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Illness and Inability to Repay: The Role of Debtor Health in the Discharge of Educational Debt

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ILLNESS AND INABILITY TO REPAY: THE ROLE OF DEBTOR HEALTH IN THE DISCHARGE OF EDUCATIONAL DEBT

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ABSTRACT

For a debtor to obtain a discharge of student loans in bankruptcy, the debtor must establish that repayment of the loans would impose an undue hardship. This Article presents the results of an empirical study of bankruptcy court doctrine over a ten-year period that involved undue hardship discharge proceedings where the court reported information on the debtor's health status, monthly household income, and monthly household expenses. The data show that a medical condition increased a debtor's odds of being granted a discharge by 140%, but that household income and expense levels did not have a statistically significant association with legal outcome. These results suggest that a great deal of bankruptcy court doctrine regarding the discharge of educational debt has given a meaning to the statutory term "undue hardship" that is far removed from financial indicia of ability to repay. As a consequence, the statute has not been given its proper reach and has failed to achieve its proper sorting function—that is, identifying those debtors without a meaningful ability to repay their educational debt.

I. INTRODUCTION

In 2005, Michelle Lacey and I reported the results of an empirical study of the application of bankruptcy court doctrine over a ten-year period in determinations involving the discharge of educational debt (the 2005 study).[1] The data showed that remarkably few statistically

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1. Rafael I. Pardo & Michelle R. Lacey, *Undue Hardship in the Bankruptcy Courts: An Empirical Assessment of the Discharge of Educational Debt*, 74 U. CIN. L. REV. 405 (2005).

significant differences existed between those debtors granted and denied a discharge. We concluded that the outcome in the analyzed cases could best be explained as the product of differing judicial perceptions of how the same legal standard—undue hardship—applied to relatively similarly situated debtors.

This Article revisits the data from the 2005 study and explores whether some of the differences between debtors granted and denied a discharge can account for the legal outcome in a particular subset of cases. Part II provides a brief overview of the 2005 study, including its salient findings. Part III discusses the subset of cases that have been identified for further study in this Article and then presents the results from a statistical analysis that seeks to predict the outcome in undue hardship discharge determinations according to three factual circumstances: (1) the debtor's monthly household income, (2) the debtor's monthly household expenses, and (3) the debtor's health. Part IV interprets the results and argues that a great deal of bankruptcy court doctrine has been misguided in its effort to classify debtors who have an ability to repay their educational debt.

II. THE 2005 STUDY

The 2005 study drew its data from 261 published and unpublished opinions that were issued during the ten-year period beginning on October 7, 1993 and ending on October 6, 2003 and that involved discharge determinations of educational debt pursuant to the undue hardship standard.[2] Since some of these opinions involved multiple discharge determinations, the data consisted of 286 discharge determinations.[3] The study tracked the demographic and financial characteristics of the debtors who sought to discharge their educational debt with two goals in mind: (1) describing the type of individual who sought a discharge in order to gain a sense of the degree of hardship faced by such an individual,[4] and (2) comparing differences between those debtors granted and those debtors denied a discharge in order to identify the factual circumstances that courts deemed to constitute undue hardship.[5] These characteristics revealed that the majority of the debtors in the study had confronted financial hardship at the time they requested a discharge and "did not have a reasonable pros-

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2. The Bankruptcy Code excepts from discharge certain educational debt unless it can be established that "excepting such debt from discharge . . . would impose an undue hardship on the debtor." 11 U.S.C.S. § 523(a)(8) (LexisNexis 2007); *see also id.* § 1328(a)(2) (providing that scope of a Chapter 13 discharge does not include § 523(a)(8) debt).

3. For a detailed discussion of the selection criteria implemented in the 2005 study, see Pardo & Lacey, *supra* note 1, at 433-38.

4. *Id.* at 439-78.

5. *Id.* at 478-86.

pect of repaying their educational debt."[6] However, only 45% of these financially distressed debtors received a discharge.[7] In seeking to account for the factual circumstances that would allow a debtor to prevail in a claim of undue hardship, the study found that the demographic and financial characteristics of debtors granted a discharge and debtors denied a discharge were, for the most part, remarkably similar.

Various financial indicators suggested that the debtors in the 2005 study did not have a realistic ability to repay their educational debt. For example, for the opinions in which the court reported the debtor's net monthly household income,[8] the average debtor's household generated $2111 per month (in 2003 dollars).[9] When converting this figure to annual household income and comparing it to the amount of household income defined by the U.S. Department of Health and Human Services (HHS) as the poverty line threshold, the study found that the average debtor household did not generate sufficient income to double the poverty line threshold.[10] Importantly, when taking into account monthly household expenses, exclusive of educational debt expenses, the average debtor household had a monthly *deficit* of $83.66. Put another way, the average debtor household did not have any disposable income to devote to repayment of the debtor's educational debt. The study also found that the average debtor would have had to devote more than two years' worth of net annual household income to repay his or her educational debt in full. This further suggested that staggering educational debt loads had placed a severe financial strain on the debtors in the study and that they had a legitimate need for relief.[11]

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6. *Id.* at 477-78.

7. *Id.* at 479.

8. The majority of opinions featured in the 2005 study reported a debtor's income in terms of net income. *Id.* at 457. The 2005 study theorized that net income constituted the debtor's current monthly gross wages, salary, and commissions reduced by the amount of any payroll deductions, such as payroll taxes, social security, insurance, and union dues. *Id.* at 453.

9. All dollar amounts reported in this Article are in 2003 dollars.

10. The 2004 HHS poverty guidelines, which were used in the 2005 study to calculate the ratio of the debtor's annual household income to the poverty line threshold, *see* Pardo & Lacey, *supra* note 1, at 462, defined the poverty line for the contiguous United States as a household with income of $9310 for the first member and $3180 for each additional member. Annual Update of the HHS Poverty Guidelines, 69 Fed. Reg. 7336, 7336 (Feb. 13, 2004). Accordingly, for an individual in a single-member household, the inability to generate sufficient income to double the poverty line threshold would mean that his or her annual household income was less than $18,620. Such proximity to the poverty line conjures the image of a debtor living a marginal existence. It seems reasonable to conclude that such an individual would not be well poised to make educational debt payments.

