate those broken promises to encourage loans from new creditors. How does that comport with the notion of “a good deed done on the promise that you will reciprocate”? Or, for that matter, why should it be acceptable in Chapter 11 for a bankrupt company to assume favorable contracts and simply disregard unfavorable ones? Aren’t promise-keeping and reciprocity just as much the foundation of an economy when dealing with a business?

Of course, in the business context, there are many factors to consider when dealing with an insolvent company. Scarberry et al. quite rightly asserted that “[t]he cost to society of business liquidations is high.” They noted the social costs of decreased tax revenues and social welfare for the displaced workers, as well as the devastating financial effect on creditors and workers alike. With that in mind, they further stated that “[k]eep the business in operation will therefore often be much more desirable than liquidating it.” However, the authors also noted that, in some cases, a bankrupt business may have “no going concern value or a going concern value less than its liquidation value”—in which case the business should be shuttered. In other words, each situation is going to be fact dependent. Obviously, trying to hold firm to platitudes or moral absolutes in fact dependent situations would only serve to impede solutions. As such,

---

210. SCARBERRY ET AL., supra note 205, at 15.
211. See id. at 21. The authors stated:

In effect, the prepetition unsecured creditors are involuntarily subordinated to the postpetition creditors. This helps create an incentive for the new creditors to extend credit, but it carries great risks for the prepetition creditors. The new credit may merely permit the debtor to operate at a loss for a longer time and lose even more money.

Id.

213. See SCARBERRY ET AL., supra note 205, at 299-300.
215. Id.
216. See id.
217. See id.
218. See id.
219. See id. at 3 (noting that more harm might befall creditors should such an entity continue operations).
220. See also SCARBERRY ET AL., supra note 205, at 2-3 n.3 (“Many courts will allow such a sale in [C]hapter 11 under the procedurally much easier § 363(b) (1), if there are good reasons for doing so. Congress could have required that a business in [C]hapter 11 be sold quickly as a going concern, so as to avoid many of the complexities discussed in this book. However, Congress did not do so and probably for good reason. There could be severe practical problems with requiring a sale of the assets, especially a quick sale.” (citation omitted)).
221. See generally Ryman, supra note 185.
rather than being a “moral as well as economic act,” bankruptcy is perhaps more fairly characterized as a systematic means of disregarding previous moral and economic acts.\textsuperscript{222} Or, said more plainly, bankruptcy really ought to be called a practical means to find equitable solutions to fact dependent problems.\textsuperscript{223}

Framed in such a fashion, there is no reason to not apply that to consumer bankruptcy as well.\textsuperscript{224} A simple illustration should suffice to clarify this: imagine two friends, Adam and Baker, who decide to go to Las Vegas to gamble for the weekend. Once there, Baker says to Adam, “Please loan me $100 for gambling. I promise that I’ll pay you back tomorrow.” Adam agrees to these terms, and Baker proceeds to lose every penny. Now imagine that later in the afternoon Baker says to a third friend, Charlie, “I have made a conscious decision to not keep my promise to Adam. I know that he did a good deed by loaning me the money to gamble, but I choose not to reciprocate. Do you think that I am immoral?” It would seem safe to say that almost anyone in Charlie’s position would respond in the affirmative.

However, change the facts and imagine instead that when Adam and Baker are returning from Las Vegas, they are involved in a terrible auto accident, which leaves Baker permanently paralyzed from the neck down. If the next day Adam goes to Charlie and says, “Accident or no, Baker made a promise. He owes me $100 and if he doesn’t pay me today, I’m going to sue him.” Adam may be technically correct in his assertion, but from a moral or ethical perspective, it is arguable that such a person would be almost universally reviled. Now change it further and say that if Adam does not receive the $100 back, he is going to lose his house. What role does morality play in Adam and Baker’s situation now?

The obvious point is that it does not really play a role, except in perhaps an abstract or philosophical sense. Yet, once inserted into a topic that requires thoughtful contemplation and equitable analysis, statements such as the ones quoted above essentially become thought-terminating clichés.\textsuperscript{225} In

