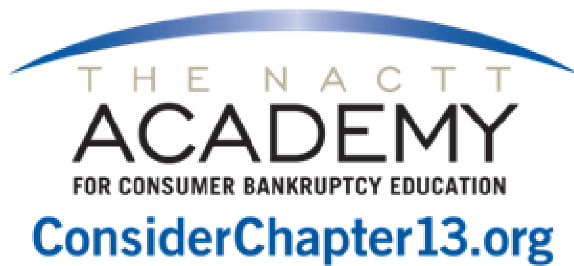

NACTT 51st Annual Seminar

Philadelphia, PA

Educational Materials for General Attendees

Friday, July 22

AGENDA

Friday, July 22

8:45 - 10:00 **What Does the CFPB Have to Do with Bankruptcy?**
Moderator: Kathleen A. Leavitt, Chapter 13 Standing Trustee for the District of Nevada (Las Vegas)
Alane A. Becket, Becket & Lee LLP (Malvern, PA)
John J. Franchini, Executive Director, JPMorgan Chase (Philadelphia, PA)
Joann Needleman, Clark Hill PLC (Philadelphia, PA)
Barbara A. Sinsley, Barron & Newburger, P.C. (Spartanburg, SC)

10:30 - 11:30 **Provisions for Student Loan Debt**: How to incorporate into the plan remedies available outside of bankruptcy.
Moderator: D. Sims Crawford, NACTT President-Elect and Chapter 13 Standing Trustee for the Northern District of Alabama, Southern Division (Birmingham)
Edward C. Boltz, The Law Offices of John T. Orcutt (Durham, NC)

11:35 - 12:35 **Life After the National Mortgage Settlement**: Mortgage and secured claims issues.
Moderator: William Mark Bonney, Chapter 13 Standing Trustee for the Eastern District of Oklahoma (Muskogee)
Michael T. Bates, Linquist and Vennum, LLP (Minneapolis, MN)
John Rao, National Consumer Law Center (Boston, MA)

INDEX OF MATERIALS BY PANEL

8:45 - 10:00 **What Does the CFPB Have to Do With Bankruptcy?**

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INDEX OF MATERIALS

1. **Overview of Consumer Financial Protection Bureau Enforcement Activity**
   a. CFPB Overview
   b. CFPB Enforcement
   c. CFPB Regulatory Agenda
   d. Mortgage Servicing and Bankruptcy
   e. Consent Orders
   f. Practice of Law Exemptions
   g. CFPB and Chapter 13 Trustees
2. **PDF of PowerPoint Presentation**
3. **Speaker Biographies**

OVERVIEW OF
CONSUMER FINANCIAL PROTECTION BUREAU
ENFORCEMENT ACTIVITY

PLENARY PANEL

NACTT ANNUAL SEMINAR
Philadelphia, PA
July 22, 2016
8:45 a.m. – 10:00 a.m.

I. CFPB Overview
   A. Structure
      1. Under the Director
         a. Consumer education and engagement
            i. Engagement
            ii. Financial education
            iii. Financial empowerment
            iv. Older Americans
            v. Service member affairs
         b. Research, markets and regulations
            i. Card markets
            ii. Deposits, liquidity, lending and reporting markets
            iii. Installment lending and collections markets
            iv. Mortgage markets
            v. Regulations
            vi. Research
         c. Supervision, enforcement and fair lending
            i. Enforcement
            ii. Fair lending and equal opportunity
            iii. Office of Supervision Examinations
            iv. Office of Supervision Policy
      2. Mandates
         a. Conduct financial education programs
         b. Collect, investigate and respond to consumer complaints
         c. Collect, research, monitor and publish information that is relevant to the functioning of markets for consumer financial products and services in order to identify risks to consumers and to the proper functioning of those markets
         d. Supervise covered persons within the CFPB’s authority for compliance with federal consumer financial laws;
         e. Take appropriate enforcement action to address violations of federal consumer financial law
      3. Authority to supervise
         a. Authorization to supervise, examine and take enforcement action against other “covered persons”

i. “Covered persons” generally defined as any entity providing consumer financial products or services, and their affiliated service providers
ii. Can require cooperation from smaller banks and credit unions

4. Supervised Entities
   a. Residential mortgage originator, broker or servicer
   b. Private student lenders
   c. Payday lenders
   d. “Larger Market participants (as defined by the CFPB
   e. Very large banks, savings associations and credit unions with assets exceeding $10 billion
   f. Service providers
      i. Any person that provides a material service to a covered person in connection with the offering or provision by such covered person of a consumer financial product or service
      ii. Any “service provider” representing a “substantial number” of smaller entities
5. Rulemaking
   a. The CFPB’s director may:
      i. “Prescribe rules and issue orders and guidance as may be necessary or appropriate to enable the Bureau to administer and carry out the purposes and objectives of the Federal consumer financial laws, and to prevent evasions thereof.”
      ii. Issue regulations under Federal consumer protection statutes, including the Fair Debt Collection Practices Act (FDCPA), Fair Credit Reporting Act, Equal Credit Opportunity Act, Home Ownership and Equity Protection Act, Real Estate Settlement Procedures Act (RESPA) and Truth in Lending Act (TILA), among others
      iii. Take any action ... to prevent a covered person or service provider from committing or engaging in an unfair, deceptive, or *abusive* act or practice [UDAAP] under Federal law in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial service
      iv. “Abusive” defined: Materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service; or takes unreasonable advantage of a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service; the inability of the consumer to protect the interests of the consumer in selecting or using a consumer financial product or service; or the reasonable reliance by the consumer on a covered person
6. Implementation of Authority
   a. Issuing civil investigation demands when it suspects has violation has occurred;
   b. Directing examinations of supervised entities, either on-site or by deposition; or
   c. Enforcement actions and consent orders
   d. Bulletins, white papers, research and examination manuals
7. Conduct addressed

a. Collection practices
b. Credit card add on fees
c. Lending discrimination
d. TILA violations
e. EFT violations
f. FCRA violations
g. Military collection violations
h. Background check requirements
i. Deposit account violations
j. Mortgage servicing
k. Student loan servicing
l. Mortgage origination
m. Land development
n. Violations in connection with ID Theft Services
o. Mortgage insurance kickbacks

II. CFPB Enforcement
  A. Historical background
    1. Enforcement actions commenced in 2012
    2. 85 actions since April 1, 2016 have resulted in consent orders
    3. Pending matters being litigated
    4. No market is immune
  B. Debt collection
    1. Oversight of 3rd party Vendors, including attorneys
      a. PRA/Encore Consent Orders
        i. Dictates what appropriate substantiation is
        ii. Knowledge of affidavit process
        iii. Buyers aware of inaccuracies in accounts they were purchasing
        iv. Collection Lawsuits
    2. Improper Debt Sales
      a. Chase Consent Order
        i. Accounts sold to debt buyers – inaccurate information
        ii. Improper interest rates
        iii. Fault affidavits
    3. Credit Reporting
    4. a. Syndicated Office Solutions (medical debts)
        i. Mishandling of disputes and credit reporting
        ii. Did not investigate within 30 days
        iii. Failed to send validation notices
    5. Overall UDAAP
    6. No debt collection rules have been promulgated to date
      a. Westlake Services - Debt collection practices
      a. i. Used service to contact consumers
      b. ii. Misrepresented who call was from
      c. iii. Disclosures made to 3rd parties
      d. iv. UDAAP found because Westlake was the original creditor
  C. Mortgage servicers / brokers / payment processors

1. Failure to abide by prior loan modifications
2. Improper incentives and compensation for referral of mortgage applications
3. Marketing of equity accelerator programs
4. Process shared consumer fees
5. Mortgage servicing rules have been promulgated but these consent orders are not the result of failure to comply
    a. Residential Credit Solutions
        i. Unfair practices – not honoring in-process loan modifications from prior servicers
        ii. Misrepresentations regarding payment obligations
        iii. Misrepresented that refund for escrow surplus would be received in 30 days
        iv. Required consumer to waive foreclosure defenses
    b. Loan Care/Pay Map
        i. Equity Accelerator partnered with payment processor
        ii. Pay Map was receiving fees on transactions that were not made as advertised
        iii. Customers say, "no savings"

D. Student loan servicing
1. Debt collection practices
2. Improper billing practices
3. Misleading information about charges incurred
4. Misapplication of payments to interest and not principal
5. No rules promulgated

6. Discover – servicer for Citibank student loan accounts
    a. Overstated minimum amounts due on billing statements
    b. Illegal debt collection practices
        i. Calling at improper times
        ii. Failure to send validation notices
8. Student Financial Aid Services
    a. Misleading information about the total cost of its subscription financial services
    b. Charged undisclosed and unauthorized automatic recurring charges
        i. Violations of Electronic Transfer Fund Act.

III. CFPB Regulatory Agenda

A. Arbitration
1. Benefit
    a. Confidentiality
2. Proposals under consideration
    a. Ban the application of pre-dispute arbitration agreements in class actions
    b. Require submission to the bureau of all arbitral disputes and awards for review and possible
    publication

B. Bankruptcy and Debt Collection
1. Fall 2015 CFPB Agenda
    a. The Bureau is also conducting research for rulemaking on debt collection activities, which are the single largest source of complaints to the federal Government of any industry."
2. Currently – 2015 and 2016

a. Consent Orders set the tone
i. PRAA and Encore – debt collection and lawsuits
ii. HANNA (Frederick Hanna & Assoc.) – lawsuits
iii. Citibank – debt sales
3. Bankruptcy
a. Stale claims
b. Filing claims as debt collection
C. Other areas under review
1. Prepaid cards
a. March 1, 2016 – Richard Cordray
i. "Prepaid products provide a crucial financial lifeline to many unbanked and under-banked households"
ii. "It is important that consumers who rely on this important financial product can do so safely and efficiently, without undue hassles and runarounds
2. Technology / security / marketing
a. March 2, 2016 – Dwolla and more?
i. Online payment platform Dwolla for *deceiving consumers about its data* security *practices and the safety of its online payment system.*
ii. The CFPB ordered Dwolla to pay a $100,000 penalty and fix its security practices
3. Mortgage servicing and mortgage originations
a. March 22, 2016 - Origination
i. "Consumer Financial Protections Bureau rule broadens qualified mortgage coverage of lenders operating in rural and underserved areas."
ii. Other types of consumers?
iii. Post bankruptcy?
b. Servicing
i. More loss mitigation options?
ii. More information to bankruptcy consumers?

4. Banking and overdraft fees / prepaid cards
a. April 28, 2016 - CFPB Fines Regions Bank $7.5 Million for Unlawful Overdraft Practices- *Bank Refunds $49 Million in Illegal Fees to Consumers Who Did Not Opt-In to Overdraft Fees*
b. Richard Cordray
i. ""Regions Bank failed to ask consumers if they wanted overdraft service before charging them fees. In the end, hundreds of thousands of consumers paid at least $49 million in illegal charges. We take the issue of overdraft fees very seriously and will be vigilant about making sure that consumers receive the protections they deserve."