11. This measure assumes that household income would remain constant, that the educational debt would not increase by virtue of interest or other charges, and that the debtor's household would live expense free. For a summary of the financial characteristics

To identify the factual circumstances associated with the grant of an undue hardship discharge, the study compared the demographic and financial characteristics of debtors granted a discharge (the discharge group) and debtors denied a discharge (the nondischarge group). Surprisingly, there were more similarities than dissimilarities between the two groups. Both groups had similar compositions in terms of the debtor's gender, age, marital status, number of dependents, employment status, occupation type, and level of educational attainment.[12] The only statistically significant demographic differences between the two groups related to three health-related characteristics. First, the discharge group had a greater percentage of unhealthy debtors: 72% compared to 54% for the nondischarge group. Second, for the subset of debtors with a medical condition, the discharge group had a greater percentage of debtors whose medical condition limited their ability to work: 49% compared to 25% for the nondischarge group. Third, for the subset of debtors with dependents, the discharge group had a higher percentage of debtors responsible for an unhealthy family member: 86% compared to 42% for the nondischarge group.[13]

With respect to financial characteristics, the study also documented more similarities than dissimilarities between the discharge group and the nondischarge group. The study did find that the median monthly household income and median monthly household expenses of the discharge group were statistically significantly lower than the nondischarge group. Specifically, the discharge group had a median monthly household income of $1623 in comparison to $2072 for the nondischarge group, and the discharge group had median monthly household expenses of $1837 in comparison to $2313 for the nondischarge group. However, no statistically significant differences existed with respect to median levels of monthly disposable household income, educational debt, or the ratio of educational debt to annual household income.[14] On the basis of these findings, the study concluded that the law had been inconsistently applied to relatively similarly situated debtors,[15] and it subsequently demonstrated through statistical modeling that the outcome of undue hardship discharge determinations in the study could be described as the product of varying judicial perceptions of the meaning of undue hardship.[16]

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of the debtors in the 2005 study, see Pardo & Lacey, *supra* note 1, at 454 tbl.1, and for a detailed discussion of these characteristics, see *id.* at 452-76.

12. *Id.* at 482 tbl.4, 483 tbls.5 & 6.
13. *Id.* at 485 tbl.8.
14. *Id.* at 484 tbl.7.
15. *Id.* at 486.
16. *Id.* at 486-509.

Although the 2005 study revealed that a limited number of factual circumstances were associated with the outcome of the undue hardship discharge determinations, it did not seek to fit a statistical model that would predict outcome according to these circumstances for two reasons. First, not all of the discharge determinations in the study reported sufficient information to document these circumstances. For example, notwithstanding the statistically significant relationship between a debtor's monthly household income and a court's decision to grant an undue hardship discharge, approximately 15% of the discharge determinations did not report sufficient information on monthly household income.[17] Second, some of the statistically significant factual circumstances were limited to an extremely narrow subset of discharge determinations. For example, the relationship between the health status of a debtor's dependents and the outcome of the discharge determination could only be explored for those discharge determinations involving debtors with dependents—specifically, only 56% of all discharge determinations.[18] Moreover, only half of these determinations provided sufficiently detailed information to document the health status of a debtor's dependents.[19] Accordingly, the relationship between this factor and legal outcome could only have been explored in 28% of the discharge determinations. Because of these constraints, the statistical modeling in the study instead focused on the conclusions reached by the court with respect to the distinct doctrinal factors that constituted the ultimate holding on undue hardship.[20] This Article now seeks to explore what, if anything, statistical modeling based on certain factual characteristics will tell us about the application of the undue hardship standard in a subset of discharge determinations from the 2005 study.

III. REVISITING *UNDUE HARDSHIP IN THE BANKRUPTCY COURTS*

The 2005 study emphasized that, since its data were drawn only from undue hardship discharge opinions disseminated to Westlaw over a ten-year period,[21] it could not be claimed that the data were representative of the manner in which courts adjudicated all dis-

17. *Id.* at 484 tbl.7.
18. *Id.* at 482 tbl.4.
19. *Id.* at 485 tbl.8.
20. The study modeled the decisionmaking process according to three core legal considerations—the debtor's current inability to repay, the debtor's future inability to repay, and the debtor's good faith effort to repay—of which at least one was referenced in each discharge determination in the study. As a result, the statistical model classified all of the discharge determinations in the study. The study then sought to determine the factual circumstances relevant for assessing each of those considerations, yet once again found that factual circumstances played a limited role in accounting for the legal conclusions reached by courts. *Id.* at 486-509.
21. *Id.* at 410 & n.21.

charge determinations during that time period.[22] In light of that limitation, one might question the value of empirical analysis of a subset of these data. The answer is simply this: If evidence of associations between certain factual characteristics and legal outcomes can be established for a large subset of the data, even when controlling for other factors, the emerging patterns will reveal what influenced a large number of bankruptcy courts in reaching their dispositions. In turn, the propriety of such associations can be evaluated from both a normative perspective and a practical perspective. Normatively speaking, if past experience demonstrates that courts have inappropriately allowed certain facts to give content and meaning to the phrase "undue hardship," or alternatively have failed to give certain facts their due weight, then prescriptions can be made that will guide future decisionmakers in giving proper reach to the law. Practically speaking, if past patterns serve a signaling function to future litigants regarding the likelihood of relief in undue hardship discharge determinations,[23] or for that matter future decisionmakers, then the effect and desirability of such signals should be assessed.

This Part presents the results from a binary logistic regression model used to predict whether a bankruptcy court granted a debtor an undue hardship discharge based on the following independent variables: (1) the debtor's monthly household income, (2) the debtor's monthly household expenses, and (3) the debtor's health status. Approximately 60% of the discharge determinations in the dataset from 2005 study had information for each of these variables.[24] The analysis that follows seeks to ascertain whether the associations discovered in the 2005 study with respect to each of these variables persist when the variables are jointly incorporated into a statistical model.

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22. *Id.* at 433-34.

23. *See* Bernard Trujillo, *Regulating Bankruptcy Abuse: An Empirical Study of Consumer Exemptions Cases*, 3 J. EMPIRICAL LEGAL STUD. 561, 574 (2006) (noting in an empirical study of bankruptcy court doctrine in consumer exemptions proceedings over a twenty-year period that "patterns [across a large number of cases] tell us not only what particular judges accomplished in specific cases, but also what courts have signaled to future litigants about . . . debtors' chance of success" (footnote omitted)).