\begin{footnotesize}
\textsuperscript{223} See In re At Home Corp., 292 B.R. 195, 202 (N.D. Cal. 2003) (“Bankruptcy courts have long possessed the power to exercise equitable powers to further the purposes and goals of the Bankruptcy Code.” (citation omitted)); see also Pottow, supra note 10, at 260; Edward D. Jellen et al., \textit{Recent Developments in Business Bankruptcy—2003}, 27 CAL. BANKR. J. 312, 341 (2004) (“A bankruptcy court has the equitable power under Bankruptcy Code section 105(a) to partially discharge a student loan, so long as the discharged portion meets the requirements of Bankruptcy Code section 523(a) (8).” (citation omitted)).
\textsuperscript{224} At Home Corp., 292 B.R. at 202 (“Bankruptcy courts have long possessed the power to exercise equitable powers to further the purposes and goals of the Bankruptcy Code.” (citation omitted)); see also Pottow, supra note 10, at 260.
\textsuperscript{225} See LIFTON, supra note 196, at 429 (alteration in original) (While defining a thought-terminating cliché, Lifton says, “The most far-reaching and complex of human problems are compressed
\end{footnotesize}
regards to the passage of BAPCPA, the effect is compounded by the fact
that, unlike Rep. Ertel’s easily disputed facts in 1976, the moral argument
above was not only put forth by a well-known academic, but it was also
accompanied by his eighty-plus page research paper.\textsuperscript{226} With that said, it is
not as if BAPCPA was without opposition.\textsuperscript{227} In fact, one of the authors
cited within this article offered very powerful arguments against both the
academic and the reforms, yet those arguments failed to prevent passage of
the Act.\textsuperscript{228} This speaks to the point, especially when one remembers that
the conditional student loan discharge was adopted in protest by “a
comparatively liberal Congress that passed the debtor-friendly 1978
overhaul of the Bankruptcy Code.”\textsuperscript{229} Thus, even though Rep. Ertel’s
supporting facts could have been refuted, once they were coupled with a
moral argument, they became sufficient to overcome the objections of
legislators that, for the most part, did not agree with him at all.\textsuperscript{230} How
difficult of a hill is it to climb when there are two, very credible sounding
experts with extensive, but opposing research, standing before a
legislature?\textsuperscript{231}

This is where the tactical use of moral arguments has its most
demonstrable impact, because decision making in this context is obviously
bounded by the limits of a legislator’s time and cognitive ability, the
complexity of the data, and the information that is available.\textsuperscript{232} However, in
such a situation, if there are known alternatives to choose from, the

\textsuperscript{226} See Bankruptcy Reform Hearing, supra note 92, at 13 (statement of Todd Zywicki, Visiting Professor of Law, Georgetown University Law Center); see also Todd J. Zywicki, An Economic Analysis of the Consumer Bankruptcy Crisis, 99 NW. L. REV. 1463, 1466 (2005) [hereinafter Zywicki, Economic Analysis] (alteration in original) (the latter paper was cited as the source for “[t]he figures presented in [his] testimony” and is eighty-one pages long).


\textsuperscript{228} See id. at 11 (statement of Elizabeth Warren, Leo Gottlieb Professor of Law, Harvard Law School).

\textsuperscript{229} Pottow, supra note 10, at 249.

\textsuperscript{230} See id.; see also Pardo & Lacey, supra note 14, at 421-25.

\textsuperscript{231} See Bankruptcy Reform Hearing, supra note 92, at 10-12 (statement of Elizabeth Warren, Leo Gottlieb Professor of Law, Harvard Law School) (statement of Todd J. Zywicki, Visiting Professor of Law, Georgetown University Law Center).

\textsuperscript{232} See 3 HERBERT A. SIMON, MODELS OF BOUNDED RATIONALITY: EMPIRICALLY GROUNDED ECONOMIC REASON 291 (1997) [hereinafter RATIONALITY] (While defining this concept as “bounded rationality,” Simon says, “The term ‘bounded rationality’ is used to designate rational choice that takes into account the cognitive limitations of the decision-maker—limitations of both knowledge and computational capacity. Bounded rationality is a central theme in the behavioral approach to economics, which is deeply concerned with the ways in which the actual decision-making process influences the decisions that are reached.”).
legislator will tend to calculate an expected utility value of each and then simply choose whichever one seems to offer the most utility—regardless of whether it is necessarily the “right” choice.233 Putting that into this context, given the complex, opposing data sets offered by two credible academics, which choice is going to offer more “utility” to an undecided legislator—the moral one, or an implicitly immoral one?234 To put this in a slightly different light, imagine a congressional lawmaker that has only a cursory understanding of bankruptcy law. Before her is a bill to repeal BAPCPA, a topic that her campaign staff has determined is of neutral value to her constituency. In hearings about the bill, the first expert she hears from is a distinguished professor that teaches at a well-known law school, who provides the following hypothetical testimony:

For the last twenty years, the big banks and finance companies have engaged in unethical and immoral behavior that nearly destroyed the United States economy as we know it. They poured millions of dollars into questionable research to enact laws favorable to their bottom line, while using millions more to dismantle even the most basic of consumer protections, like they did with BAPCPA. They did this all with the promise that doing so would be good for all of us, and good for America.