IV. Mortgage servicing and bankruptcy
A. 2013 Amendments to the Mortgage Rules under the Real Estate Settlement Procedures Act (Regulation X) and the Truth in Lending Act (Regulation Z)
1. Clarifies compliance requirements in relation to bankruptcy and the Fair Debt Collection Practices Act (FDCPA)
a. Servicers needed guidance on how to communicate with consumers (live contact)

i. Bankruptcy trustees expressed concerned about consumers being confused by
communication during bankruptcy

ii. Servicers expressed concern about how to fulfill servicing requirements without
violating the law

2. Bankruptcy Exemptions
   a. §1024.39(d)(1) – Servicers exempt from loss mitigations when debtor is in bankruptcy
   b. §1026.41(e)(5) – Exempts a servicer from the periodic statement requirements
   in §1026.41 for a mortgage loan while a consumer is a debtor in bankruptcy

B. 2014 Amendments to the Mortgage Rules under the Real Estate Settlement Procedures Act (Regulation X) and the Truth in Lending Act (Regulation Z)
   1. Early intervention/live contact
      a. Must comply with live contact requirement for a non-debtor with someone in a Chapter 7 or 11
      b. Exempt from live contact with a debtor in Chapter 12 or 13
   2. Early written intervention notice requirements for all debtors in bankruptcy unless:
      a. No loss mitigation requirements are available
      b. Plan provides for surrender of property or avoidance of lien, or no provision for
      payment of pre-bankruptcy arrears or maintenance due under the loan
      c. Statement of intent to surrender property; or
      d. Order to avoid lien or lift stay entered

C. HSBC Settlement
   1. Parties involved in settlement agreement
      a. Department of Justice
      b. CFPB
      c. HUD
      d. All 50 Attorneys General
   2. Improper conduct involved
      a. Mortgage servicing
         i. Failing to timely and accurately apply payments made by borrowers
         ii. Failing to maintain accurate account statements
         iii. Charging unauthorized fees for default-related services
         iv. Imposing force-places insurance when Defendants knew or should have known that borrowers already had adequate coverage; and
         v. Providing false or misleading information in response to borrower complaints
      b. Loss mitigation

i. Failing to establish adequate processes for loan modifications (lack of training and adequate staff)
ii. Wrongfully denying loan modifications
iii. Providing false or misleading information to consumers about the status of loss mitigation review, including while referring loans to foreclosure

c. Foreclosure
i. Filing false or misleading documents with the Courts
ii. Preparing affidavits with no personal knowledge (robo-signing)
iii. Charging inappropriate fees
iv. Dual tracking foreclosure and loss mitigation

d. Bankruptcy related activity
i. Lack of oversight and supervision over bankruptcy attorneys (local counsel)
ii. Pleadings signed without reasonable inquiry into allegations (Proofs of claim, relief from stay, etc.)
iii. Failure to apply payment made post petition and failing to advise the trustee of
payments made

2. Indeterminate whether misconduct occurred before or after servicing rules were promulgated

V. Consent Orders

A. Regulation by consent
B. Consistency with Trustee Expectations
C. Intersection with developing law
D. Operational issues
E. Collaboratively moving forward together

VI. Practice of Law Exemptions

A. 12 U.S. Code § 5117 – Limitations on authorities of the Bureau

1. 12 U.S. Code § 5117 (e) Exclusion for Practice of Law

(1) In General. Except as provided under paragraph (2), the Bureau may not exercise any supervisory or enforcement authority with response to an activity engaged in by an attorney as part of the practice of law under the laws of a State in which the attorney is licensed to practice law.
(2) Rule of Construction. –Paragraph (1) shall not be construed so as to limit the exercise by the Bureau of any supervisory, enforcement, or other authority regarding the offering or provision of a consumer financial product or service described in any subparagraph of section 5481(5) of this title—

(A) that is not offered or provided as part of, or incidental to, the practice of law, occurring exclusively within the scope of the attorney-client relationship; or

(B) that is otherwise offered or provided by the attorney in question with respect to any consumer who is not receiving legal advice or services from the attorney in connection with such financial product or service.

(3) Existing authority. Paragraph (1) shall not be construed so as to limit the authority of the Bureau with respect to any attorney, to the extent that such attorney is otherwise subject to any of the enumerated consumer laws or the authorities transferred under subtitle F or H.

B. CFPB v. Frederick Hanna & Assocs. PC
   1. Lack of meaningful involvement in suit
   2. Improper client affidavits
C. CFPB v. The Mortgage Law Group, et al.
   1. Charging illegal up-front fees for mortgage modifications
   2. Deceptive marketing of services

VII. CFPB and Chapter 13 Trustees

A. Proofs of Claim on Time Barred Debt
   1. Filing proofs of claim for stale debt does not violate the FDCPA
      a. Only three states (Mississippi, Wisconsin, and North Carolina) forbid normal collection activity after the passage of the statute of limitations. The right and the remedy expire in these states only.
      b. State law determination of statute of limitations
      c. The Federal Trade Commission agree in Policy Statements
      d. The CFPB only wants disclosures on time barred debts
   2. Filing proofs of claim for stale debt complies with Rule 9011
      a. Fed. R. Bankr. P. 3001, Advisory Committee Notes, 2011 Amendment II
         i. "Disclosure of the information require by Paragraph (3) will…provide a basis for assessing the timeliness of the claim."
         ii. FRBP 3001(c)(3) *Claim Based on an Open-End or Revolving Consumer Credit Agreement*
      b. Advisory Committee Minutes, March 1-2, 2009 at 25
         i. Suggestion to add statute of limitations date was rejected
      c. Considerations on requiring creditors to state whether a statute of limitations defense is applicable – NOT ADOPTED:
         i. It would shift the burden of proof on the matter; and
         ii. Members thought that there were "too many factors involved in a statutes of limitations defense to affirmatively certify whether it is applicable."
   3. Case law re: Proof of Claim on time barred debt. The majority of courts to address these issues agree.
      a. Crawford v. LVNC Funding, LLC, 758 F. 3d. 1254, 1261 (11th Cir. 2014) Creditor violated the Fair Debt Collection Practices Act ("FDCPA") by filing a proof of claim to collect a debt that was unenforceable because the statute of limitations had expired.
      b. *Glenn v. Cavalry Investments LLC*, 2016 WL 55672, at *12 (Bankr. N.D. Ill. Jan. 5, 2016) (where a creditor has complied with the Bankruptcy

Rules, the "mere filing of a proof of claim on a time-barred claim" does not violate Rule 9011 or the FDCPA).

c. *Martel v. LVNV Funding*, 2015 WL 5984890 (Bankr. D. Me. Oct. 13, 2015) ("The fact that the debts were subject to the affirmative defense of the statute of limitation does not make filing the proofs of claim violative of the FDCPA, the Maine FDCPA or the Code. Statutes of limitation do not extinguish debts, but bar actions to collect once raised.").

d. *Johnson v. Midland Funding, LLC*, 528 B.R. 462, 467-68 & n.15 (S.D. Ala. 2015) (claim for time-barred debt is a legally enforceable right to payment and therefore permitted under Bankruptcy Code) *appeal docketed*, No. 15-11240 (11th Cir.).

e. *In re Freeman*, 540 B.R. 129, 143 (Bankr. E.D. Pa. 2015) (filing stale-debt claim "fits none of the examples of improper purpose stated in [Rule 9011] … Nor does the filing of a stale proof of claim appear to satisfy the more general type of improper purpose").

f. *In re Jenkins*, 538 B.R. 129, 135 (Bankr. N.D. Ala. 2015) ("the filing of a claim on a debt that is stale under state law—where the proof of claim is otherwise in all material respects compliant—is not egregious and offensive conduct that Rule 9011 was intended to address").

g. *United States v. Moriarty*, 8 F.3d 329, 334 (6th Cir. 1993) (a creditor has a "'claim,' against the debtor even though the [creditor] is barred by the statute of limitations from bringing an action against the debtor for money damages").

B. Chapter 13 Trustees

1. Does the Trustee provide a financial product or related service to a financial product?
   a. See CFPB v. Morgan Drexen, Inc.- March, 2016.
      i. Debt settlement attorneys firm
      ii. Illegally charged upfront fee to consumers claiming it could settle their debt
      iii. Court ordered the now-defunct firm to pay $173 million in fines and restitution
   c. See CFPB v. Mortgage Law Group, LLP
      i. Foreclosure assistance
      ii. Attorney exemption
2. Collection attorneys are "supervised entities"
   a. Practicing law exclusion in Dodd-Frank
      i. Filing suit is "incidental to the practice of law"
   b. CFPB is creating a new class of attorneys
      i. Clients are not afforded First Amendment or Equal Protection
   c. Streamlining and automation of clerical/non-legal tasks
      i. Not "unauthorized practice of law"
      ii. In the best interest of attorney's clients

OVERVIEW OF CFPB ENFORCEMENT ACTIVITY

NACTT 2016
Philadelphia, PA

Alane A. Becket, Becket & Lee LLP
Joann Needleman, Clark Hill PLLC
Barbara A. Sinsley, Sr. VP, Resurgent Capital
John Franchini, VP, JP Morgan Chase

Disclaimer

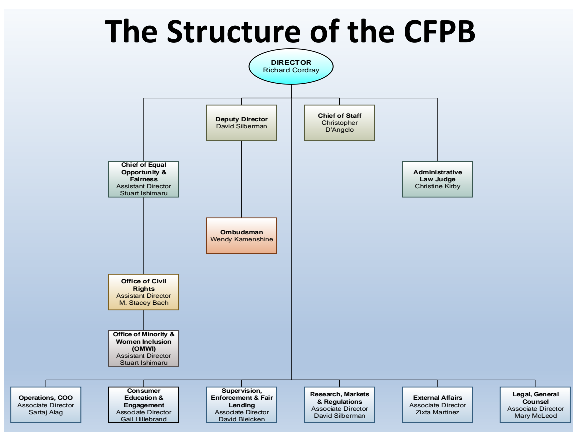
This information is not intended to be legal advice and may not be used as legal advice. Legal advice must be tailored to the specific circumstances of each case. Every effort has been made to assure this information is up-to-date. It is not intended to be a full and exhaustive explanation of the law in any area. It should not be used to replace the advice of your own legal counsel.

CFPB Overview

2010: Dodd-Frank Act created the Bureau of Consumer Financial Protection (CFPB)

- To implement and, where applicable, enforce Federal consumer financial law consistently for the purpose of ensuring that all consumers have access to markets for consumer financial products and services
- To ensure consumer financial products and services are fair, transparent, and competitive
- Ensures that consumers "are provided with timely and understandable information to make responsible decisions about financial transactions" and "are protected from unfair, deceptive, or abusive acts and practices and from discrimination."

The Structure of the CFPB



Under the Director

- Consumer Education and Engagement
- Research, Markets and Regulations
- Supervision, enforcement and fair lending

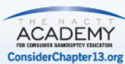
Mandates

- Conduct financial education programs;
- Collect, investigate, respond to consumer complaints;
- Collect, research, monitor, publish information relevant to the functioning of markets for consumer financial products and services
- Identify risks to consumers and to the proper functioning of those markets;
- Supervise covered persons within the CFPB's authority for compliance with federal consumer financial laws;
- Take appropriate enforcement action to address violations of federal consumer financial law

Authority

- Authorization to supervise, examine and take enforcement action against other "covered persons," generally defined as any entity providing consumer financial products or services, and their affiliated service providers.

Supervised Entities



- Any residential mortgage originator, broker or servicer
- Private student lenders
- Payday lenders
- "Larger market participants" (as defined by the CFPB)
- Very large banks, savings associations, and credit unions: those with assets exceeding $10 billion
- Can require cooperation from smaller banks and credit unions

- **Service Providers:**
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  - Any "service provider" representing a "substantial number" of smaller entities

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The CFPB's Director May:

- **Prescribe rules and issue orders and guidance** as "may be necessary or appropriate to enable the Bureau to administer and carry out the purposes and objectives of the Federal consumer financial laws, and to prevent evasions thereof."
- **Issue regulations** under Federal consumer protection statutes, including
  - Fair Debt Collection Practices Act (FDCPA)
  - Fair Credit Reporting Act, Equal Credit Opportunity Act, Home Ownership and Equity Protection Act, Real Estate Settlement Procedures Act (RESPA) and
  - Truth in Lending Act (TILA), among others

UDAAP Protection

The CFPB: May take any action . . . to prevent a covered person or service provider from committing or engaging in an "unfair, deceptive, or ***abusive*** act or practice" [UDAAP]

"Abusive"

- Materially interferes with ability of consumer to understand a term or condition of a consumer financial product or service; *or*
- Takes unreasonable advantage of —
  - a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service;
  - inability of the consumer to protect the interests of the consumer in selecting or using a consumer financial product or service; or
  - the reasonable reliance by the consumer on a covered person

Implementation of Authority

- Issuing civil investigation demands
- Directing examinations of supervised entities
- Enforcement actions and consent orders
- Bulletins, white papers, research and examination manuals

Conduct Addressed

- Collection practices
- Credit card add on fees
- Lending discrimination
- TILA violations
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- Military collection violations
- Background check requirements
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- Mortgage servicing
- Student loan servicing
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- Mortgage insurance kickbacks

CFPB Enforcement Activity

Historical Background

- Enforcement actions commenced in 2012
- 85 actions since April 1, 2016 have resulted in consent orders
- Pending matters being litigated
- No market is immune

Debt Collection Enforcement

- Oversight of 3rd party vendors, including attorneys
  - PRA/Encore consent orders
- Improper debt sales
  - Chase consent order
- Credit Reporting
  - Syndicated Office Solutions
- UDAAP
- Debt Collection
  - Westlake Services