24. Of the 286 discharge determinations in the dataset from the 2005 study, 175 included information for the debtor's health, monthly household income, and monthly household expenses. However, any observation involving a debtor with an extreme amount of monthly household income or monthly household expenses was omitted from the statistical model in this Article. For this subset of debtors, any debtor with monthly household income that fell above the third quartile ($2715.47) of the household income data by more than three times the interquartile range ($1531.90) for such data was deemed to be an extreme outlier. In similar fashion, any debtor with monthly household expenses that fell above the third quartile ($2762.82) of the household expense data by more than three times the interquartile range ($1472.82) for such data was deemed to be an extreme outlier. Three extreme outliers were identified on the basis of monthly household income and none on the basis of monthly household expenses. Thus, the statistical analyses in this Article are based on 172 discharge determinations.

The data show that the financial indicators have no statistically significant effect on the outcome of the discharge determination. On the other hand, a debtor's health status is a statistically significant predictor of outcome: If a debtor suffered from a medical condition, the existence of that condition increased the debtor's chances of being granted a discharge. A detailed discussion of these findings now follows.

Overall, the model is statistically significant as compared to a model without independent variables, and it correctly predicts the outcome in approximately 63% of the discharge determinations.[25] Of course, without referring to any of the independent variables in the model, one could correctly classify the outcome in some of these determinations by assigning the most-frequent category of outcome (i.e., the marginal distribution of the dependent variable) to all of the determinations. In this case, one could correctly classify the outcome in 52% of the discharge determinations by guessing nondischarge for all determinations.[26] Thus, when predicting with the model that includes the independent variables of the debtor's monthly household income and expenses, as well as the debtor's health status, the error rate drops by approximately 22% (i.e., the adjusted count R^2) compared to a prediction based solely on the marginal distribution of the dependent variable.

When controlling for the effect of all other variables in the model, only the debtor's health status remains a statistically significant predictor of an undue hardship discharge. In other words, for these discharge determinations, no relationship existed between discharge and a debtor's monthly household income or household expenses. The question arises then as to the size of the effect a debtor's health had upon a court's propensity to grant an undue hardship discharge. The model indicates that suffering from a medical condition made a debtor's odds of being granted a discharge 2.40 times higher.[27] Put another way, holding all other variables constant, the existence of a medical condition increased the debtor's odds of being granted a discharge by 140%.[28]

These findings can further be interpreted using predicted probabilities. Using the actual values for all of the independent variables

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25. For any observation for which the model predicted a probability of over 50% for the outcome of discharge, the model assigned the positive outcome of discharge; for any observation for which the model predicted a probability of under 50%, the model assigned the negative outcome of nondischarge.

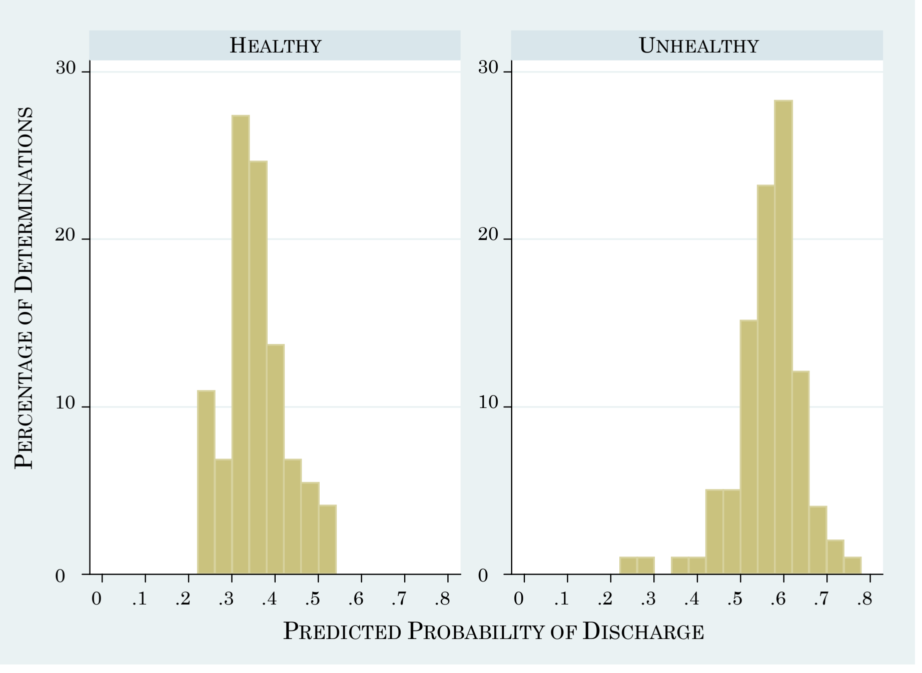
26. For the 172 observations included in the regression model, the court denied a discharge in 90 of those observations.

27. It can be said with 95% certainty that this figure could be as low as 1.27 times and as high as 4.52 times.

28. It can be said with 95% certainty that this figure could be as low as 27% and as a high as 352%.

included in the model, the predicted probability of discharge is calculated. Figure 1 below presents the predicted probabilities for discharge in the actual observations in the regression model through use of a histogram that separately displays the distribution of those probabilities for healthy debtors and unhealthy debtors. The width of each bar represents a specific interval of the predicted probability of discharge, and the height of each bar represents the percentage of discharge determinations that fall within that interval. For any observation with a predicted probability of over 50% (i.e., greater than 0.5), the model assigned the positive outcome of discharge. A comparison of the two distributions reveals that, whereas approximately 86% of the determinations involving unhealthy debtors had greater than a 50% predicted probability of a discharge being granted, only 4% of the determinations involving healthy debtors did so.

FIGURE 1
PREDICTED PROBABILITY OF DISCHARGE BY DEBTOR HEALTH STATUS



Probabilities of discharge for *hypothetical* sets of values can also be predicted. For example, holding monthly household income and expenses at their mean values (respectively, $2018 and $2158), the probability of an unhealthy debtor being granted a discharge is predicted to be approximately 57%,[29] whereas for a healthy debtor it is predicted to be 35%.[30] Accordingly, the presence of a medical condition is predicted to have increased the likelihood of discharge for a debtor with average income and expenses by twenty-two percentage points.

On the basis of these data, it is clear that the status of a debtor's health greatly influenced a court's decision to grant an undue hardship discharge in 60% of the discharge determinations from the 2005 study. How should one interpret the primacy of a debtor's health status in influencing the outcome in over half of the discharge determinations documented in opinions issued by bankruptcy courts from the end of 1993 through the end of 2003? Moreover, what importance should be given to the failure of financial considerations (i.e., monthly household income and household expenses) to play an explanatory role in ascertaining whether the nondischarge of educational debt would impose an undue hardship on a debtor? Part IV seeks to answer these questions.