But, when their schemes didn’t pay off as they had hoped, instead of taking responsibility, they broke their promise to America. They made a conscious decision not to reciprocate a benefit received, a good deed done on the promise that the changes they asked for were good for the economy. Instead, they took billions of dollars in bailouts, gave themselves enormous bonuses, and then left the taxpayers in economic ruin while they enjoyed record profits. This is not only wrong; it is immoral, because promise-keeping and reciprocity are the foundation of an economy and healthy civil society.

Now they say that we still need BAPCPA. We need it not because it helps them keep their ill-gotten profits. No, they say it’s because before the law, bankruptcies were on the rise. They claim that they

233. See HERBERT A. SIMON, AN EMPIRICALLY BASED MICROECONOMICS 17 (1997) [hereinafter MICROECONOMICS] (“Bounded rationality, a rationality that is consistent with our knowledge of actual human choice behavior, assumes that the decision maker must search for alternatives, has egregiously incomplete and inaccurate knowledge about the consequences of actions, and chooses actions that are expected to be satisfactory (attain targets while satisfying constraints).”).
234. See id. at 17; see also Bankruptcy Reform Hearing, supra note 92, at 10-12 (statement of Elizabeth Warren, Leo Gottlieb Professor of Law, Harvard Law School) (statement of Todd J. Zywicki, Visiting Professor of Law, Georgetown University Law Center).
were rising because it was too easy to file for bankruptcy. Yet, the charts below show that the increase in bankruptcies went up at almost the exact same rate that the Dow Jones Industrial Average did. It should be clear from the charts that they’re just using the same misinformation they did before in order to hide their real motivation—profit at any expense.\textsuperscript{235}

\textsuperscript{235} See FCIC Report, \textit{supra} note 144, at 401 (“The securities industry has reported record profits and is once again distributing large bonuses just for those who work in New York City, bonuses at Wall Street securities firms in 2009 were $20.3 billion, up 17% from the year before, with ‘average compensation [rising] by 27 percent to more than $340,000.’ After reporting $54 billion of losses during 2007 and 2008, the New York State Comptroller reported that in 2009, ‘industry profits reached a record $61.4 billion—almost triple the level of three years earlier.’”). The Financial Crisis Inquiry Commission (FCIC) says:

\begin{quote}
[T]he financial industry itself played a key role in weakening regulatory constraints on institutions, markets, and products. It did not surprise the Commission that an industry of such wealth and power would exert pressure on policy makers and regulators. From 1999 to 2008, the financial sector expended $2.7 billion in reported federal lobbying expenses; individuals and political action committees in the sector made more than $1 billion in campaign contributions.
\end{quote}

In light of the fact pattern above, what sort of facts and figures would be sufficient to persuade this legislator to vote in favor of the financial industry? Is it going to matter to her that the increase in the DJIA and the rate of bankruptcy filings are a factually isolated correlation? Even if that did matter to her, how would she explain such a concept in a ten-second soundbite to the public that voted for her? Given the choice between digesting a detailed, eighty-page economic and legal research document supplied by the financial industry or simply voting for the “moral” choice, which one wins in a contest of political “utility”? How much further does the scale tip if the hypothetical academic also has a detailed, eighty-page economic and legal research document to back her claims? Even absent

236. See Zywicki, Economic Analysis, supra note 226, at 1468 fig.1; see also Dow Jones—100 Year Historical Chart, MACROTRENDS, http://www.macrotrends.net/1319/dow-jones-100-year-historical -chart (last visited Sept. 11, 2016).
that, is it realistic to think that a legislator with a currently neutral constituency would risk a negative response simply to support the financial industry’s interests, even if they were in the right? Beyond a fanciful journey through morality and politics, this all bears on the broader discussion at hand regarding student loan discharges in bankruptcy, because as shall now be seen, the effects outlined above are not limited to the legislative branch.237

IV. UNDUE HARDSHIP

As noted by many courts and commentators, when Congress passed the 1978 Bankruptcy Code, it declined to provide a definition for “undue hardship.”238 Consequently, in the years following the Code’s passage, the courts developed a number of tests in order to define “undue hardship,” and these have essentially coalesced into the two predominant tests in use today.239 Both tests offer a significant barrier to student loan discharges in bankruptcy, and while there is some variation, there seems to be little difference between the two schemes when it comes to discharging student loan obligations.240 However, perhaps one of the oddest things within all of that judicial wrangling is the fact that Congress uses the term “undue hardship” twice in the bankruptcy code—one in the section regarding exemptions, and again in the section regarding the effects of discharge.241

This is odd for two reasons: first, in the 261 opinions that Pardo and Lacey examined in their 2005 paper (cited in this article), they only found one instance of a court taking note of the aforementioned fact, and that was in a case decided in 2001.242 This gives rise to the second reason, which is that the undue hardship language in both sections of the Code goes back to its passage in 1978.243 Thus, by the time Congress passed BAPCPA in 2005, twenty-plus years of judicial statutory construction passed before a