Mortgage Servicing - Mortgage Brokers Payment Processors

- Failure to abide by prior loan modifications
- Improper incentives and compensation for referral of mortgage applications
- Marketing of equity accelerator programs—processor shared consumer fees with servicer
- Mortgage servicing rules have been promulgated but these consent orders are not the result of a failure to comply
  - Residential Credit Solutions
  - Loan Care/Pay Map

Student Loan Servicing

- Debt collection practices
- Improper billing practices
- Misleading information about charges incurred
- Misapplication of payments to interest and not principal.
- No rules promulgated

Discover

- Servicer for Citibank student loan accounts
- Overstated minimum amounts due on billing statements
- Illegal debt collection practices (calling at improper times, failure to send validation notices)

Student Financial Aid Services

- Misleading information about the total cost of its subscription financial services
- Charged undisclosed and unauthorized automatic recurring charges (violations of Electronic Transfer Fund Act)

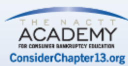
CFPB Regulatory Agenda

Categories of Products on Current Regulatory Agenda

- Arbitration
- Payday lending and installment loans
- Bankruptcy and Debt Collection
- Others

Other Areas Under Review

- Prepaid cards
- Technology/security/marketing
- Mortgage Servicing and Mortgage Originations
- Banking and overdraft fees/prepaid cards



Mortgage Servicing & Bankruptcy

Amendments to Mortgage Rules – Oct 2013 Bankruptcy & FDCPA Addressed

- Clarifies compliance requirements in relation to bankruptcy law and the FDCPA
  - Servicing requirements
  - Consumer confused by communication during bankruptcy
- Bankruptcy Exemptions
  - §1024.39(d)(1) - Servicers exempt from loss mitigations when debtor in bankruptcy
  - §1026.41(e)(5) - exempting a servicer from the periodic statement requirements in § 1026.41 for a mortgage loan while the consumer is a debtor in bankruptcy

2014 Amendments to Mortgage Rules Bankruptcy & FDCPA Addressed

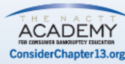
- Early Intervention/Live Contact required
- Early written intervention notice requirements for all debtors in bankruptcy unless:
  - no loss mitigation requirements available
  - plan provides for surrender of property or avoidance of lien, or no provision for payment of pre-bankruptcy arrears or maintenance due under the loan
  - statement of intent to surrender property; or -
  - order to avoid lien or lift stay entered

HSBC Settlement

- DOJ/CFPB/HUD and all 50 Attorneys General
- Servicing violations
- Loan Modification / Loss Mitigation violations
- Foreclosure misconduct
- Bankruptcy related misconduct

Consent Orders

- Regulation by consent
- Consistency with Trustee Expectations
- Intersection with developing law
- Operational issues
- Collaboratively moving forward together



Practice of Law Exclusion

12 U.S. Code § 5517 Limitations on Authorities of the Bureau

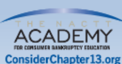
- **(e) Exclusion for practice of law**
  - **(1) In general.** Except as provided under paragraph (2), the Bureau may not exercise any supervisory or enforcement authority with respect to an activity engaged in by an attorney as part of the practice of law under the laws of a State in which the attorney is licensed to practice law.

12 U.S. Code § 5517 Limitations on Authorities of the Bureau

- **(2) Rule of construction**
  - Paragraph (1) shall not be construed so as to limit the exercise by the Bureau of any supervisory, enforcement, or other authority …
    - (A) that is not offered or provided as part of, or incidental to, the practice of law, occurring exclusively within the scope of the attorney-client relationship; or
    - (B) that is otherwise offered or provided by the attorney in question with respect to any consumer who is not receiving legal advice or services from the attorney in connection with such financial product or service.
- **(3) Existing authority**
  - Paragraph (1) shall not be construed so as to limit the authority of the Bureau with respect to any attorney, to the extent that such attorney is otherwise subject to any of the enumerated consumer laws or the authorities transferred under subtitle F or H.

Cases re: Practice of Law Exclusion

- *CFPB v. Frederick Hanna & Assocs. PC*
  - Lack of meaningful involvement in suit
  - Improper client affidavits
- *CFPB v. The Mortgage Law Group, et al.*
  - Charging illegal up front fees for mortgage modifications
  - Deceptive marketing of services



CFPB and Chapter 13 Trustees

Proofs of Claim

- Filing proofs of claim for stale debt does not violate the FDCPA.
  - Only three states (Mississippi, Wisconsin, and North Carolina) forbid normal collection activity after the passage of the statute of limitations. The right and the remedy expire in these states only.
  - EXCEPT! see *Crawford v. LVNC Funding, LLC, 758 F.3d 1254, 1261 (11th Cir. 2014).*
- Filing proofs of claim for stale debt complies with Rule 9011.
  - Fed. R. Bankr. P. 3001, Advisory Committee Notes, 2011 Amendment II
  - Advisory Committee Minutes, March 1-2, 2009, at 25

Case law re: Proof of Claim on Time Barred Debt

The majority of courts to address these issues agree.

- *Glenn v. Cavalry Investments LLC*, 2016 WL 55672, at *12 (Bankr. N.D. Ill. Jan. 5, 2016)
- *Martel v. LVNV Funding*, 2015 WL 5984890 (Bankr. D. Me. Oct. 13, 2015)
- *Johnson v. Midland Funding, LLC*, 528 B.R. 462, 467-68 & n.15 (S.D. Ala. 2015)
- *In re Freeman*, 540 B.R. 129, 143 (Bankr. E.D. Pa. 2015)
- *In re Jenkins*, 538 B.R. 129, 135 (Bankr. N.D. Ala. 2015)
- *United States v. Moriarty*, 8 F.3d 329, 334 (6th Cir. 1993)

Chapter 13 Trustees

- **Chapter 13 Trustees**
  - Does the Trustee provide a financial product or related service to a financial product?
    - See Morgan Drexen – Debt Settlement Attorneys- March 2016- Court ordered the now-defunct Morgan Drexen to pay $173 million in fines and restitution, on grounds that the firm illegally charged upfront fees to consumers, claiming it could settle their debt.
  - However, see Wisconsin case- Foreclosure Assistance- The Mortgage Law Group.

Chapter 13 Trustees - Supervised Entities?

- Collection Attorneys are in…and maybe Trustees next?
  - Practicing law exclusion in Dodd-Frank: filing a suit is ~~not~~ "incidental to the practice of law"
  - CFPB is creating a new class of attorneys whose clients are not afforded First Amendment or Equal Protection Rights
  - Streamlining and automation of clerical/non-legal tasks is not "unauthorized practice of law" and is in the best interest of attorney's clients

Speaker Biographies

Kathleen A. Leavitt has served as a Standing Chapter 13 Bankruptcy Trustee for the District of Nevada since 1981. She has served as editor of *The Quarterly*, a publication dealing with Chapter 13 bankruptcy and consumer bankruptcy matters for over ten years. She was president of the National Association of Chapter 13 Trustees in 1997 and currently chairs its Bankruptcy Rules Committee. She also serves on the NACTT IRS Liaison Committee and Publication Editorial Board. From 1995 through 2005, Ms. Leavitt served on the Executive Board of Consumer Credit Counseling of Southern Nevada. She has prepared and presented educational programs for the American Bankruptcy Institute, the State Bar of Nevada, and the Southern Nevada Association of Bankruptcy Attorneys, and the Department of Justice – U.S. Trustee Program.

Alane A. Becket is an AV® rated attorney and Managing Partner of Becket & Lee LLP, a Malvern, Pa. law firm providing comprehensive nationwide representation of creditors in bankruptcy matters. In addition to client and industry relations, Alane focuses on litigation strategy, and Becket & Lee has been lead or co-counsel in some of the most influential decisions in consumer bankruptcy over the last 10 years. In addition to the NACTT, Alane is a member of the Executive Committee and Vice-President of Publications for the American Bankruptcy Institute (ABI). She is also a member of the National Association of Retail Collection Attorneys (NARCA) and the National Association of Bankruptcy Trustees. Alane has written and lectured extensively on consumer bankruptcy issues for a variety of professional organizations, including the NACTT, Norton Bankruptcy Law Advisor, NARCA, National Conference of Bankruptcy Judges, ABI, Commercial Law League of America and a host of local and regional creditor organizations. Recently, Alane co-authored the revised edition of the ABI treatise *Consumer Bankruptcy: Fundamentals of Chapter 7 and Chapter 13 of the U.S. Bankruptcy Code* (Third Edition).

John Franchini is the head of the legal bankruptcy group for Consumer and Community Banking at JP Morgan Chase. John and his team support all of the lines of business within Consumer and Community Banking, as well as all of the cross line of business initiatives. Prior to joining JP Morgan Chase, John was at the international law firm of Morgan, Lewis and Bockius. John is a graduate of the University of Virginia Law School.

Joann Needleman is leader of Clark Hill's Consumer Financial Services Regulatory & Compliance group in Philadelphia, PA. Joann has extensive litigation experience in state and federal courts, successfully defending creditors against claims brought under the Fair Debt Collection Practices Act and Fair Credit Reporting Act as well as state statutes. She provides counsel, consultation and litigation services to financial institutions, law firms, credit reporting agencies, and debt buyers throughout the country. Joann is the immediate past President of the Board of Directors of the National Creditors Bar Association (NARCA). She also serves on the Consumer Financial Protection Bureau Consumer Advisory Board. Joann was named a Pennsylvania Super Lawyer in 2004-2006, 2010-2011, and 2013-2016.

Barbara A. Sinsley is nationally known for her intelligent, aggressive representation of creditors, debt collectors and debt buyers, with a focus on developing and improving Compliance Management Systems and handling CFPB, FTC, and Attorneys General investigations and examinations. She is AV rated by Martindale Hubbell. Prior to rejoining Barron & Newburger in an of counsel capacity, Ms. Sinsley practiced with Barron, Newburger & Sinsley from 2007

to 2011. Prior to that, Ms. Sinsley was Vice President for Asset Acceptance Capital Corp during the time when that company launched its Initial Public Offering. As part of her daily responsibilities at Asset Acceptance, she assisted in the due diligence of corporate acquisition and portfolio acquisitions. In addition to these positions, Ms. Sinsley demonstrated her industry leadership through serving as the General Counsel of DBA International where she negotiated significant legislation impacting the operations of the collections industry. Ms. Sinsley received a B.A. in Behavioral Science and Law in 1985 from the University of Wisconsin – Madison. She received a J.D. in 1989 from South Texas College of Law in Houston, Texas.

10:30 - 11:30 **Provisions for Student Loan Debt**: How to incorporate into the plan remedies available outside of bankruptcy.
Moderator: D. Sims Crawford, NACTT President-Elect and Chapter 13 Standing Trustee for the Northern District of Alabama, Southern Division (Birmingham)
Edward C. Boltz, The Law Offices of John T. Orcutt (Durham, NC)

INDEX OF MATERIALS

1. **Chronology of Student Loan Discharge**
2. **Opinion -** ***Inst. of Imaginal Studies v. Christoff (In re Christoff)***
3. **Memorandum of Opinion Denying Summary Judgment –** ***Nightingale v. North Carolina State Education Assistance Authority***
4. **NCLC Amicus Brief –** ***Murphy v. United States Department of Education Credit Management Corporation***
5. **PDF of PowerPoint Presentation**
6. **Speaker Biographies**

Chronology of Student Loan Discharge	
Date	**Event**
1978	Under the Bankruptcy Code, all student loans were dischargeable in Chapter 7 five years after first due and always dischargeable in Chapter 13
May 1982	Bruner receives Masters degree in Social Work.
December 1982	Bruner files Chapter 7, seeking discharge of $9,000 of student loans.
1987	*Bruner* decided.
1990	Crime Control Act of 1990 extended period for discharge in Chapter 7 from five to seven years, with dischargability of all government student loan subject to the "undue hardship" standard in Chapter 13 also.
1991	Higher Education Act amended to permit administrative wage garnishment of 10% of income and intercept tax refunds for student loans.
1996	Debt Collection Improvement Act of 1996 amended to allow offset of Social Security benefits and 6-year statute of limitations for collection of student loans was repealed.
1998	Higher Education Amendments eliminated the waiting period, making dischargability of all government student loan subject to the "undue hardship" standard.
2005	BAPCPA makes dischargability of all private student loan subject to the "undue hardship" standard.
2006	Deficit Reduction Act of 2005 increase administrative wage garnishment from 10% to 15% of income.