IV. RECONSIDERING THE ROLE OF DEBTOR HEALTH IN THE DISCHARGE OF EDUCATIONAL DEBT

This Part interprets the results from the regression analysis presented in Part III. In doing so, it assesses the effectiveness of the manner in which bankruptcy court doctrine has functioned to resolve the issue of the discharge of educational debt. Again, it should be emphasized that this Article does not purport to provide a definitive or exhaustive account of such doctrine. The data only represent 60% of a decade's worth of undue hardship opinions—a snapshot in time. Accordingly, caution must be exercised in drawing inferences regarding the representativeness of such data with respect to bankruptcy court doctrine on the topic that has subsequently emerged. Keeping these limitations in mind, it is not an unreasonable proposition to think that the past practice has informed the manner in which bankruptcy judges continue to apply the doctrine that elaborates on the meaning of undue hardship, especially as there have not been any recent seismic shifts in the doctrine prompted by hierarchical mandates from the U.S. Courts of Appeals or the Supreme Court. By focusing on patterns that have emerged over time and discerning their import, a more concrete understanding of the doctrine can be achieved than if one were to analyze a handful of opinions in isolation.

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29. It can be said with 95% certainty that this figure could be approximately as low as 47% and no higher than approximately 67%.

30. It can be said with 95% certainty that this figure could be approximately as low as 24% and no higher than approximately 46%.

In order to understand why a debtor's illness has played a substantive role in giving meaning to the term "undue hardship," a brief discussion of the doctrinal framework bankruptcy courts have adopted to implement the standard is necessary. Since the Bankruptcy Code fails to define the term,[31] courts have formulated tests to apply the standard. In *Brunner v. New York State Higher Education Services Corp.*,[32] the Second Circuit Court of Appeals articulated a three-part test (the *Brunner* test) for undue hardship that requires a debtor to establish:

> (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 period of the student loans; and (3) that the debtor has made good faith efforts to repay the loans.[33]

With the formal adoption of this framework by eight other federal regional circuits,[34] this framework has become the dominant mode for analyzing a debtor's claim of undue hardship. Some courts, however, have implemented the "totality of the circumstances" test (the totality test), which "requires an analysis of (1) the debtor's past, present, and reasonably reliable future financial resources; (2) calculation of the debtor's and his dependents' reasonable necessary living expenses; and (3) any other relevant facts and circumstances surrounding that particular bankruptcy case."[35] This approach has been endorsed by the Eighth Circuit Court of Appeals,[36] as well as by courts within the First Circuit,[37] although the First Circuit Court of Appeals has not formally adopted an analytical framework for applying the

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31. *See* 11 U.S.C.S. § 101 (LexisNexis 2007).

32. 831 F.2d 395 (2d Cir. 1987) (per curiam).

33. *Id.* at 396.

34. *See* Educ. Credit Mgmt. Corp. v. Frushour (*In re* Frushour), 433 F.3d 393, 400 (4th Cir. 2005); Oyler v. Educ. Credit Mgmt. Corp. (*In re* Oyler), 397 F.3d 382, 385 (6th Cir. 2005); Educ. Credit Mgmt. Corp. v. Polleys, 356 F.3d 1302, 1309 (10th Cir. 2004); U.S. Dep't of Educ. v. Gerhardt (*In re* Gerhardt), 348 F.3d 89, 91 (5th Cir. 2003); Hemar Ins. Corp. of Am. v. Cox (*In re* Cox), 338 F.3d 1238, 1241 (11th Cir. 2003); United Student Aid Funds, Inc. v. Pena (*In re* Pena), 155 F.3d 1108, 1112 (9th Cir. 1998); Pa. Higher Educ. Assistance Agency v. Faish (*In re* Faish), 72 F.3d 298, 306 (3d Cir. 1995); *In re* Roberson, 999 F.2d 1132, 1135 (7th Cir. 1993).

35. Andresen v. Neb. Student Loan Program, Inc. (*In re* Andresen), 232 B.R. 127, 139 (B.A.P. 8th Cir. 1999).

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

37. *See, e.g.,* Brunell v. Citibank (S.D.), N.A. (*In re* Brunell), 356 B.R. 567, 575-76 (Bankr. D. Mass. 2006); Lamanna v. EFS Servs., Inc. (*In re* Lamanna), 285 B.R. 347, 353 (Bankr. D.R.I. 2002); Kopf v. U.S. Dep't of Educ. (*In re* Kopf), 245 B.R. 731, 741 (Bankr. D. Me. 2000).

undue hardship standard.[38] Courts have made a debtor's health a relevant factor under both approaches, and this bears further examination given that the overwhelming majority of courts in the discharge determinations analyzed in this Article implemented one of these two approaches, with 70% applying the *Brunner* test and 21% applying the totality test.[39]

Under the second prong of the *Brunner* test, a debtor must establish that *additional circumstances* exist indicating that the debtor's inability to maintain a minimal standard of living will persist for a significant portion of the repayment period of the educational debt.[40] Courts that have applied the test have considered a debtor's illness to be one type of additional circumstance that would support a finding of a future inability to repay.[41] Similarly, under the totality test, courts have considered a debtor's illness as one of several relevant factors in assessing undue hardship.[42] Some have done so under the first prong of the test, which examines the debtor's past, present, and reasonably reliable future financial resources.[43] Others have done so pursuant to the third prong of the test, which examines any other relevant facts and circumstances surrounding the debtor's case.[44]

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38. *See* Nash v. Conn. Student Loan Found. (*In re* Nash), 446 F.3d 188, 190 (1st Cir. 2006) ("We see no need in this case to pronounce our views of a preferred method of identifying a case of 'undue hardship.' "). Neither has the Bankruptcy Appellate Panel for the First Circuit formally adopted the "totality of the circumstances" test. *See* Smith v. Educ. Credit Mgmt. Corp. (*In re* Smith), 328 B.R. 605, 611 (B.A.P. 1st Cir. 2005).

39. It should be noted that neither test proved to be more forgiving than the other for the discharge determinations analyzed in this Article. Approximately half of the debtors whose undue hardship claim was analyzed pursuant to the *Brunner* test received a discharge, whereas approximately 44% of the debtors whose undue hardship claim was analyzed pursuant to the totality test received a discharge. This difference is not statistically significant.

40. *See supra* note 33 and accompanying text.