237. See Pardo & Lacey, supra note 14, at 487.
238. See, e.g., id. at 486-87.
239. See id. at 487 (“[T]wo judicial tests account[] for the overwhelming majority (86%) applied by bankruptcy courts in [Pardo & Lacey’s study].” The authors then further identify the tests as the Brunner test and the totality of the circumstances test. (alteration in original)).
240. See id. at 487 (noting similar discharge rates for the two tests, with 49% of petitioners under either test receiving a discharge).
241. See 11 U.S.C.S. § 523(a)(8) (LEXIS through Pub. L. No. 114-219) (noting that certain debts are exempt from discharge “unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor’s dependents”); see also 11 U.S.C.S. § 524(c)(3)(B) (LEXIS through Pub. L. No. 114-219) (stating that an agreement to waive a dischargeable debt is only valid if “such agreement does not impose an undue hardship on the debtor or a dependent of the debtor”).
242. See Pardo & Lacey, supra note 14, at 511 n.408.
243. See § 523(8)(B), 92 Stat. at 2591 (stating of an otherwise exempt student loan, “excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor’s dependents . . . ”).
court even attempted to look anywhere else in the Code for assistance in determining the meaning of the phrase. 244 Further, with the passage of BAPCPA in 2005, Congress provided a clear definition for undue hardship under § 524, in the form of statutorily mandated disclosures that a debtor must acknowledge prior to reaffirming an otherwise dischargeable debt. 245 One of the forms reads in pertinent part: “I understand that if my income less my monthly expenses does not leave enough to make the payments, this reaffirmation agreement is presumed to be an undue hardship on me and must be reviewed by the court.” 246

It bears mentioning here that a recent court said of statutory construction that “it is axiomatic that a term ‘may have a plain meaning in the context of a particular section’ of a statute without having ‘the same meaning in all other sections and in all other contexts.’” 247 The court attempted to determine the meaning of the phrase “gainful employment” as used in HEA, but pulled the internally quoted language from Robinson v. Shell Oil Co. 248 In turn, the Robinson court attempted to determine the meaning of the word “employees” in yet another statute. 249 In Robinson, the Supreme Court stated that “[o]nce it is established that the term ‘employees’ includes former employees in some sections, but not in others, the term standing alone is necessarily ambiguous and each section must be analyzed to determine whether the context gives the term a further meaning.” 250 However, this is clearly not the case with BAPCPA, as the context in both sections in which the term “undue hardship” appears is nearly identical—namely, the potentially detrimental effect upon a debtor in continuing to pay for a nondischargeable debt. 251

Further, the term “undue hardship” makes an appearance in the lead up to BAPCPA, when Congress said that it was modifying section 362(b) of

244. See id.
245. See 11 U.S.C.S. § 524(c)(2) (LEXIS through Pub. L. No. 114-219) (noting requirement to receive disclosures described in subsection (k)).
246. 11 U.S.C.S. § 524(k)(1), (3)(J) (LEXIS) (“Part D: Debtor’s Statement in Support of Reaffirmation Agreement . . . . I understand that if my income less my monthly expenses does not leave enough to make the payments, this reaffirmation agreement is presumed to be an undue hardship on me and must be reviewed by the court.”).
248. See id. at 187.
249. See id. at 186.
250. Robinson, 519 U.S. at 343-44.
251. See 11 U.S.C.S. § 523(a)(8) (LEXIS) (noting the debt would be nondischargeable unless it caused an undue hardship); see also 11 U.S.C.S. § 523(a)(10) (LEXIS) (barring discharge of a debt “that was or could have been listed or scheduled by the debtor in a prior case concerning the debtor under this title or under the Bankruptcy Act in which the debtor waived discharge, or was denied a discharge . . . .”).
the Code to allow a debtor’s tax refund to set off a prepetition tax obligation without court approval.252 This was done because “[i]nterest and penalties that may continue to accrue may also be nondischargeable . . . and cause individual debtors undue hardship.”253 Clearly, the rationale behind that modification accords quite well with the usage of “undue hardship” in § 523 and § 524, for it again speaks directly to the potentially detrimental effect on a debtor in paying for a nondischargeable debt.254 Thus, there is not only clear statutory usage of the phrase “undue hardship,” but there is also legislative history that supports a similar application of the phrase in a similar setting.255