11 U.S.C. § 524(m)(1):

Until 60 days after an agreement of the kind specified in subsection (c) is filed with the court (or such additional period as the court, after notice and a hearing and for cause, orders before the expiration of such period), **it shall be presumed that such agreement is an undue hardship on the debtor if the debtor's monthly income less the debtor's monthly expenses as shown on the debtor's completed and signed statement in support of such agreement required under subsection (k)(6)(A) is less than the scheduled payments on the reaffirmed debt.** This presumption shall be reviewed by the court. The presumption may be rebutted in writing by the debtor if the statement includes an explanation that identifies additional sources of funds to make the payments as agreed upon under the terms of such agreement. If the presumption is not rebutted to the satisfaction of the court, the court may disapprove such agreement. No agreement shall be disapproved without notice and a hearing to the debtor and creditor, and such hearing shall be concluded before the entry of the debtor's discharge.

Neutral
As of: September 15, 2015 3:23 PM EDT

Inst. of Imaginal Studies v. Christoff (In re Christoff)

United States Bankruptcy Appellate Panel for the Ninth Circuit
February 19, 2015; March 27, 2015, Filed
BAP No. NC-14-1336-PaJuTa

Reporter

527 B.R. 624; 2015 Bankr. LEXIS 973; Bankr. L. Rep. (CCH) P82,795; 73 Collier Bankr. Cas. 2d (MB) 689

In re: TARRA NICHOLE CHRISTOFF, Debtor. INSTITUTE OF IMAGINAL STUDIES dba MERIDIAN UNIVERSITY, Appellant, v. TARRA NICHOLE CHRISTOFF, Appellee.

Prior History: **[**1]** Appeal from the United States Bankruptcy Court for the Northern District of California. Bk. No. 13-10808, Adv. No. 13-3186. Hon. Dennis Montali, U.S. Bankruptcy Judge, Presiding.
Inst. of Imaginal Studies v. Christoff (In re Christoff), 510 B.R. 876, 2014 Bankr. LEXIS 2628 (Bankr. N.D. Cal., 2014)

LexisNexis® Headnotes

Bankruptcy Law > Procedural Matters > Adversary Proceedings > Judgments

Bankruptcy Law > ... > Judicial Review > Standards of Review > De Novo Standard of Review

Civil Procedure > Appeals > Summary Judgment Review > Standards of Review

HN1 A bankruptcy appellate panel reviews a bankruptcy court's grant of summary judgment de novo.

Bankruptcy Law > Procedural Matters > Adversary Proceedings > Judgments

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Appropriateness

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Legal Entitlement

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Materiality of Facts

HN2 According to *Fed. R. Civ. P. 56*, made applicable to adversary proceedings in *Fed. R. Bankr. P. 7056*, summary judgment is appropriate if there is a showing that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law. *Fed. R. Civ. P. 56(a)*. A trial court, in the exercise of its discretion, may grant a summary judgment for a nonmovant pursuant to *Rule 56(f)(1)*.

Bankruptcy Law > ... > Judicial Review > Standards of Review > De Novo Standard of Review

Bankruptcy Law > Discharge & Dischargeability > Exceptions to Discharge > Student Loans

Governments > Legislation > Interpretation

HN3 A bankruptcy appellate panel reviews de novo a bankruptcy court's application of the legal standard in determining whether a student loan debt is dischargeable. To the extent the bankruptcy court interpreted statutory law, the panel reviews the issues of law de novo.

Governments > Legislation > Interpretation

Bankruptcy Law > Discharge & Dischargeability > Exceptions to Discharge > Student Loans

HN4 While *11 U.S.C.S. § 523(a)(8)(A)(i)* and *(B)* make ″loans″ nondischargeable in bankruptcy, absent undue hardship, *§ 523(a)(8)(A)(ii)* applies to a different type of debt: a debtor's obligation to repay funds received as an educational benefit, scholarship, or stipend. Because Congress did not refer to ″loans″ in this subsection of the Bankruptcy Code, it was intended to apply to a distinctly different type of debt, an obligation to repay the creditor for ″funds received.″ Therefore, it is inappropriate to borrow from the logic of the cases construing the ″loan″ language used in the other student debt exceptions to construe the meaning of ″funds received″ in *§ 523(a)(8)(A)(ii)*.

Bankruptcy Law > General Overview

Governments > Legislation > Interpretation

HN5 Any analysis of the Bankruptcy Code begins with the text of the statute. Furthermore, the words of the Code must be read in their context and with a view to their place in the overall statutory scheme. If the statutory language is unambiguous and the statutory scheme is coherent and consistent, judicial inquiry must cease.

Bankruptcy Law > Discharge & Dischargeability > Exceptions to Discharge > General Overview

HN6 Courts must limit the provisions granting exceptions to discharge to those plainly expressed in *11 U.S.C.S. § 523(a)*. The exception to discharge provisions of the Bankruptcy Code are interpreted strictly in favor of debtors.

Bankruptcy Law > Discharge & Dischargeability > Exceptions to Discharge > Student Loans

HN7 *11 U.S.C.S. § 523(a)(8)* provides that a debtor may not discharge a debt: unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor's dependents, for -- (A)(i) an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit or nonprofit institution; or (ii) an obligation to repay funds received as an educational benefit, scholarship, or stipend; or (B) any other educational loan that is a qualified education loan, as defined in *26 U.S.C.S. § 221(d)(1)*, incurred by a debtor who is an individual.

Bankruptcy Law > Discharge & Dischargeability > Exceptions to Discharge > Student Loans

Tax Law > Federal Income Tax Computation > Nonbusiness Expenses > Educational Expenses

Education Law > Administration & Operation > Career & Technical Schools

HN8 Under *11 U.S.C.S. § 523(a)(8)(B)* to be a ″qualified education loan″ under *26 U.S.C.S. § 221(d)(1)*, it must, among other things, be a debt for a ″qualified higher education expense,″ as defined by *§ 221(d)(2)*, which is the costs of attendance at an eligible educational institution. An ″eligible educational institution″ is one as defined by *26 U.S.C.S. § 25A(f)(2)*, which provides that an ″eligible educational institution″ means an institution -- (A) which is described in § 481 of the Higher Education Act of 1965 (*20 U.S.C.S. 1088*); (B) which is eligible to participate in a program under Title IV of such Act. An ″eligible program″ is further defined at *§ 1088(b)*.

Bankruptcy Law > Discharge & Dischargeability > Exceptions to Discharge > Student Loans

Governments > Legislation > Interpretation

Governments > Courts > Judicial Precedent

HN9 The language of *11 U.S.C.S. § 523(a)(8)* is plain, and it must be read in context with a view to the overall statutory scheme. Moreover, as instructed by the United States Supreme Court and Ninth Circuit, the United

States Bankruptcy Appellate Panel for the Ninth Circuit must construe § 523(a) narrowly, limiting this discharge exception to those debts described in the statute. Finally, the panel must construe the provisions of § 523(a)(8) that were found in the pre-BAPCPA version of that statute in accord with the Ninth Circuit authorities interpreting them.

Bankruptcy Law > Discharge & Dischargeability > Exceptions to Discharge > Student Loans

HN10 11 U.S.C.S. § 523(a)(8)(A)(ii) plainly provides that a bankruptcy discharge will not impact an obligation to repay funds received as an educational benefit, scholarship, or stipend. To except a debt from discharge under this subsection, a creditor must demonstrate that the debtor is obliged to repay a debt for "funds received" for the educational benefits.

Bankruptcy Law > Discharge & Dischargeability > Exceptions to Discharge > Student Loans

Governments > Legislation > Interpretation

HN11 The exact wording used in amended 11 U.S.C.S. § 523(a)(8)(A)(ii) was formerly a part of § 523(a)(8). However, BAPCPA set off the "obligation to repay funds received" language from the other provisions of § 523(a)(8) in a new subsection. In restructuring the discharge exception in this fashion, Congress created a separate category de-linked from the phrases "educational benefit or loan" in § 523(a)(8)(A)(i) and "any other educational loan" in § 523(a)(8)(B). Put another way, "new" § 523(a)(8)(A)(ii), now standing alone, excepts from discharge only those debts that arise from "an obligation to repay funds received as an educational benefit," and must therefore be read as a separate exception to discharge as compared to that provided in § 523(a)(8)(A)(i) for a debt for an "educational overpayment or loan" made by a governmental unit or nonprofit institution or, in § 523(a)(8)(B), for a "qualified education loan."

Governments > Legislation > Interpretation

HN12 In interpreting a statute, a court should always turn first to one, cardinal canon before all others. Courts must presume that a legislature says in a statute what it means and means in a statute what it says there.

Bankruptcy Law > Discharge & Dischargeability > Exceptions to Discharge > Student Loans

Governments > Legislation > Interpretation

HN13 A court must presume that, in organizing the provisions of 11 U.S.C.S. § 523(a)(8) as it did in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), Congress intended each subsection to have a distinct function and to target different kinds of debts.

Governments > Legislation > Interpretation

Bankruptcy Law > Discharge & Dischargeability > Exceptions to Discharge > Student Loans

HN14 11 U.S.C.S. § 523(a)(8)(A)(ii) is not a "catch-all" provision designed to include every type of credit transaction that bestows an educational benefit on a debtor. Instead, this subsection includes a condition, distinct from those in the other subsections of § 523(a)(8), that must be fulfilled. This unique requirement, that funds be received by the debtor, mandates that cash be advanced to or on behalf of the debtor. In light of the many programs available to students which provide cash benefits to students, like veteran's educational benefits, stipends for teaching assignments, and cash scholarships, it is not absurd to assume that Congress intended the scope of § 523(a)(8)(A)(ii) to target obligations other than those arising from traditional student loans.

Counsel: Scott D. Schwartz of Rust, Armenis & Schwartz, P.C. argued for Appellant Institute of Imaginal Studies d/b/a Meridian University.

Lindsay Torgerson of Wine Country Family Law & Bankruptcy Office argued for Appellee Tarra Nichole Christoff.

Judges: Before: PAPPAS, JURY, and TAYLOR, Bankruptcy Judges.

Opinion by: PAPPAS

Opinion

[*625] PAPPAS, Bankruptcy Judge:

This appeal raises an important issue of first impression concerning the scope of the exception to discharge for student debts in bankruptcy. Creditor Institute of Imaginal Studies d/b/a Meridian University ("Meridian") appeals the summary judgment of the bankruptcy court determining that the debt owed to Meridian by chapter **[*626]** 7[1] debtor Tarra Nichole Christoff ("Debtor") was not excepted from discharge pursuant to *§ 523(a)(8)(A)(ii)*. Based upon the plain language of the Bankruptcy Code, we AFFIRM.

I. FACTS[2]

A. Relationship of the Parties.

Meridian is a for-profit California corporation which operates a private university licensed under California's Private Post Secondary Education Act of 2009, *Cal. Educ. Code § 94800, et seq.* If a graduate of Meridian fulfills other post-graduate requirements, the graduate may obtain a license from California to practice as an independent, unsupervised psychologist.

Debtor applied for admission to Meridian in 2002. Meridian agreed to admit Debtor and offered her $6,000 in financial aid to pay a portion of the tuition for that school year. Under this arrangement, Debtor did not receive any actual funds from Meridian, but instead she received a tuition credit. Debtor signed an enrollment agreement acknowledging Meridian's offer to "finance" $6,000 of the tuition, and she signed a promissory note in favor of Meridian evidencing her obligation. The promissory note provided that the debt for the tuition credit was to be paid by Debtor in installments of $350 per month after Debtor completed her course work or withdrew from Meridian. Interest accrued on the unpaid balance of the note at nine percent per annum, compounded **[**3]** monthly.

In 2003, Debtor submitted a similar application, and Meridian granted her a financial aid award of $5,000 for that school year. As before, Debtor signed a promissory note for $5,000. Again, Debtor did not receive any funds but instead received a tuition credit. The promissory note contained payment terms identical to those in the prior note.

Debtor completed her course work at Meridian, and Debtor's note payments began in October 2005. After making several payments on the notes, in 2009, Debtor sought a deferral of her payments for a period of one year. Meridian granted the extension. Also in 2009, Debtor withdrew from Meridian without completing her dissertation, a requirement for obtaining her degree.

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[1] Unless otherwise indicated, all chapter, section and rule references are to the Bankruptcy Code, ***11 U.S.C. §§ 101-1532***, and to the Federal Rules of Bankruptcy Procedure, Rules 1001-9037. "Civil Rule" references are to the Federal Rules of Civil Procedure 1-86.