41. *See, e.g.,* Oyler v. Educ. Credit Mgmt. Corp. (*In re* Oyler), 397 F.3d 382, 385-86 (6th Cir. 2005); Triplett v. ACS/PNC Educ. Loan Ctr. (*In re* Triplett), 357 B.R. 739, 743 (Bankr. E.D. Va. 2006); Simmons v. U.S. Dep't of Educ. (*In re* Simmons), No. 06-3012, 2006 WL 2556581, at *2 (Bankr. C.D. Ill. Aug. 31, 2006); Clark v. U.S. Dep't of Educ. (*In re* Clark), 341 B.R. 238, 253 (Bankr. N.D. Ill. 2006); Mosley v. Gen. Revenue Corp. (*In re* Mosley), 330 B.R. 832, 842 (Bankr. N.D. Ga. 2005); Lowe v. Educ. Credit Mgmt. Corp. (*In re* Lowe), 321 B.R. 852, 859 (Bankr. N.D. Ohio 2004); Folsom v. U.S. Dep't of Educ. (*In re* Folsom), 315 B.R. 161, 165 (Bankr. M.D. Fla. 2004); Hafner v. Sallie Mae Servicing Corp. (*In re* Hafner), 303 B.R. 351, 356 (Bankr. S.D. Ohio 2003); Hoskins v. Educ. Credit Mgmt. Corp. (*In re* Hoskins), 292 B.R. 883, 887 (Bankr. C.D. Ill. 2003); Pace v. Educ. Credit Mgmt. Corp. (*In re* Pace), 288 B.R. 788, 792 (Bankr. S.D. Ohio 2003); Thoms v. Educ. Credit Mgmt. Corp. (*In re* Thoms), 257 B.R. 144, 149 (Bankr. S.D.N.Y. 2001); Jones v. Nat'l Payment Ctr. (*In re* Jones), 242 B.R. 321, 326 (Bankr. E.D. Va. 1998).

42. *See, e.g.,* Anelli v. Sallie Mae Servicing Corp. (*In re* Anelli), 262 B.R. 1, 8 (Bankr. D. Mass. 2000).

43. *See, e.g.,* Limkemann v. U.S. Dep't of Educ. (*In re* Limkemann), 314 B.R. 190, 194-95 (Bankr. N.D. Iowa 2004).

44. *See, e.g.,* Albee v. U.S. Dep't of Educ. (*In re* Albee), 338 B.R. 407, 410-11, 413 (Bankr. W.D. Mo. 2006).

Notwithstanding that a debtor's health is a relevant consideration under current doctrine, should it be so, and, if so, what weight should be afforded to it? Answering whether a debtor's health should be a relevant consideration in the undue hardship inquiry necessarily involves figuring out its relationship to a debtor's ability to repay his or her educational debt. Courts have observed that, since illness can negatively impact a debtor's ability to work, a debtor who suffers from a medical condition may not be well poised to generate sufficient income in the future to repay his or her educational debt.[45] This, however, is only one way in which a medical condition may prevent repayment. Uninsured medical costs have been documented to be one of the leading causes of bankruptcy filings,[46] and, perhaps not surprisingly, many of the opinions in the 2005 study contained references to debtors who could not afford health insurance.[47] In light of these considerations, it seems eminently reasonable to conclude that the status of a debtor's health should play a role in an undue hardship discharge determination. But should it play as central a role as it did in 60% of the doctrine that emerged from bankruptcy courts in the decade spanning 1993 to 2003?

At its core, an undue hardship discharge determination seeks to answer whether the debtor requesting relief will have the ability to repay his or her educational debt without suffering impermissible sacrifice—namely, undue hardship.[48] This, of course, requires a court

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45. *See, e.g.,* Educ. Credit Mgmt. Corp. v. Polleys, 356 F.3d 1302, 1311 (10th Cir. 2004) (noting that "a permanent medical condition will certainly contribute to the unlikelihood of a debtor earning enough money to repay her student loan debt"); *In re Clark*, 341 B.R. at 253 ("[A] strong nexus between the medical condition and its adverse effect on the debtor's employment, specifically the debtor's income, must be demonstrated. If health problems contribute to a debtor's sub-minimal standard of living, then the prospect for recovery and defrayal of medical expenses within the repayment period are relevant." (citation omitted)); *cf. In re Hafner*, 303 B.R. at 356 ("The focus is whether the medical conditions are so serious that a debtor's ability to repay is impaired for the duration of the obligation. . . . What matters is the effect that impairment has upon a debtor's ability to obtain and sustain adequate financial resources in the future.").

46. *See* TERESA A. SULLIVAN, ELIZABETH WARREN & JAY LAWRENCE WESTBROOK, THE FRAGILE MIDDLE CLASS: AMERICANS IN DEBT 141-71 (2000); Melissa B. Jacoby & Elizabeth Warren, *Beyond Hospital Misbehavior: An Alternative Account of Medical-Related Financial Distress*, 100 NW. U. L. REV. 535 (2006); Melissa B. Jacoby, Teresa A. Sullivan & Elizabeth Warren, *Rethinking the Debates over Health Care Financing: Evidence from the Bankruptcy Courts*, 76 N.Y.U. L. REV. 375 (2001).

47. *See* Pardo & Lacey, *supra* note 1, at 448 & n.192. For an example of a court that has recognized that medical costs borne by the debtor may support a claim of undue hardship, albeit under a narrow set of circumstances, see *Wilson v. Missouri Higher Education Loan Authority (In re Wilson)*, 177 B.R. 246, 248 (Bankr. E.D. Va. 1994) (" 'Undue hardship' must mean more than unpleasantness associated with repayment of a just debt. Generally, there must be a showing of exceptional or unique circumstances—e.g., that the debtor must bear the burden of heavy medical expenses *while living at the poverty level* . . . ." (emphasis added)).

48. Put another way, "the undue hardship examination should have as its essential starting point one simple question: Is there a reasonable prospect that the debtor will ever

to predict on the basis of a variety of factors the likelihood that the financial distress suffered by the debtor will persist into the future.[49] As suggested by the 2005 study, very few factual circumstances appeared to be associated with the outcome of discharge determinations.[50] Further statistical analysis has revealed that, of the three most prevalent factors (i.e., the debtor's health status, monthly household income, and monthly household expenses), only a debtor's health status had a statistically significant association with legal outcome.[51] As outlined above, this factor should have an effect on legal outcome,[52] but it should not be the *only* factor that does so.