Returning to Robinson, the Supreme Court stated that its “first step in interpreting a statute is to determine whether the language at issue has a plain and unambiguous meaning . . . [o]ur inquiry must cease if the statutory language is unambiguous and ‘the statutory scheme is coherent and consistent.’”256 The Court went on to say that “[t]he plainness or ambiguity of statutory language is determined by reference to the language itself, the specific context in which that language is used, and the broader context of the statute as a whole.”257 Following these three simple prongs in order, Merriam-Webster defines “undue” as “more than is reasonable or necessary.”258 Further, it defines “hardship” as “something that causes pain, suffering or loss.”259 Combined, this gives a rough definition for “undue hardship” as that which “unreasonably or unnecessarily causes pain, suffering, or loss.”260

Arguably, “pain” and “suffering” likely do occur in some fashion in the bankruptcy context, but for purposes of legally defining a financial hardship, these terms do not seem ideally oriented to the task.261 However, Merriam-Webster offers a definition of “loss” that reads “money that is spent and that is more than the amount earned or received,” which seems nearly purpose built.262 Putting this all together, we can fashion a definition of “undue hardship” that tracks along the lines of “something that

253. Id.
255. See § 523(b)(8), 92 Stat. at 2591.
257. Id. at 341 (citations omitted).
260. Undue, supra note 258; Hardship, supra note 259.
261. Undue, supra note 258; Hardship, supra note 259.
unreasonably or unnecessarily causes money to be spent that is more than the amount earned or received.” Recalling § 524, which states that “I understand that if my income less my monthly expenses does not leave enough to make the payments, this reaffirmation agreement is presumed to be an undue hardship on me and must be reviewed by the court,” it would seem that, regardless of the rationale that preceded the 1978 Bankruptcy Code, the definition above appears to reasonably comport with what Congress likely intended when they wrote BAPCPA.

As such, if (1) the definition above coherently addresses the language itself; (2) the specific contexts in which that language is used are consistent in the statute; and (3) the broader context of the statute as a whole deals with ameliorating the deleterious effects of defaulting on debt, then it would seem that all three prongs of the Robinson test are satisfied. Therefore, it logically follows that judicial inquiry “must cease” in regards to defining undue hardship, as “the statutory language is unambiguous and ‘the statutory scheme is coherent and consistent.’” However, the incorrect statutory construction by the judiciary is not the only issue present, as an analysis of the two most commonly employed tests for undue hardship will now reveal.

A. Judicial Tests for Undue Hardship

The Brunner test derives its name from a 1985 bankruptcy case that was subsequently affirmed by the United States Court of Appeals for the Second Circuit in 1987. In that affirmation, the Second Circuit wrote that:

[T]he district court adopted a standard for ‘undue hardship’ requiring a three-part showing: (1) that the 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; (2) that additional circumstances exist indicating that this state of affairs is likely to persist for a significant portion of the repayment

263. See Undue, supra note 258; Hardship, supra note 259; Loss, supra note 262.

264. 11 U.S.C.S. § 524(k)(1), (3)(J) (LEXIS) (“Part D: Debtor’s Statement in Support of Reaffirmation Agreement . . . . I understand that if my income less my monthly expenses does not leave enough to make the payments, this reaffirmation agreement is presumed to be an undue hardship on me and must be reviewed by the court.”).

265. See Robinson, 519 U.S. at 340 (citation omitted) (quoting Ron Pair Enterprises, 489 U.S. at 240); see also Undue, supra note 258; Hardship, supra note 259; Loss, supra note 262.

266. See Robinson, 519 U.S. at 340 (citation omitted) (quoting Ron Pair Enterprises, 489 U.S. at 240).

267. See Pardo & Lacey, supra note 14, at 487.

268. See generally In re Brunner, 46 B.R. 752 (S.D.N.Y. 1985), aff’d per curiam, 831 F.2d 395 (2d Cir. 1987).
period of the student loans; and (3) that the debtor has made good faith efforts to repay the loans.  

As one can clearly see, the test as articulated envisions inquiries into the debtor’s income, both past and future. Additionally, before one can make a determination of “undue hardship,” there must be a demonstration of “good faith” by the debtor in attempting repayment.  

In 1981, the United States Court of Appeals for the Eighth Circuit rendered a decision in *Andrews v. S.D. Student Loan Assistance Corp. (In re Andrews)* in which it: (1) articulated the totality of the circumstances test (the totality test); and (2) subsequently reaffirmed the test in *Long v. Educ. Credit Mgmt. Corp. (In re Long)* in 2003.  

In the latter case, the Eighth Circuit gave guidance in administering the test as follows: “[i]n evaluating the totality-of-the-circumstances, our bankruptcy reviewing courts should consider: (1) the debtor’s past, present, and reasonably reliable future financial resources; (2) a calculation of the debtor’s and her dependent’s reasonable necessary living expenses; and (3) any other relevant facts and circumstances surrounding each particular bankruptcy case.” Similar to the *Brunner* test above, one can clearly see a test that delves into the debtor’s income, and that both tests require some manner of inquiry into the debtor’s necessary expenses, with the latter tacking on the circumstantial language in place of the “good faith” prong.  