[2] This recitation of the undisputed facts is taken primarily from the **[**2]** bankruptcy court's decision, which neither of the parties has challenged.

After the extension expired, Debtor did not pay the amounts due under the two promissory notes. Thereafter, Meridian unsuccessfully attempted to collect the balance due from Debtor. Eventually, Meridian and Debtor agreed to submit Meridian's claims to arbitration under a provision in the enrollment agreement. In July 2012, an arbitrator ordered Debtor to pay Meridian the unpaid balance due on the promissory notes, $5,950, plus accrued interest.

B. The Bankruptcy Case and Adversary [4] Proceeding**.

Debtor filed a chapter 7 bankruptcy petition on August 19, 2013. Debtor listed Meridian in schedule F as an unsecured, nonpriority creditor. Meridian commenced an adversary proceeding against Debtor seeking a determination by the bankruptcy court that the debt owed by **[*627]** Debtor to Meridian was excepted from discharge pursuant to *§ 523(a)(8)*.

On April 30, 2014, Meridian filed a motion for summary judgment. In its motion, Meridian conceded that Debtor's debt did not qualify for an exception to discharge under either *§ 523(a)(8)(A)(i)* or *(a)(8)(B)*.[3] However, it argued that the debt was excepted from discharge under *§ 523(a)(8)(A)(ii)*. Debtor disputed that this Code provision applied to her debt to Meridian.[4] The parties appeared at a motion hearing on May 30, 2014, presented their arguments, and the bankruptcy court took the issues under advisement.

On June 11, 2014, the bankruptcy court entered a Memorandum Decision in which it held that Debtor's debt to Meridian did not qualify for an exception to discharge under *§ 523(a)(8)(A)(ii)*. *Inst. of Imaginal Studies dba Meridian Univ. v. Christoff (In re Christoff), 510 B.R. 876, 884 (Bankr. N.D. Ca. 2014)*. In making this ruling, the bankruptcy court noted that the question raised by the motion was an issue of first impression in the Ninth Circuit following enactment of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA).[5] After a thorough review of amended *§ 523(a)(8)* and the cases addressing the issue, the bankruptcy court concluded:

> [b]ecause Debtor's obligations under applicable documents were to pay the amount under the [p]romissory [n]otes, and thereafter the arbitration award, but did not flow from 'funds received' either by her as the student or by Meridian from any other source, the debt is not covered by *[§ 523(a)(8)(A)(ii)]* and is therefore eligible for discharge in Debtor's discharge.

In re Christoff, 510 B.R. at 884.

Interpreting the "funds received" requirement in *§ 523(a)(8)(A)(ii)*, the bankruptcy court explained that "Meridian simply agreed to be paid the tuition later . . . [i]t did not receive any funds, such **[**6]** as from a third party financing source." *Id. at 879*. The bankruptcy court therefore concluded that, while the transactions between Debtor and Meridian were clearly loans, *§ 523(a)(8)(A)(ii)* does not extend to loans but, instead, grants an exception to discharge for "an obligation to repay funds received." *Id. at 879*. The bankruptcy court observed that BAPCPA had amended the prior version of *§ 523(a)(8)* and had created a "newly separated *[§ 523(a)(8)(A)(ii)*, which] refers to an 'obligation to repay funds received as an educational benefit, scholarship[,] or stipend,' without reference to educational loans or any other kind of loan." Id.

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[3] We agree that Meridian cannot take advantage of these discharge exceptions because it was neither a governmental unit nor a nonprofit institution as required for an exception under ***§ 523(a)(8)(A)(i)***, nor was the debt in this case a "qualified education loan" as defined by the Internal Revenue Code, a condition for an exception to discharge under ***§ 523(a)(8)(B)***.

[4] The parties agreed that if the bankruptcy court determined that **[**5]** the Meridian debt qualified for an exception to discharge under ***§ 523(a)(8)(A)(ii)***, Debtor would be allowed to amend her answer and plead that she could not repay the debt without an "undue hardship".

[5] Pub. L. No. 109-8, 119 Stat. 23.

Meridian filed a notice of appeal concerning the Memorandum Decision on June 26, 2014. The bankruptcy court, on July 2, 2014, entered an order granting summary judgment in favor of Debtor and denying Meridian's motion for summary judgment; it also entered a judgment incorporating these rulings. On July 11, 2014, Meridian filed an amended notice of **[*628]** appeal to include the order and judgment entered by the bankruptcy court.

II. JURISDICTION

The bankruptcy court had jurisdiction under *28 U.S.C. §§ 1334* and *157(b)(2)(I)*. We have jurisdiction under *28 U.S.C. § 158*.

III. ISSUE

Whether the bankruptcy court erred in holding that the Meridian debt was not excepted from **[**7]** discharge under *§ 523(a)(8)(A)(ii)* because it was not an obligation for "funds received."

IV. STANDARDS OF REVIEW

HN1 We review a bankruptcy court's grant of summary judgment de novo. *The President & Bd. of Ohio Univ. v. Hawkins (In re Hawkins), 317 B.R. 104, 108 (9th Cir. BAP 2004)*, aff'd, *469 F.3d 1316 (9th Cir. 2006)*; *Thorson v. Cal. Student Aid Comm'n (In re Thorson), 195 B.R. 101, 103 (9th Cir. BAP 1996)* (citing *Jones v. Union Pac. R.R. Co., 968 F.2d 937, 940 (9th Cir. 1992))*. ***HN2*** According to *Civil Rule 56*, made applicable to adversary proceedings in *Rule 7056*, summary judgment is appropriate if there is a showing "that there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." *Civil Rule 56(a)*; *Celotex Corp. v. Catrett, 477 U.S. 317, 322, 106 S. Ct. 2548, 91 L. Ed. 2d 265 (1986)*. A trial court, in the exercise of its discretion, may grant a summary judgment for a nonmovant pursuant to *Civil Rule 56(f)(1)*.

HN3 "We review de novo the bankruptcy court's application of the legal standard in determining whether a student loan debt is dischargeable." *Educ. Credit Mgmt. Corp. v. Jorgensen (In re Jorgensen), 479 B.R. 79, 85 (9th Cir. BAP 2012)* (citing *Rifino v. United States (In re Rifino), 245 F.3d 1083, 1087 (9th Cir. 2001))*. "To the extent the bankruptcy court interpreted statutory law, we review the issues of law de novo." *In re Thorson, 195 B.R. at 103*.

V. DISCUSSION

A. Arguments of the Parties.

Meridian argues that the bankruptcy court erred when it interpreted *§ 523(a)(8)(A)(ii)* to require that actual funds be received by a debtor in order for a debt to qualify for an exception to discharge under that provision. According to Meridian, "funds received," as that language is used in *§ 523(a)(8)(A)(ii)*, is the equivalent to "loans" received by the debtor, as described in the other provisions **[**8]** of *§ 523(a)(8)*. To support this argument, Meridian cites to *McKay v. Ingleson, 558 F.3d 888 (9th Cir. 2009)*, and to *Johnson v. Mo. Baptist Coll. (In re Johnson), 218 B.R. 449 (8th Cir. BAP 1998)*, a decision cited and relied upon by the Ninth Circuit in McKay. Meridian argues that the bankruptcy court erred in distinguishing these cases because those decisions determined that a "loan" under *§ 523(a)(8)* required no funds to be transferred to a debtor. Meridian argues that since the terms "loan" and "funds received" are synonymous as used in *§ 523(a)(8)*, McKay and In re Johnson control the outcome in this case.

Debtor points to the difference in the language employed by Congress to delineate what types of student debts are excepted from discharge under *§ 523(a)(8)*. ***HN4*** While *§ 523(a)(8)(A)(i)* and *(B)* indeed make "loans"

nondischargeable in bankruptcy, absent undue hardship, § 523(a)(8)(A)(ii) applies to a different type of debt: a debtor's ″obligation to repay funds received as an educational benefit, scholarship, or stipend [.]″ Because Congress **[*629]** did not refer to ″loans″ in this subsection of the Code, Debtor urges that it was intended to apply to a distinctly different type of debt, an obligation to repay the creditor for ″funds received.″ Therefore, Debtor argues, it is inappropriate to borrow from the logic of the cases construing the ″loan″ language used in the other student debt exceptions **[**9]** to construe the meaning of ″funds received″ in § 523(a)(8)(A)(ii).

We agree with Debtor.

B. Statutory Interpretation and Exceptions to Discharge.

HN5 Any analysis of the Bankruptcy Code begins with the text of the statute. *Ransom v. FIA Card Servs., N.A., 562 U.S. 61, 69, 131 S. Ct. 716, 178 L. Ed. 2d 603 (2011)*; *Danielson v. Flores (In re Flores), 735 F.3d 855, 859 (9th Cir. 2013)* (en banc) (citing *Miranda v. Anchondo, 684 F.3d 844, 849 (9th Cir. 2011)*. ″Furthermore, 'the words of [the Code] must be read in their context and with a view to their place in the overall statutory scheme.'″ *In re Flores, 735 F.3d at 859* (quoting *Gale v. First Franklin Loan Servs., 701 F.3d 1240, 1244 (9th Cir. 2012))*. ″If the statutory language is unambiguous and the statutory scheme is coherent and consistent, judicial inquiry must cease.″ *Fireman's Fund Ins. Co. v. Plant Insulation Co. (In re Plant Insulation Co.), 734 F.3d 900, 910 (9th Cir. 2013)* (citations and internal quotation marks omitted).

HN6 Courts must limit the provisions granting exceptions to discharge to those plainly expressed in § 523(a). *Bullock v. BankChampaign, N.A., 133 S. Ct. 1754, 1760, 185 L. Ed. 2d 922 (2013)* (noting the ″long-standing principle that exceptions to discharge should be confined to those plainly expressed″) (internal quotations marks and citations omitted); *Hawkins v. Franchise Tax Bd. of Cal., 769 F.3d 662, 666 (9th Cir. 2014)* (reminding that ″the Supreme Court has interpreted exceptions to the broad presumption of discharge narrowly″); *Sachan v. Huh (In re Huh), 506 B.R. 257, 263 (9th Cir. BAP 2014)* (en banc) (stating ″the exception to discharge provisions of the Bankruptcy Code are interpreted strictly in favor of debtors″); *Benson v. Corbin (In re Corbin), 506 B.R. 287, 291 (Bankr. W.D. Wa. 2014)* (observing, in a § 523(a)(8) case, that ″[c]ourts construe exceptions to discharge strictly against a creditor and liberally in favor of the debtor″).

B. The Pre-BAPCPA § 523(a)(8).

The student debt **[**10]** exception to discharge, embodied in § 523(a)(8), has been amended several times over the years, most recently by BAPCPA in 2005.

Prior to BAPCPA, § 523(a)(8) provided that a bankruptcy discharge would not apply to a debt for:

> an educational benefit overpayment or loan made, insured or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit, or nonprofit institution, or for an obligation to repay funds received as an educational benefit, scholarship, or stipend, unless excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor's dependents.

In re Hawkins, 317 B.R. at 108 (quoting § 523(a)(8)).

Interpreting this version of § 523(a)(8), the Panel stated,

> [g]enerally speaking, debts that are potentially nondischargeable under § 523(a)(8) fall into two categories: 1) debts for educational benefit overpayments or loans made, insured, or guaranteed by a governmental unit or nonprofit institution; or 2) debts for **[*630]** obligations to repay funds received as an educational benefit, scholarship[,] or stipend.

Id. at 109 (citing Mehlman v. N.Y. City Bd. of Educ. (In re Mehlman), 268 B.R. 379, 383 (Bankr. S.D.N.Y. 2001)).

In In re Hawkins, the Panel examined an agreement between the debtor and Ohio University wherein the debtor agreed, in exchange for admission to the University's medical school, that when **[**11]** she completed her studies she would practice medicine in Ohio for at least five years after licensure. 317 B.R. at 107. If she failed to do this, the agreement provided that she would pay liquidated damages to the University. Id. The debtor graduated but promptly moved to a different state. Id. The University sued the debtor in state court and obtained a money judgment for the liquidated damages specified in the agreement. Id. The debtor filed for chapter 7 relief, and the University sought a determination from the bankruptcy court that the judgment debt was excepted from discharge under § 523(a)(8). Id. at 108. Applying § 523(a)(8) to these facts, the Panel addressed both categories of debt covered by the discharge exception. Id. at 110-11.