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be able to repay . . . ?" Mallinckrodt v. Chem. Bank (*In re* Mallinckrodt), 260 B.R. 892, 898 (Bankr. S.D. Fla. 2001), *rev'd*, 274 B.R. 560 (S.D. Fla. 2002).

49. *See* Lieberman v. Educ. Credit Mgmt. Corp. (*In re* Lieberman), Bankr. No. 00-50978, Adv. No. 02-5018, 2003 WL 21397713, at *9 (Bankr. D. Minn. June 3, 2003) ("Simply stated, one must take the debtor in an educational-loan dischargeability proceeding exactly as he presents himself, vocational profile, medical condition, net worth, actual earnings, family responsibilities, and all. Then, one must make a reasonable prognostication as to the debtor's future ability to generate a meaningful income surplus.").

50. *See supra* Part II.

51. *See supra* Part III.

52. It bears mentioning that formal incorporation of a debtor's health status into the analytical framework for analyzing undue hardship may have produced an unintended consequence—namely, making it more difficult for debtors who claim undue hardship on the basis of illness to satisfy their burden of proof. While some courts do not require a debtor to produce expert testimony to corroborate the existence of a medical condition, *see, e.g.,* Hoskins v. Educ. Credit Mgmt. Corp. (*In re* Hoskins), 292 B.R. 883, 887-88 (Bankr. C.D. Ill. 2003); Mayer v. Pa. Higher Educ. Assistance Agency (*In re* Mayer), 198 B.R. 116, 121 n.1 (Bankr. E.D. Pa. 1996), others have intimated that such testimony may be required for a debtor to satisfy his or her burden of proof, *see, e.g.,* Burkhead v. United States (*In re* Burkhead), 304 B.R. 560, 565 (Bankr. D. Mass. 2004) ("Although the Debtor testified about the seriousness of her medical condition and modest living arrangements, she did not call any expert witnesses to testify about her long-term prognosis."); VanderMast v. Educ. Res. Inst. (*In re* VanderMast), Bankr. No. 00-13445-JMD, Adv. No. 01-1074-JMD, 2002 WL 1402535, at *7 (Bankr. D.N.H. June 27, 2002) ("The Debtor did testify about her health problems and her testimony indicates that she expects her health problems to continue into the future. However, the Debtor did not present any evidence from a medical expert regarding the Debtor's prospects of recovery and ability to return to a more normal lifestyle."); Kelsey v. Great Lakes Higher Educ. Corp. (*In re* Kelsey), 287 B.R. 132, 143 (Bankr. D. Vt. 2001) ("[T]his Court closely scrutinizes claims for undue hardship based on psychological or emotional disability due to the susceptibility of such claims to fabrication, exaggeration and fraud. Well qualified and substantiated expert testimony is essential."); *cf.* Craig Peyton Gaumer, *Use Expert Witness Testimony in Student Loan Hardship Discharge Litigation*, AM. BANKR. INST. J., Nov. 2004, at 8 (arguing that the Federal Rules of Evidence require expert testimony to support an undue hardship claim based on medical conditions). Given that debtors who seek an undue hardship discharge are likely to lack the resources necessary to litigate the matter generally, *see* 1 NAT'L BANKR. REV. COMM'N, BANKRUPTCY: THE NEXT TWENTY YEARS 212 (1997) ("It hardly is surprising that some courts see few requests for hardship discharges of educational loans given the pitfalls of the undue hardship standard. The borrowers most likely to prevail in many courts are those with the least possibility of being able to litigate the question. The risk of losing is also high. Failure to meet the burden of proof leaves the debtor with the student loan debts and substantial litigation expenses." (footnote omitted)), courts have recognized the paradox that arises from a rule requiring debtors to present expert testimony, which entails more financial resources, to support an undue hardship claim based on a medical condi-

At bottom, financial characteristics should play a dominant role. The amounts an individual has earned and spent in the past should be probative of ability to repay—at least as much as the health status of that individual, if not more so. In fact, in order to identify those debtors who should not be eligible for Chapter 7 relief because of their ability to repay prebankruptcy debts, Congress has placed emphasis on the predictive power of past financial considerations by creating a means test structured around the concept of "current monthly income,"[53] an amount based on an historical six-month average of the debtor's income.[54] While this is not to say that bankruptcy courts ought to implement a formulaic approach in structuring their inquiry into a debtor's ability to repay pursuant to the undue hardship standard, courts must start applying the standard in such a way that financial criteria have a statistically significant bearing on legal outcome.

One way to do so would be to adopt an approach similar to the statutory presumption of undue hardship that arises in the context of reaffirmation agreements when a debtor's disposable income is less than the scheduled payments on the reaffirmed debt.[55] While it has been argued elsewhere that this presumption should inform the meaning of undue hardship in the educational debt context,[56] that is not the point here. Rather, the suggestion is offered as one way in which uniformity could be brought to the doctrine by focusing on certain financial criteria.[57] If courts were to adopt such an approach, one would expect to witness a statistically significant relationship between a debtor's disposable income and the legal outcome of the discharge determination. The point remains, however, that financial indicia of ability to repay have not been associated with legal outcome, and that is troubling. A closer examination of the financial indicators in the discharge determinations analyzed in this Article reveals how

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tion, *see, e.g.,* Burton v. Educ. Credit Mgmt. Corp. (*In re* Burton), 339 B.R. 856, 877 (Bankr. E.D. Va. 2006) ("Cases that involve debtors that lack the resources to pay experts to testify at trial as to debtors' medical conditions undoubtably [sic] create a paradox."); Doherty v. United Student Aid Funds, Inc. (*In re* Doherty), 219 B.R. 665, 669 (Bankr. W.D.N.Y. 1998) (noting that "dischargeability litigation involves real persons who are *debtors* under the Bankruptcy Code, and cannot afford to hire medical experts to testify to the effect of their disease on their earning capacity"); Sands v. United Student Aid Funds, Inc. (*In re* Sands), 166 B.R. 299, 311 n.22 (Bankr. W.D. Mich. 1994).

53. *See* 11 U.S.C.S. § 707(b)(2)(A)(i) (LexisNexis 2007).

54. *See id.* § 101(10A)(A).

55. *See id.* § 524(m)(1).

56. *See* Pardo & Lacey, *supra* note 1, at 510-14.

57. Another possibility would be for courts to focus on the debtor's income in relation to the federal poverty guidelines, an approach introduced by the U.S. Bankruptcy Court for the Eastern District of Pennsylvania but ultimately rejected by the Third Circuit Court of Appeals. *See id.* at 521 n.447.

bankruptcy courts have failed to sort debtors based on ability to repay.