One should note here that both of these tests draw heavily from comments made in a report by the Bankruptcy Commission to Congress in 1973. In forming its namesake test, the *Brunner* court relies in large part

---

270. *See Brunner*, 831 F.2d at 396-97.
271. 661 F.2d 702 (8th Cir. 1981).
272. 322 F.3d 549 (8th Cir. 2003).
273. *See Long*, 322 F.3d at 553 (citing *Andrews*, 661 F.2d at 702).
274. *Id.* at 554.
275. *Id.* at 553-54.
276. *See Brunner*, 46 B.R. at 754 (“As a calculation of ‘undue hardship,’ the Commission envisioned a determination of whether the amount and reliability of income and other wealth which the debtor could reasonably be expected to receive in the future could maintain the debtor and his or her dependents at a minimal standard of living as well as pay off the student loans.”); *see also Andrews*, 661 F.2d at 704 (“In order to determine whether the nondischargeability of the student loan would impose an ‘undue hardship’ on the debtor, the Commission stated that: . . . the rate and amount of [the debtor’s] future resources should be estimated reasonably in terms of ability to obtain, retain, and continue employment and the rate of pay that can be expected. Any unearned income or other wealth which [sic] the debtor can be expected to receive should also be taken into account. The total amount of income, its reliability, and the periodicity of its receipt should be adequate to maintain the debtor and [the debtor’s] dependents, at a minimal standard of living within their management capability, as well as to pay the educational debt.”).
on *In re Johnson*, In re Andrews, and *In re Briscoe* for much of its analysis. The Brunner court utilizes *In re Briscoe* in support of the need to estimate the debtor’s future earnings and the conditional need for a “certainty of hopelessness” in not being able to repay. All four of these decisions, in whole or in part, reference the following passage from the aforementioned 1973 report:

In order to determine whether nondischargeability of the debt will impose an ‘undue hardship’ on the debtor, the rate and amount of his future resources should be estimated reasonably in terms of ability to obtain, retain, and continue employment and the rate of pay that can be expected. Any unearned income or other wealth which the debtor can be expected to receive should also be taken into account. The total amount of income, its reliability, and the periodicity of its receipt should be adequate to maintain the debtor and his dependents, at a minimal standard of living within their management capability, as well as to pay the educational debt.

As noted above, not only does the Brunner court cite *In re Andrews*, but *Andrews* also forms the basis of the totality test favored by the Eighth Circuit. *Andrews* further references yet another case, *In re Wegfehrt*, which also pulls the same text noted above. However, the Wegfehrt court goes further still and quotes two particularly illuminating passages in support of its findings. The first quote reads: “a few serious abuses of the bankruptcy laws by debtors with large amounts of educational loans, few other debts, and well-paying jobs, who have filed bankruptcy shortly after leaving school and before any loans became due, have generated the movement for an exception to discharge,” while the second quote states that: “[i]f under eighty percent (80%) of the debtor’s debts were educational...

---

279. See generally Brunner, 46 B.R. at 752.
280. Id. at 755.
282. See Long, 322 F.3d at 554.
283. 10 B.R. at 826.
284. See id. at 830.
debts, then it is likely that the debtor has encountered financial difficulty after school, and that the bankruptcy is a result of a true need for bankruptcy relief rather than an abuse of the bankruptcy system.\(^\text{286}\)

With that said, if one steps back a bit, what is plain to see is that the two predominant tests for determining undue hardship are judicially created, means-based tests rooted in a Congressional desire to prevent abuse of the bankruptcy system.\(^\text{287}\) In fact, the Wegfehrt court actually said of the petitioner that “[t]his Court is of the opinion that debtor herein is not guilty of the intentional abuse of bankruptcy laws which 11 U.S.C. Section 523(a)(8) was intended to bar.”\(^\text{288}\) Bear in mind, of course, that at the time these cases were decided, the bankruptcy court had provisions in place to dismiss a case “if it finds that the granting of relief would be a substantial abuse” of Chapter 7.\(^\text{289}\) Thus, it was entirely appropriate for the courts to fashion the tests outlined above to further the policy of preventing abuse in the undue hardship context.\(^\text{290}\)

However, with the passage of BAPCPA, this is no longer the case, as Congress has precluded the judiciary from precisely this type of endeavor.\(^\text{291}\) To wit, Congress states that “[t]he standard for dismissal—substantial abuse—is inherently vague, which has led to its disparate interpretation and application by the bankruptcy bench.”\(^\text{292}\) In order to remedy this, Congress amended the law to “require a court to presume that abuse exists if the amount of the debtor’s remaining income, after certain expenses and other specified amounts are deducted from the debtor’s current monthly income.”\(^\text{293}\) In support of this, the academic noted above said:

> [c]urrent law requires a case-by-case investigation that turns on little more than the personal predilections of the judge. The Bill narrows the judge’s discretion by establishing a presumption of abuse where a high-income debtor has the ability to repay a substantial portion of his debts, as measured by an objective standard.\(^\text{294}\)

---

\(^{286}\) Id.