First, the Panel concluded that the agreement between the debtor and the University was not an "educational loan" because "while an educational loan need not include an actual transfer of money . . . to [the d]ebtor, in order for it to fall within the definition of . . . § 523(a)(8), the loan instrument must sufficiently articulate definite repayment terms and the repayment obligation must reflect the value of the benefit actually received [by the debtor], rather than some other ill defined measure of damages **[**12]** or penalty." Id. at 110 (emphasis deleted).

Next, the Panel considered whether the agreement created a debt for "an obligation to repay funds received as an educational benefit." Id. at 112. The Panel quickly concluded that it did not, "because the plain language of this prong of the statute requires that a debtor receive actual funds in order to obtain a nondischargeable educational benefit." Id. (citing Cazenovia Coll. v. Renshaw (In re Renshaw), 229 B.R. 552, 555 n.5 (2d Cir. BAP 1999), aff'd, 222 F.3d 82 (2d Cir. 2000)). The University appealed the BAP's decision and the Ninth Circuit affirmed, adopting the opinion of the BAP as its own. See Ohio Univ. v. Hawkins (In re Hawkins), 469 F.3d 1316, 1317 (9th Cir. 2006) ("We adopt the opinion of the BAP, which is reported at 317 B.R. 104, and affirm its judgment.").

A few years later, the Ninth Circuit again addressed whether an agreement between a student and a college constituted a "loan" for purposes of the pre-BAPCPA version of § 523(a)(8). In McKay v. Ingleson, 558 F.3d 888, 889 (9th Cir. 2009), the court reviewed an agreement between the debtor and Vanderbilt University that deferred payment of the debtor's tuition and costs of other "educational services" to monthly bills to be sent to the debtor. Id. If the debtor did not pay the bills as they became due, a late fee would be assessed. Id. The debtor did not pay the bills as agreed and later filed for bankruptcy relief. A couple of years after the **[**13]** debtor received her discharge, the University sued the debtor in state court to recover the amounts owed under the agreement. In response, the debtor commenced an adversary proceeding against the University in the bankruptcy court claiming that the University violated the discharge injunction of § 524(a) by prosecuting the state court action. Id. The bankruptcy court, and later the district court on appeal, concluded that no violation of the discharge injunction occurred because the debt at issue was excepted from discharge **[*631]** under § 523(a)(8). Id. The Ninth Circuit affirmed, reasoning that the agreement between the parties was a nondischargeable "loan" under § 523(a)(8), and that it did not matter that no actual money had changed hands between the parties under their arrangement. Id. at 890. In explaining its decision, the court cited to In re Johnson, 218 B.R. 449 (8th Cir. BAP 1998). Id. The court also cited to the BAP's opinion in In re Hawkins for the proposition that the amount of the loan must be based on the amount of benefit the debtor received; the court concluded that the "loan" in McKay complied with that requirement. Id. at 891.

In re Johnson, the decision relied upon by the Ninth Circuit in McKay, addressed what constituted a "loan" under the pre-BAPCPA version **[**14]** of § 523(a)(8): "Since the parties stipulate that the [c]ollege is a non-profit institution and that the credit was extended for educational purposes . . . the only issue presently on appeal is whether the [c]ollege's extension of credit was a loan." In re Johnson, 218 B.R. 450-51. In re Johnson

focused on a debt represented by a promissory note, executed to evidence the debtor's obligation to a college to pay for tuition, books, and other expenses. *Id. at 450*. The debtor defaulted on the note and filed a chapter 13 case. Id. The college filed an adversary proceeding in the debtor's bankruptcy case asking the bankruptcy court to declare that the debt represented by debtor's note was excepted from discharge. Id. The bankruptcy court concluded that the debt was a ″loan″ for purposes of *§ 523(a)(8)*, and the Eighth Circuit BAP agreed. Id. The panel rejected the debtor's argument that the note was not a ″loan″ because no funds had ever been given to him by the college:

> [W]e conclude[] that the arrangement between [the debtor] and the [c]ollege constitutes a loan . . . . [B]y allowing [the debtor] to attend classes without prepayment, the [c]ollege was, in effect, 'advancing' funds . . . to [the debtor] . . . [and i]t is immaterial that no money actually changed hands.

Id. at 457.

It is important to note that the BAP in In re **[**15]** Johnson, as relied upon by the Ninth Circuit in McKay, acknowledged that another avenue may have existed for the college to obtain an exception to discharge under *§ 523(a)(8)*, characterizing the note as ″an obligation to repay funds received as an educational benefit″; however, the panel determined it need not venture down that path because the debt arising from the agreement with the debtor was determined to be an educational benefit ″loan″ made by a nonprofit or a governmental unit.[6] *218 B.R. at 450*. By contrast, in In re Hawkins, the Panel was required to decide whether the agreement before it created ″an obligation to repay funds received as an educational benefit″ because it had concluded the agreement was not a ″loan″ under the statute. *317 B.R. at 112*. In addressing this issue, the Panel stated ″the plain language of this prong of the statute requires that a debtor receive actual funds in order to obtain a nondischargeable benefit.″ Id. (citations omitted; emphasis added). The Panel found this requirement was not satisfied because no ″actual funds″ were received by the debtor in consideration of her admission and education at the medical school. Id.

C. Enter BAPCPA.

As a result of the Code amendments in BAPCPA, since 2005, ***HN7*** *§ 523(a)(8)* has provided **[*632]** that a debtor may not discharge a debt:

> unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor's dependents, for—
>
> (A)(i) an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit or nonprofit institution; or
>
> (ii) an obligation to repay funds received as an educational benefit, scholarship, or stipend; or
>
> (B) any other educational loan that is a qualified education loan, as defined in *section 221(d)(1) of the Internal Revenue Code of 1986*, incurred by a debtor who is an individual.[7]

As can be seen, many of the statute's former attributes survived BAPCPA's revisions. On the other hand, there

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[6] Of course, the college/creditor in In re Johnson was a nonprofit organization. **[**16]** See In re Johnson, 218 B.R. 450. (stating the ″parties stipulate that the [c]ollege is a non-profit institution″). Similarly, Vanderbilt University is a nonprofit institution.

[7] ***HN8*** Under ***§ 523(a)(8)(B)*** to be a ″qualified education loan″ under 26 U.S.C. § 221(d)(1), it must, among other things, be a debt for a ″qualified higher education expense,″ as defined by 26 U.S.C. § 221(d)(2), which is the ″costs of attendance . . . at an eligible educational institution.″ An **[**17]** ″eligible educational institution″ is one as defined by 26 U.S.C. § 25A(f)(2), which provides an ″'eligible educational institution' means an institution - (A) which is described in section 481 of the Higher Education Act of 1965 (20

were some additions to its text, and there was also a clear restructuring of the statute.

Since enactment of BAPCPA, neither the Ninth Circuit nor this Panel has published decisions interpreting *§ 523(a)(8)(A)(ii)*. And only one published decision, other than the bankruptcy court's decision at issue in this appeal, was located from bankruptcy courts in the Ninth Circuit interpreting *§ 523(a)(8)(A)(ii)*. *Benson v. Corbin (In re Corbin), 506 B.R. 287 (Bankr. W.D. Wa. 2014)*.[8] In *In re Corbin,* the bankruptcy court explained that, post-BAPCPA, this Code provision:

> protects four categories of educational claims from discharge: (1) loans made, insured, or guaranteed by a governmental unit; (2) loans made under any program partially or fully funded by a governmental unit or nonprofit institution; (3) claims for funds received as an educational benefit, scholarship, or stipend; and (4) any "qualified educational loan" as that term is defined in the Internal Revenue Code.

506 B.R. at 291 (citing *Rumer v. Am. Educ. Servs. (In re Rumer), 469 B.R. 553 (Bankr. M.D. Pa. 2012))*. The bankruptcy court explained that *§ 523(a)(8)(A)(ii)* "was added, covering loans made by nongovernmental **[**18]** and profit-making organizations . . . ." *Id. at 296*. Canvassing the out-of-circuit bankruptcy court decisions, the court noted that they "pay no attention to who the lender is, but focus instead [under *§ 523(a)(8)(A)(ii)*] on whether, in the plain language of the subsection, the obligation is 'to repay funds received as an educational benefit' as reflected by the debtor's agreement and intent to use the funds at the time the obligation arose." *Id. at 296-97* (citing *Roy v. Sallie Mae (In re Roy), 2010 Bankr. LEXIS 1218, 2010 WL 1523996 (Bankr. D.N.J. Apr. 15, 2010)*; *Carow v. Chase Student Loan Serv. (In re Carow), 2011 Bankr. LEXIS 823, 2011 WL 802847 (Bankr. D.N.D. Mar. 2, 2011)*; *Skipworth v. Citibank Student Loan Corp. (In re Skipworth),* **[*633]** 2010 Bankr. LEXIS 1201, 2010 WL 1417964 (Bankr. N.D. Ala. Apr. 1, 2010)).

Given the lack of case law, the bankruptcy court set out to apply post-BAPCPA *§ 523(a)(8)(A)(ii)* to the facts before it. *In re Corbin* involved cash advances from a third-party lender to the debtor to attend college made, in part, because the debtor's co-worker had agreed to co-sign the loan. *506 B.R. at 290*. The lender later notified the co-signer that the debtor was not paying the loan. Id. The co-signer paid the loans and sued the debtor in state court to recover the amounts he had paid the lender. Id. The debtor then filed a bankruptcy case, and the **[**19]** co-signer commenced an adversary proceeding against the debtor arguing that the debt owed by the debtor to the co-signer was excepted from discharge under both *§ 523(a)(8)(A)(i)* and *(a)(8)(A)(ii)*. Id. The bankruptcy court declined to hold that this arrangement qualified for an exception from discharge under *§ 523(a)(8)(A)(i)* based upon Ninth Circuit authority on subrogated claims. *Id. at 295-96* (citing *Nat'l Collection Agency v. Trahan, 624 F.2d 906 (9th Cir. 1980))*. However, the bankruptcy court concluded that the debt was excepted from discharge under *§ 523(a)(8)(A)(ii)*, reasoning that because the debtor

> intended to and did use the funds she received to pay for educational expenses . . . this [c]ourt concludes that the provisions of an accommodation, in order to secure for a student funds for the purpose of paying educational expenses, gives rise to an obligation on the part of the debtor to repay funds received as an educational benefit once the co-signer is required to honor its obligation to pay the debt.

Id. at 297-98.

Of course, the *In re Corbin* debtor actually received funds from the lender to pay for her education; the facts here are different.

U.S.C. 1088) . . . (B) which is eligible to participate in a program under title IV of such Act." An "eligible program" is further defined at 20 U.S.C. § 1088(b).

[8] In addition, only one unpublished decision in this circuit has tackled this chore. In a case that involved Meridian, relying heavily upon the bankruptcy court's decision here, the bankruptcy court declined to grant an exception to discharge. Inst. of Imaginal Servs. v. Coelho (In re Coelho), No. 13-10975, 2014 Bankr. LEXIS 3295, 2014 WL 3858514 (Bankr. N.D. Ca. Aug. 4, 2014).

D. Application of § 523(a)(8)(A)(ii) to Meridian's Debt

We agree with the bankruptcy court that ***HN9*** the language of *§ 523(a)(8)* is plain and that it must be read in context with a view to the overall statutory scheme. Moreover, **[**20]** as instructed by the Supreme Court and Ninth Circuit, we must construe *§ 523(a)* narrowly, limiting this discharge exception to those debts described in the statute. *Bullock, 133 S. Ct. at 1760*; *Hawkins, 769 F.3d at 666*; *In re Huh, 506 B.R. at 263*. Finally, we must construe the provisions of *§ 523(a)(8)* that were found in the pre-BAPCPA version of that statute in accord with the Ninth Circuit authorities interpreting them. Doing all this, we conclude that the debt represented by Meridian's arbitration award against Debtor is not excepted from discharge under *§ 523(a)(8)(A)(ii)*. As a result, the bankruptcy court did not err in granting summary judgment to Debtor, and denying Meridian's motion for summary judgment.