Since courts have interpreted congressional intent underlying the undue hardship discharge provision to be the prevention of abuse of the bankruptcy system by student loan debtors,[58] it is useful to assess how well bankruptcy courts have performed the sorting function by reference to the statute's perceived purpose. Whether a bankruptcy court effectuates the statute's perceived purpose can be understood as a function of the relationship between (1) the type of debtor (based on repayment ability) making a claim of undue hardship and (2) the outcome of the debtor's discharge determination. Table 1 depicts this relationship.[59]

TABLE 1: THE SORTING FUNCTION OF UNDUE HARDSHIP

	DISCHARGE DETERMINATION OUTCOME	
DEBTOR TYPE	*(A) Discharge Granted*	*(B) Discharge Denied*
(1) Able to Repay	Improper Sorting	Proper Sorting
(2) Unable to Repay	Proper Sorting	Improper Sorting

Assuming that, by establishing the undue hardship threshold, Congress truly sought to prevent abuse of the bankruptcy system by student loan debtors, then only debtors with an ability to repay (Row 1) should be a legitimate target of the undue hardship provision—that is, all such debtors should be denied an undue hardship discharge. Debtors who are unable to repay their educational debt (Row 2) should be beyond the reach of the statute. Accordingly, bankruptcy courts properly execute the sorting function when they deny a discharge to debtors who have an ability to repay (Cell B1) and grant a discharge to debtors who have an inability to repay (Cell A2). Conversely, they improperly execute the sorting function when they grant a discharge to debtors who have an ability to repay (Cell A1) and deny a discharge to debtors who have an inability to repay (Cell B2).

58. It should be noted that the historical record suggests an *absence* of unequivocal intent to this effect. *See id.* at 419-28.

59. This approach is derived from Trujillo, *supra* note 23, at 572-74.

As a thought experiment, let us postulate that a debtor with the following profile would be a prime candidate for being deemed to have an ability to repay his or her educational debt: a debtor (1) with disposable income, (2) whose household generates sufficient income to double the poverty line threshold, and (3) who would have to devote one year's worth or less of household income to repay his or her educational debt in full.[60] Using this profile as a metric of repayment ability, how did bankruptcy courts perform the sorting function in the 172 discharge determinations analyzed in this Article? Table 2 presents the results, listing the actual numbers with the cell percentages in parentheses.

TABLE 2:
SORTING UNDUE HARDSHIP DEBTORS:
A HYPOTHETICAL CONSTRUCT

	DISCHARGE DETERMINATION OUTCOME	
DEBTOR TYPE	*(A) Discharge Granted*	*(B) Discharge Denied*
(1) Able to Repay	2 (1.16)	9 (5.23)
(2) Unable to Repay	80 (46.51)	81 (47.09)

60. The use of financial indicators such as these to predict repayment ability should be accompanied by an inquiry into the amount of time that the repayment obligation has been outstanding. Because the indicators represent a financial snapshot, they may produce a distorted picture. The amount of time that the debtor has had an obligation to repay but failed to do so can help illuminate whether there has been a distortion. This type of evidence allows an assessment of whether the financial indicators are consistent with an historical inability to repay.

The undue hardship opinions in the 2005 study generally did not provide sufficiently detailed information to account for the amount of time that the debtor's repayment obligation had been due and owing. A rough approximation can be obtained, however, by considering the debtor's age in relation to the level of educational attainment. For the 172 discharge determinations analyzed in this Article, 125 determinations (73%) provided sufficiently detailed information to code for the debtor's age and educational attainment. The average age for this subset of debtors was 41.5 years old, and the median age was 41 years old. Since the majority of these debtors (61%) did not obtain a level of education higher than a bachelor's degree, it seems reasonable to conclude that many of the debtors had been in repayment status for quite some time.

It should be noted that, pursuant to the repayment metric defined above, only 6% of the debtors should have been deemed to have an ability to repay, which would mean that the other 94% litigated over a provision that was not intended to apply to them. While it may be argued that this repayment metric defines ability to repay too narrowly, it should be noted that, of the analyzed discharge determinations that reached a legal conclusion regarding a debtor's current ability to repay,[61] 85% concluded that the debtor did not have such an ability.

As Table 1 indicated, the outcomes in Cells A2 and B1 represent proper application of the statute. Accordingly, under this hypothetical construct, courts gave the undue hardship standard its proper reach in slightly more than half of the discharge determinations. On the other hand, approximately 48% of the determinations (Cells A1 and B2) entailed an improper sorting of debtors. Perhaps most striking, all but two of those determinations involved *nonabusive* student loan debtors. For the 81 debtors with an inability to repay who were nonetheless denied a discharge (Cell B2), the average debtor in this group lived in a household that had a monthly *deficit* of $153, a household whose income was only 1.8 times that of the poverty line threshold, and a household that would have had to devote 2.7 years' worth of its income to repay the debtor's educational debt in full.[62] Thus, while courts were effective gatekeepers in preventing abuse of the bankruptcy system, it would appear they cast an overly broad net that captured a significant number of debtors in true need of financial relief.[63]

Perhaps these findings should not be so surprising. Empirical evidence exists that bankruptcy courts have not been successful in predicting a debtor's future repayment ability in a different context—Chapter 13. In Chapter 13, a debtor generally receives a discharge

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61. There were 163 such discharge determinations.

62. The financial characteristics of the average debtor in the discharge group that would be deemed to have an inability to repay based on the postulated repayment metric (Cell A2) are only slightly worse. The average debtor in this group lived in a household with a monthly *deficit* of $222 and with income that was only 1.5 times that of the poverty line threshold. On the other hand, one might conclude that this group was *better off* given that the average debtor's household would have had to devote 2.3 years' worth of its income (i.e., *less* than the nondischarge group) to repay the debtor's educational debt in full.

63. This echoes one of the conclusions of the 2005 study:

> While bankruptcy courts have perceived the Bankruptcy Code's undue hardship provision to have been enacted by Congress as a necessary measure to curb abuse of the bankruptcy system, the data have shown that the statute has proved to be much less selective, primarily because of its inherently overbroad scope. The inevitable result has been a law applied, counter to its purported objective, to a class of individual whose behavior could not have been deemed by Congress to be a legitimate target for legislative reform.