\(^{287}\) See Brunner, 831 F.2d at 396; see also Long, 322 F.3d at 553-54 (alteration in original).

\(^{288}\) Wegfehrt, 10 B.R. at 830.

\(^{289}\) See § 312, 98 Stat. at 355.

\(^{290}\) See id.


\(^{293}\) Id. at 13.

\(^{294}\) Bankruptcy Reform Hearing, supra note 92, at 248 (statement of Todd Zywicki, Visiting Professor of Law, Georgetown University Law Center).
So, while the “the judge will retain discretion to override this presumption in cases of hardship,” the judge has not been afforded the discretion to make determinations of what constitutes abuse for over a decade now.295 In fact, BAPCPA provides very clear, income-based guidelines on what is or is not abusive conduct by the consumer debtor, and it requires a judge to convert or dismiss the case if the debtor falls outside of those guidelines.296 Further, as noted above, Congress has also specifically drafted a test to determine when an undue hardship exists in relation to a debtor’s ability to pay a continuing, nondischargeable obligation.297 With that said, by what reading of the statute does the judiciary then presume to impart its own means test using a “case-by-case investigation that turns on little more than the personal predilections of the judge” in determining if undue hardship claims are “an abuse of the bankruptcy system”?298 Such a judicial policy may have had its place under the 1978 Bankruptcy Code, but that Code is no longer the law of the land.299

It has been said by both the courts and commentators alike that the increase in restrictions on discharging student loans in bankruptcy demonstrates that Congress wants the bar to discharge to be made more difficult.300 Yet, the assertion only has merit if taken in isolation, for while it is true that the time-based restrictions have been curtailed, it is also true that determinations of what abusive conduct is and when a condition imposes an undue hardship have been greatly clarified as well.301 Put another way, it could be fairly said that while Congress has increased the restrictions on discharging student loan debt, it has also restricted a judge’s discretion in determining both when abuse is occurring and what standard of living is acceptable for a debtor post discharge.302 Congress did this by requiring the judiciary to use a statutorily mandated means test that also accounts for a debtor’s reasonable expenses.303 Further, just as Congress clarified when abuse is occurring, it also made clear when an undue hardship exists and, by rational extension, when a debtor should be allowed

295. Id.
296. See generally 11 U.S.C.S. § 707(b) (LEXIS) (detailing requirements for determining abuse and requirement for dismissal or conversion if abuse is determined by results of means test).
297. See Wegfehr, 10 B.R. at 830.
298. See Bankruptcy Reform Hearing, supra note 92, at 248 (statement of Todd Zywicki, Visiting Professor of Law, Georgetown University Law Center); see also id.
299. See generally 119 Stat. at 23.
300. See, e.g., Pottow, supra note 10, at 250 (quoting In re Cox, 338 F.3d 1238, 1242 (11th Cir. 2003)) (“Congress’s [sic] intent to make it harder for a student to shift his debt responsibility onto the taxpayer.”).
301. See § 102(a), 119 Stat. at 27 (providing tests for when abuse exists).
302. See 11 U.S.C.S. § 707(b) (LEXIS) (listing statutorily allowable expenses and means of calculating them).
303. See id.
to eliminate student loan debt in bankruptcy.\textsuperscript{304} Rather than making student loan discharge insurmountable, Congress instead appears to have made it difficult, yet also more equitable, by removing judicial interpretation of the debtor’s means and standard of living entirely.\textsuperscript{305}

As such, it should be clear that after a debtor overcomes the statutory presumption of abuse and then further demonstrates in an adversarial proceeding that their “income less [their] monthly expenses does not leave enough to make [their] payments,” they should be allowed to discharge their student loan debt as an undue hardship.\textsuperscript{306} If Congress subsequently determines that such a policy is too “loose,” it is free to fashion a new regulation or test as it sees fit.\textsuperscript{307} However, what should be abundantly clear is that, under the law as it currently stands, the judiciary absolutely may not make this determination.\textsuperscript{308}