HN10 *Section 523(a)(8)(A)(ii)* plainly provides that a bankruptcy discharge will not impact ″an obligation to repay funds received as an educational benefit, scholarship, or stipend.″ It is undisputed that the agreements between Meridian and Debtor constitute an ″obligation to repay″ ″educational benefits″ provided by Meridian to Debtor. However, *§ 523(a)(8)(A)(ii)* requires more. To except a debt from discharge under this subsection, the creditor must demonstrate that the debtor is obliged to repay a debt for ″funds received″ for the educational benefits. The phrase ″funds received″ has been interpreted by the BAP, in an opinion which **[**21]** was as adopted by the Ninth Circuit as its own, to require ″that a debtor receive actual **[*634]** funds in order to obtain a nondischargeable benefit.″ *In re Hawkins, 317 B.R. at 112* (emphasis added); accord *In re Oliver, 499 B.R. 617, 625 (Bankr. S.D. Ind. 2013)* (holding under *§ 523(a)(8)(A)(ii)*, ″[i]n order to be obligated to repay funds received, [the] [d]ebtor had to have received funds in the first place.″) (emphasis in original). Because the In re Hawkins decision construed the very same language of the statute implicated here, we conclude that *In re Hawkins* controls the outcome in this case notwithstanding that BAPCPA later amended *§ 523(a)(8)*. See *Ball v. Payco-General Am. Credits, Inc. (In re Ball), 185 B.R. 595, 597 (9th Cir. BAP 1995)* (″We will not overrule our prior rulings unless a Ninth Circuit Court of Appeals decision, Supreme Court decision or subsequent legislation has undermined those rulings.″). That the arrangement between the parties in *In re Hawkins* was dissimilar to the agreement in this case is of no consequence, and renders that decision no less binding, concerning the proper construction of *§ 523(a)(8)(A)(ii)*. This is so because In re Hawkins construed the very same statutory language implicated here, and because the Panel and the Circuit have concluded that this language requires that ″a debtor receive actual funds.″ *Id. at 112*.

This result is bolstered by the changes made to *§ 523(a)(8)* by Congress in BAPCPA. As **[**22]** noted above, ***HN11*** the exact wording used in amended *§ 523(a)(8)(A)(ii)* was formerly a part of *§ 523(a)(8)*. However, BAPCPA set off the ″obligation to repay funds received″ language from the other provisions of *§ 523(a)(8)* in a new subsection. We agree with the bankruptcy court, that in restructuring the discharge exception in this fashion, Congress created ″a separate category delinked from the phrases 'educational benefit or loan' in *§ 523(a)(8)(A)(i)* and 'any other educational loan' in *§ 523(a)(8)(B)*.″ *In re Christoff, 510 B.R. at 882*. Put another way, ″new″ *§ 523(a)(8)(A)(ii)*, now standing alone, excepts from discharge only those debts that arise from ″an obligation to repay funds received as an educational benefit,″ and must therefore be read as a separate exception to discharge as compared to that provided in *§ 523(a)(8)(A)(i)* for a debt for an ″educational overpayment or loan″ made by a governmental unit or nonprofit institution or, in *§ 523(a)(8)(B)*, for a ″qualified education loan.″

Meridian's arguments conflating ″loan″ as used in *§ 523(a)(8)(A)(i)* and *(a)(8)(B)*, and as interpreted by McKay and In re Johnson with ″an obligation to repay funds received″ as provided in *§ 523(a)(8)(A)(ii)*, are unconvincing. According to Meridian, ″[t]here is no reason why the word 'funds' should not be interpreted in the same light that 'loans' has been interpreted in prior cases in the Ninth Circuit **[**23]** . . . .″ Appellant's Op. Br. at 14. In effect, Meridian argues that we should read *§ 523(a)(8)(A)(ii)* to say ″loans received″ as opposed to ″funds received.″ But this we must not do. See *Conn. Nat'l Bank v. Germain, 503 U.S. 249, 253-54, 112 S.*

Ct. 1146, 117 L. Ed. 2d 391 (1992) (***HN12*** "[I]n interpreting a statute a court should always turn first to one, cardinal canon before all others. We have stated time and again that courts must presume that a legislature says in a statute what it means and means in a statute what it says there.") (citations omitted). Instead, ***HN13*** we must presume that, in organizing the provisions of *§ 523(a)(8)* as it did in BAPCPA, Congress intended each subsection to have a distinct function and to target different kinds of debts.[9]

[*635] We are also unpersuaded by Meridian's reliance on those bankruptcy cases that, perhaps inadvertently, imprecisely quote the provisions of the discharge exception statute as applying to "loans received," as opposed to the "obligation to repay funds received" dealt with by *§ 523(a)(8)(A)(ii)*. See, e.g., *In re Rumer, 469 B.R. at 561* (stating "loans received as an educational benefit, scholarship, or stipend" are excepted from discharge); see also *Beesley v. Royal Bank of Canada (In re Beesley), 2013 Bankr. LEXIS 3811, 2013 WL 5134404 (Bankr. W.D. Pa. Sept. 13, 2013)* (quoting Rumer and its misstatement of the law); *Liberty Bay Credit Union v. Belforte (In re Belforte), 2012 Bankr. LEXIS 4574, 2012 WL 4620987 (Bankr. D. Mass. 2012)* (same). In addition, as observed by the bankruptcy court, the other cases relied upon by Meridian are distinguishable because they all dealt with cases where the debtor actually received funds. See, e.g., *In re Corbin, 506 B.R. at 287*; *Brown v. Rust (In re Rust), 510 B.R. 562, 2014 WL 1796154 (Bankr. E.D. Ky. 2014)*; *Maas v. Northstar Educ. Fin., Inc. (In re Mass), 497 B.R. 863 (Bankr. W.D. Mich 2013)*; *In re Beesley, 2013 Bankr. LEXIS 3811, 2013 WL 5134404*; *In re Belforte, 2012 Bankr. LEXIS 4574, 2012 WL 4620987*; *In re Carow, 2011 Bankr. LEXIS 823, 2011 WL 802847*; *Sensient Techs. Corp. v. Baiocchi (In re Baiocchi), 389 B.R. 828 (Bankr. E.D. Wis. 2008)*. Finally, while we have reviewed the other decisions cited by Meridian that, arguably, reach a different conclusion than we do here, because the courts' analysis and reasoning in those cases is not fully developed, we find them unpersuasive. See *In re Roy, 2010 Bankr. LEXIS 1218, 2010 WL 1523996*; *The Rabbi Harry H. Epstein School, Inc. v. Goldstein (In re Goldstein), 2012 Bankr. LEXIS 6034, 2012 WL 7009707 (Bankr. N.D. Ga. Nov. 26, 2012)*. Simply put, because Debtor did not **[**25]** actually receive any funds, Meridian's debt is not excepted from discharge under *§ 523(a)(8)(A)(ii)*.

VI. CONCLUSION

The bankruptcy court did not err in granting summary judgment to Debtor. We therefore AFFIRM the decision of the bankruptcy court.

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[9] On this point, we agree with Debtor's counsel's statement at oral argument that ***HN14 § 523(a)(8)(A)(ii)*** is not a "catch-all" provision designed to include every type of credit transaction that bestows an educational benefit on a debtor. Instead, this subsection includes a condition, distinct from those in the other subsections of ***§ 523(a)(8)***, that must be fulfilled. In re Hawkins held that this unique requirement, that "funds [be] received" by the debtor, mandates that cash be advanced to or on behalf of the debtor. In light of the many programs available to students which provide cash benefits to **[**24]** students, like veteran's educational benefits, stipends for teaching assignments, and cash scholarships, it is not absurd to assume that Congress intended the scope of ***§ 523(a)(8)(A)(ii)*** to target obligations other than those arising from traditional student loans.

SO ORDERED.

SIGNED this 20th day of April, 2015.

BENJAMIN A. KAHN
UNITED STATES BANKRUPTCY JUDGE

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF NORTH CAROLINA
GREENSBORO DIVISION

In re:	)	
Alice Marie Nightingale,	)	Case No. 13-10834
Debtor.	)	
Alice Marie Nightingale,	)	
Plaintiff,	)	
v.	)	Adversary No. 13-02060
North Carolina State Education Assistance Authority,	)	
Defendant.	)	

MEMORANDUM OPINION DENYING SUMMARY JUDGMENT

This case is before the Court on the Defendant's Motion for Summary Judgment [Adv. No. 13-02060, Doc. #19] filed on November 3, 2014 [Adv. No. 13-02060, Doc. #19] (the "Motion for Summary Judgment"). The Defendant, the North Carolina State Education Assistance Authority ("NCSEAA"), also filed a Brief in Support of its Motion for Summary

Judgment on November 3, 2014 [Adv. No. 13-02060, Doc. #20] ("NCSEAA's Brief"). Plaintiff Alice Marie Nightingale ("Plaintiff" or "Nightingale"), filed a Brief in Opposition to the Motion for Summary Judgment on December 5, 2014 [Adv. No. 13-02060, Doc. # 21] (the "Response").[1] Pursuant to Local Rule 7007-1(d), the Court has considered the Motions on the pleadings, admissible evidence in the record, and motion papers and briefs without hearing or oral argument. On April 1, 2015, the Court entered its Amended Order granting the Motion for Summary Judgment in part, and denying the remainder of the motion.[2] This opinion sets forth the bases for the Court's ruling.

JURISDICTION

This Court has jurisdiction pursuant to 11 U.S.C. § 1334 because this matter arises in a case under title 11. See Harvey v. Dambowsky (In re Dambowsky), Case No. 13-81410, Ap. No. 14-09010, 526 B.R. 590, (Bankr. M.D.N.C. Jan. 6, 2015). This Court has statutory authority pursuant to 11 U.S.C. § 157 and Local Rule 83.11 for the United States District Court for the Middle District of North Carolina. Finally, this Court has constitutional authority to enter final order in this dischargeability action. See In re Dambowsky, 526 at 590.

FACTS

1. On June 25, 2013, Plaintiff Alice M. Nightingale filed a voluntary petition (the "Petition") under Chapter 7 of the United States Bankruptcy Code (the "Code") in this Court [Bankr. No. 13-10834, Doc. #1].

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[1] Although the Response was untimely as initially filed, the Response shall be allowed and will be considered by the Court as ordered on January 21, 2015 in the Court's Order on Show Cause. [Adv. No. 13-02060, Doc. # 27].

[2] There were no factual disputes concerning the status of the Debts as "an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit . . . ." 11 U.S.C. § 523(a)(8)(A)(i). Therefore, the Court granted Defendant partial summary judgment stating the Debts did qualify as Debts exempted from discharge unless it would impose an undue hardship on the debtor.

2. On October 7, 2013, the Court issued an order granting the Plaintiff a discharge (the "Discharge") pursuant to Section 727 of the Code [Bankr. No. 13-10834, Doc. #20]. On October 15, 2013, the Court issued a Final Decree closing the Debtor's Chapter 7 case [Bankr. No. 13-10834, Doc. #22]. The Final Decree was then vacated on October 18, 2013 due to the Plaintiff's forthcoming adversary proceeding regarding the Debts [Bankr. No. 13-10834, Doc. #24].

3. On October 24, 2013, the Plaintiff commenced the current adversary proceeding by filing a Complaint [Adv. No. 13-02060, Doc. #1] (the "Complaint") seeking a discharge of student loan debts (the "Debts") held by the Defendant and College Foundation, Inc. ("CFI"). On October 30, 2013, CFI assigned all of its rights and interests in the Debts to the Defendant [Adv. No. 13-02060, Doc. #10, Exhibit A].

4. According to the Complaint, the exemption of the Debts from the Chapter 7 discharge imposes an undue hardship on the Plaintiff (Complaint ¶ 17) pursuant to 11 U.S.C. § 523(a)(8)(A)(i).

5. The Plaintiff is approximately sixty-six years old and currently resides in Albuquerque, New Mexico. [Adv. No. 13-02060, Doc. #19-3, Exhibit 30J]. She is unemployed as a result of various physical disabilities.[3] She retired from Guilford County Schools in June of 2014 after being on short-term disability. [Adv. No. 13-02060, Doc. #19-2, Exhibit 29N].

6. Between August 2005 and August 2008, the Plaintiff received $48,255.94 (the "Total Principal") in student loans while pursuing a Master's degree in Special Education at the University of North Carolina at Greensboro. [Adv. No. 13-02060, Doc. #19-3, Exhibit 30F;

[3] These disabilities include: chronic fatigue syndrome, obstructive sleep apnea, walking issues, depleted enzymes, hypothyroidism, Reynaud's Syndrome, and high levels of metal in the Plaintiff's blood. [Adv. No. 13-02060, Doc. #19-3, ¶ 13].