Pardo & Lacey, *supra* note 1, at 479.

after completing a repayment plan pursuant to which a portion of his or her future income has been devoted to repaying the claims of creditors.[64] In order for a debtor's repayment plan to be confirmed, the court must make a finding of financial feasibility, including that "the debtor will be able to make *all* payments under the plan."[65] Thus, all confirmed Chapter 13 plans embody the court's judgment that the debtor's repayment efforts over no longer than a five-year period will succeed.[66]

A recent empirical study of Chapter 13 documented that, of the 613 *confirmed* cases in the study's sample, 351 of those cases were either dismissed or converted to Chapter 7.[67] In other words, bankruptcy courts erroneously determined the financial feasibility of future repayment by the debtor in 57% of the confirmed cases. If bankruptcy courts cannot properly gauge repayment ability in the relatively controlled environment of Chapter 13 where various constituencies with different stakes are given the opportunity to object to plan confirmation,[68] where the repayment plan may be modified after confirmation in response to changed circumstances,[69] and where the repayment period will not exceed five years, then why should they fare any better in undue hardship discharge determinations that require them to forecast repayment ability over a period that can be as long as thirty years?

For a judge, there may be an intuitive appeal to focus on a debtor's health in assessing repayment ability insofar as it may be easier to validate internally the prediction of inability to repay. We have all witnessed someone who has suffered from a medical condition and the manner in which it can interfere with everyday living. But courts should be cautious not to rely too much on a debtor's health as a proxy for repayment ability. As illustrated above, reference to a debtor's medical condition as part of the undue hardship inquiry may result in the improper sorting of debtors. Moreover, a debtor's health as the major determinant of a finding of undue hardship raises serious concerns about judicial activism. While no court has announced a per se rule that suffering from a medical condition constitutes undue hardship, the legal doctrine studied in this Article approaches this decision standard. Were courts to adopt such an outcome-determinative rule, it would impermissibly encroach into the

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64. *See* 11 U.S.C.S. § 1328(a) (LexisNexis 2007).

65. 11 U.S.C. § 1325(a)(6) (2000) (emphasis added).

66. *See* 11 U.S.C.S. § 1322(d).

67. *See* Scott F. Norberg & Andrew J. Velkey, *Debtor Discharge and Creditor Repayment in Chapter 13*, 39 CREIGHTON L. REV. 473, 506 tbl.19 (2006).

68. *See* 11 U.S.C. § 1325(b)(1) (granting trustee and unsecured creditors standing to object to Chapter 13 plan).

69. *See* 11 U.S.C.S. § 1329(a).

legislative sphere by creating a categorical class of debtor entitled to an undue hardship discharge.[70] Lest bankruptcy courts exceed the scope of their judicial power, it is imperative that other determinants give content to the meaning of undue hardship.

V. CONCLUSION

Bankruptcy courts have been assigned the unenviable task of predicting the future suffering of individuals who seek relief from their educational debt. One, and only one, factual circumstance has emerged in a great deal of bankruptcy court doctrine as the major determinant of the legal outcome in undue hardship discharge proceedings—a debtor's health status. As a result of this focus, the doctrine has lost its mooring to the essential question sought to be answered in such determinations: "Will repayment of the educational debt impose an undue hardship on the debtor?" If past evidence has demonstrated that a debtor has been subject to financial distress at the time he or she makes a claim for relief, absent positive evidence that the debtor's situation will improve, it seems sensible to conclude that the debtor's financial situation will persist if relief is not granted. Notwithstanding the inevitable coordination problem faced by bankruptcy courts that operate in distinct judicial districts and circuits, the bankruptcy system ought to strive to bring a measure of consis-

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70. One need look no further than the Supreme Court's recent decisions on equitable subordination in support of this conclusion. In *United States v. Noland*, 517 U.S. 535 (1996), and *United States v. Reorganized CF&I Fabricators of Utah, Inc.*, 518 U.S. 213 (1996), the Supreme Court reviewed two separate bankruptcy court decisions that equitably subordinated certain IRS tax penalty claims to the claims of general unsecured creditors, merely on the basis of the nature of the IRS's claims and not with regard to the individual circumstances of the case. As I have commented previously:

> Both cases stand for the proposition that a bankruptcy court may not subordinate categorically whole classes of claims and thereby transgress the line distinguishing adjudication from legislation. The decisions reflect the Supreme Court's concern that any categorical subordination of claims would exceed the constitutional limits on judicial power and encroach upon Congress's Article I powers.

Rafael Ignacio Pardo, Note, *Beyond the Limits of Equity Jurisprudence: No-Fault Equitable Subordination*, 75 N.Y.U. L. REV. 1489, 1494-95 (2000) (footnote omitted). There is every reason to believe that the Supreme Court would view the creation of a categorical class of debtors entitled to discharge under the undue hardship standard to be equally impermissible as the categorical subordination of IRS tax penalty claims under the Code's equitable subordination provision.

Interestingly, a strand of undue hardship discharge doctrine holds (for all intents and purposes) that a debtor's failure to participate in one of the federal government's repayment plans, such as the income contingent repayment plan, will preclude a finding of undue hardship. *See* Terrence L. Michael & Janie M. Phelps, "*Judges?!—We Don't Need No Stinking Judges!!!": The Discharge of Student Loans in Bankruptcy Cases and the Income Contingent Repayment Plan*, 38 TEX. TECH L. REV. 73, 92-94 (2005). A decision standard such as this would also run afoul of the principles set forth in *Noland* and *Reorganized CF&I Fabricators*.

tency to the undue hardship doctrine by rooting it in financial predictors of ability to repay.

APPENDIX

BINARY LOGISTIC REGRESSION MODEL OF UNDUE HARDSHIP DISCHARGE

VARIABLE	Discharge
Monthly Household Income	0.9995 (0.9990, 1.0000)
Monthly Household Expenses	1.0003 (0.9998, 1.0009)
Debtor Health Status**	2.3961 (1.2691, 4.5240)
Observations	172
Log likelihood	-113.313
McFadden's R^2	0.0481

Note: ***$p < 0.001$, ** $p < 0.01$, * $p < 0.05$. Odds ratios presented with 95% confidence interval in parentheses. The dependent variable is whether the court granted the debtor a discharge, whether in full or in part, with denial of discharge coded 0 and grant of discharge coded 1. The third independent variable ("Debtor Health Status") tracks whether the debtor suffered from either a physical or mental condition (or both), with a healthy debtor coded 0 and an unhealthy debtor coded 1.