V. CONCLUSION

Though the research is clear, it is not lost on this author that this paper essentially proposes that over a decade of judicial decision making is clearly erroneous.\textsuperscript{309} It was largely with this in mind that the discussion on moral hazard and moral arguments was developed in Part III.\textsuperscript{310} For, not only does this paper posit that over a decade of judicial decision-making is incorrect, it also points out that even some of the staunchest opponents of the undue hardship tests have missed the broader point as well.\textsuperscript{311} This traces back to the discussion in Part II, for it is arguably the central purpose of the “thought-terminating cliché” to do what has ostensibly happened in this context—namely, to prevent otherwise conscientious and thoughtful people from seeing clearly erroneous information.\textsuperscript{312}

While the use of moral arguments may have been a bit disingenuous in enacting BAPCPA, the perhaps unintended consequence of the new regulations is that they clearly make more room for the student debtor to discharge loans in bankruptcy, if one allows themselves to step back from the myopia of the current analysis.\textsuperscript{313} For those who might question the wisdom of such a judicial policy, it one should note that the Duncan case

\textsuperscript{305} See id. at 233-35.
\textsuperscript{306} See id. at 242.
\textsuperscript{307} See U.S. CONST. art. I, § 1.
\textsuperscript{308} See supra Part III.
\textsuperscript{309} See supra Part I.
\textsuperscript{310} See supra Part III.
\textsuperscript{311} See supra Part III.
\textsuperscript{312} See Lifton, supra note 196, at 429.
\textsuperscript{313} See supra Part III.
cited above is (as of this writing) a very recent case that approved new tests by the Department of Education (DOE) “to establish minimal measures for determining whether certain post-secondary educational programs lead to gainful employment in recognized occupations.” The consequence of an institution failing this test is that they will no longer qualify for federally guaranteed student loans. In other words, DOE is trying “to ensure that participating schools actually prepare their students for employment, such that those students can repay their loans.”

To determine if a student loan recipient is gainfully employed, the DOE will use the two tests as follows:

The first is a debt-to-discretionary-income metric, which the Department calculates by dividing the median annual loan payment for a program’s students by those same students’ discretionary income (which is equal to ‘the higher of the mean or median annual earnings’ of the students minus 150% of the poverty-guidelines figure). The second is a debt-to-annual-income metric, which the Department calculates using a simpler equation—just dividing the median annual loan payment for a program’s students by the mean or median annual earnings of those students, whichever is greater.

These new tests are likely in response to DOE’s recent findings that “nearly 3 million Direct Loan borrowers [are] more than 30 days delinquent on their loans, and 3.2 million borrowers are in default on more than $44 billion in Federal loans.” As such, it seems eminently reasonable that DOE take steps to ensure that taxpayer dollars are allocated to programs that will actually provide some benefit to the recipients. However, these new tests are also going to come too late to help those that have already borrowed to pay for an education, but still find themselves in default or worse yet, as part of the 16% of unemployed graduates that have almost no possibility of relief. It is unconscionable to burden an entire generation

314. Duncan, 110 F. Supp. 3d at 182.
315. See id. at 183 (“A program loses eligibility for all Title IV financial aid if it fails the debt-to-earnings test for two out of three consecutive years.
316. See id. at 181.
317. See generally id.
319. See generally id.
320. See CONSUMER FIN. PROTECTION BUREAU, PRIVATE STUDENT LOANS 4 (2012) (alteration in original), http://files.consumerfinance.gov/f/201207_cfpb_Reports_Private-Student-Loans.pdf (“In 2009, the unemployment rate for private student loan borrowers who started school in the 2003-2004 academic year was 16%.”). It should be said that, while the figures represented are dated, the Consumer Financial Protection Bureau (“CFPB”) also pointed out in a later report that 25% of student loan borrowers are
of students with a potential lifetime of debt based on erroneous presumptions and outdated tests that do not represent the current state of the law. 321 Those encumbered by unmanageable debts precisely represent the fact-dependent issues that the mechanism of bankruptcy is designed to address. 322 With that said, applying the undue hardship analysis, as demonstrated above, to those fact-dependent issues is hardly revolutionary. 323 It is simply following the law and common sense.

“collectively, either delinquent or in default on more than $175 billion in student debt.” See CONSUMER FIN. PROTECTION BUREAU, STUDENT LOAN SERVICING: ANALYSIS OF PUBLIC INPUT AND RECOMMENDATIONS FOR REFORM 9 (2015), http://files.consumerfinance.gov/f/201509_cfpb_student-loan-servicing-report.pdf. “[T]here are also significant gaps in available data about higher education and student loan performance, including key outcome measures such as job attainment and wage information[.]” Id. at 10. Thus, the information from 2009 was utilized for illustrative purposes.

321. See supra Part III.
322. See supra Part III.
323. See supra Part IV.