Doc. #19-8, Exhibit 47E]. These loans, which have accrued interest and now constitute the Debts, were made by College Foundation Inc. ("CFI"). The loans were backed by the United States Government, and the Plaintiff executed a Federal Stafford Loan Promissory Note on June 5, 2005. [Adv. No. 13-02060, Doc. #19-8, Exhibit 2A].

7. The Plaintiff worked as a teacher at Southeast Guilford High School in Greensboro, North Carolina, while pursuing her Master's degree. Of the Total Principal, $31,925.04 constituted student loan refunds (the "Refunds") that were not applied to the Plaintiff's tuition charges. [Adv. No. 13-02060, Doc. #19-9, Exhibit #1; Doc. #19-8, ¶4]. Instead, the Plaintiff used the Refunds for living expenses and to supplement her income, particularly during the summer months in which she was not working as a teacher. The Plaintiff contributed $19,749 to charity between 2006 and 2013. [Adv. No. 13-02060, Doc. #19-3, Exhibit 30E]. The Plaintiff graduated with her Master's degree in Education in 2011. [Adv. No. 13-02060, Doc. #19-2, Exhibit 29L].

8. The Debts were originally serviced by CFI. On October 30, 2013, CFI transferred the entirety of its rights and interests in the Debts to the Defendant. [Adv. No. 13-02060, Doc. #10, Exhibit A]. As of October 2014, the outstanding amount due on the Debts totaled over $59,000 with interest. [Adv. No. 13-02060, Doc. #19-8, ¶33].

9. The Plaintiff entered into the Income-Based Repayment ("IBR") Program in 2013. [Adv. No. 13-02060, Doc. #19-11, Exhibit #19]. She began making payments under the IBR Program in April of 2013. [Adv. No. 13-02060, Doc. #19-8, ¶31]. Under this program, the Plaintiff made monthly payments, based on her income, of $133.31 towards the Debts. At the time, the Plaintiff was receiving short-term disability income that totaled $26,813.02 annually. [Adv. No. 13-02060, Doc. #19-11, Exhibit 5H].

10. The Plaintiff's payments on the Debts total $11,416.04. Of this, the Plaintiff paid $10,349.56 prior to filing the Complaint. [Adv. No. 13-02060, Doc. #19-8, ¶25].

11. In June of 2014, the Plaintiff experienced a significant decrease in income when she retired and ceased to receive short-term disability payments. Her approximate current monthly income as provided in answers to interrogatories consists of Social Security benefits and state retirement benefits of approximately $1,645.91. [Adv. No. 13-02060, Doc. #19-3, Exhibit #30C]. She receives $820.00 per month in Social Security and $825.91 per month from Guilford County Schools. As of September 29, 2014, as stated also in interrogatories, the Plaintiff's approximate expenses totaled $1,417.00. [Adv. No. 13-02060, Doc. #19-4, Exhibit #30P]. The Plaintiff's current annual income totals $19,750.92.

12. The Plaintiff contends that she does not expect her income to increase in the future due to limited employability. [Adv. No. 13-02060, Doc. #19-3, Exhibit #29T, ¶17].

13. The Complaint asserts that: (i) the Debts impose an undue hardship upon the Plaintiff and (ii) the Debts should be discharged accordingly under Section 523(a)(8) of the Code. (Complaint ¶ 17).

DISCUSSION

Summary judgment is appropriate when the matters presented to the Court "show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(c); Fed. R. Bankr. P. 7056; Celotex Corp. v. Catrett, 477 U.S. 317, 322 (1986). Although a debtor seeking discharge of student loans bears the burden of proving an undue hardship, 11 U.S.C. § 523(a)(8), in considering a motion for summary judgment, the Court must construe the "facts and inferences drawn therefrom in the light most favorable to the non-moving party." Seabulk Offshore, Ltd. v. Am. Home Assur. Co., 377 F.3d

408, 418 (4th Cir. 2001). The party moving for summary judgment has the initial burden of proving the absence of a genuine issue of material fact based on the pleadings, depositions, answers to interrogatories, admissions on file, and affidavits, if any. Celotex, 477 U.S. at 323. Once this initial burden has been met, the nonmoving party must then set forth specific facts sufficient to raise a genuine issue for trial. Matsushita Elect. Indus. Co., Ltd. v. Zenith Radio Corp., 475 U.S. 574, 586-87 (1986). Without weighing the evidence or making findings of fact, the Court must determine "whether the evidence presents a sufficient disagreement to require submission to a jury or whether it is so one-sided that one party must prevail as a matter of law." Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 251-52 (1986). Here, the moving party must demonstrate an absence of any genuine dispute as to any material fact where a material fact is one of those necessary to establish the elements of the cause of the action. Id. at 248. Furthermore, in order to be entitled to summary judgment, the uncontested facts as established by the movant must entitle the movant to judgment. In re Smith, 231 B.R. 130, 134 (Bankr. M.D. Ga. 1999) (when Trustee's statement of facts, though undisputed, came up short of establishing that a preferential transfer occurred, the court could not grant summary judgment; it is the movant's burden to establish all facts necessary to prevail under substantive law). Finally, "[a]lthough the burden is on the Debtor to establish that the student loan debt is dischargeable, the burden is on the Defendant as the moving party to establish an entitlement to summary judgment that the debt is excepted from discharge." In re Macon, Bankr. Case No. 12-42846-PWB, Adv. Pro. No. 13-4014, 2014 WL 5080410 (Bankr. N.D. Ga. October 6, 2014).

Motion for Summary Judgment

I. Dischargeability of Educational Loan Debts Based on the Brunner Standard

In a Chapter 7 bankruptcy case, educational loan debts are excepted from discharge, "unless excepting such debt from discharge . . . would impose an undue hardship on the debtor and the debtor's dependents."[4] 11 U.S.C. § 523(a)(8)(A)(i). The term "undue hardship" is not defined in the Code. As a result, courts have developed various standards and tests to establish when excepting an educational loan debt from discharge would impose an "undue hardship" on an individual Debtor. The Second Circuit first articulated a three-pronged approach in considering the meaning of "undue hardship" in Brunner v. New York State Higher Educ. Servs. Corp.[5] 831 F.2d 395 (2d. Cir. 1987). The Fourth Circuit formally adopted this three-pronged analysis, the "Brunner test," in 2005. Educ. Credit Mgmt. Corp. v. Frushour (In re Frushour), 433 F.3d 393, 398 (4th Cir. 2005). In adopting the Brunner test, the Fourth Circuit explained that "[s]ince Congress did not provide express standards to guide the undue hardship analysis, the Brunner test best incorporates the congressional mandate to allow discharge of student loans only in limited circumstances." Id. at 400.

Undue hardship is found only if a debtor can prove all three of the required prongs by a preponderance of the evidence. In re Frushour at 400 (4th Cir. 2005). The debtor must demonstrate:

> (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

[4] The full statutory provision reads: "A discharge under section 727, 1141, 1228(a), 1228(b), or 1328(b) of this title does not discharge an individual debtor from any debt – (8) unless excepting such debt from discharge under this paragraph would impose an undue hardship on the debtor and the debtor's dependents for – (A)(i) an educational benefit overpayment or loan made, insured, or guaranteed by a governmental unit . . . ." 11 U.S.C. 523(a)(8)(A)(i).

[5]Since its creation by the Second Circuit in 1987, the Brunner test has been adopted by the Third, Fourth, Fifth, Sixth, Seventh, Tenth, and Eleventh Circuit Courts of Appeals. Pa. Higher Educ. Assistance Agency v. Faish (In re Faish), 72 F. 3d 298, 307 (3d Cir. 1995); Educ. Credit Mgmt. Corp. v. Frushour (In re Frushour), 433 F. 3d 393 (4th Cir. 2005); U.S. Dept. of Educ. V. Gerhardt (In re Gerhardt), 348 F.3d 89, 91 (5th Cir. 2003); Oyler v.Educ. Credit Mgmt. Corp. (In re Oyler), 397 F.3d 382 (6th Cir. 2005); Roberson v. Illinois Student Assistance Corp. (In re Roberson), 999 F.3d, 1132, 1135 (7th Cir.1993); Educ. Credit Mgmt. Corp v. Polleys (In re Polleys), 356 F.3d1302, 1309 (10th Cir. 2004); Hemar Ins. Corp. of Am. v. Cox (In re Cox), 338 F.3d 1238 (11th Cir. 2003).

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.

Brunner, 831 F.2d at 396. In applying the Brunner test to a motion for summary judgment, the Defendant, as the movant, must establish material facts about which there are no genuine issues, which would prevent the Debtor from meeting its burden at trial with respect to at least one of the three prongs. None of the facts offered by the Defendant accomplishes this requirement.

II. First Brunner Prong: Can the Plaintiff Maintain a Minimal Standard of Living if Required to Repay the Debts?

The first prong of the Brunner test requires a court to determine whether a Debtor can maintain a minimal standard of living if required to repay his student loan debts. The analysis demands a case-by-case analysis of a debtor's income as compared to his expenses. Matthess v. U.S. Dept. of Educ., 2000 WL 33673763, at *1 (Bankr. M.D.N.C. 2000). The Fourth Circuit instructs that "[a] court should . . . examine the debtor's standard of living, 'with a view toward ascertaining whether the debtor has attempted to minimize expenses of himself and his dependents.'" U.S. Dep't of Health & Human Servs. v. Smitley, 347 F.3d 109, 117 (4th Cir. 2003) (internal citations omitted). A debtor's living situation and expenses are a key part of the minimal expenses analysis. At its core, a minimal standard of living necessitates inquiry as to whether the "debtor's need for care, including food, shelter, clothing, and medical treatment are met." Salinas v. United Student Aid Funds, Inc., 240 B.R. 305 (Bankr. W.D. Wis. 1999).

Plaintiff's income and expenses have fluctuated since filing her Petition. The Motion for Summary Judgment proposes to use the earnings Plaintiff currently receives from retirement benefits as income and does not dispute this amount for the purpose of this Motion for Summary Judgment. [Adv. No. 13-02060, Doc. #19, ¶ 10]. Defendant also presents the Plaintiff's most recently approximated monthly expenses as provided in interrogatories of $1,417.00. [Adv. No.

13-02060, Doc. #19, ¶ 14]. Factors about Plaintiff's living situation, as stated in the Response and numerous times in interrogatories, raise significant doubt that Plaintiff is currently maintaining a minimal standard of living while minimizing her expenses, much less that she would be able to meet minimal standard of living requirements if required to repay the Debts. The Plaintiff reports to currently reside with a friend in New Mexico. She contributes $300.00 per month to her friend's household for rent and utilities. [Adv. No. 13-02060, Doc. #19, Exhibit 30N ¶25]. The sustainability of this arrangement is presently unclear, and whether this arrangement presently would allow the Debtor to maintain a minimal standard of living is unclear. See id. The Plaintiff contends that, if she were to seek her own housing on the private market, her rent and utility expenses would be considerably higher. Additionally, Plaintiff predicts her current medical expenses to increase due to the worsening of medical conditions keeping her from employment.

The Defendant counters that the Plaintiff may repay the loans and avoid undue hardship by seeking one of two repayment options: (1) to resume monthly payments of $133.31; or (2) enter the William D. Ford Program, in which the Plaintiff's required monthly payment on the Debts would be $0.00. [Adv. No. 13-02060, Doc. #19-8, ¶40]. The Defendant asserts that either of these options would afford the Plaintiff the ability to maintain a minimal standard of living while repaying the Debts. This contention, however, is insufficient to entitle the Defendant to summary judgment.

Even if the Court were to assume that the Plaintiff currently would qualify for either of these repayment options, the availability of these options is insufficient to entitle the Defendant to judgment at this stage. The Plaintiff previously participated in an IBR program, in which her monthly payments on the Debts amounted to $133.31. The Defendant contends that the Plaintiff

could resume these payments, which would leave her with a monthly budgetary surplus of approximately $95.00. The Defendant's analysis of the Plaintiff's ability to resume Income-Based Repayments, however, is based on the Plaintiff's current expenses. Her current expense statement reflects her $300.00 rent payment and does not include any provision for increased medical costs. Even if the Court accepted the current income amounts as suggested by the Defendant to be Plaintiff's income amounts, they do not conclusively establish for purposes of summary judgment that the Plaintiff will be able to maintain a minimal standard of living if she is required to pay $133.31 per month on the Debts.

Alternatively, the Defendant contends that the Plaintiff's participation in the William D. Ford Program, in which her monthly repayment amount would be $0.00, cannot and will not affect the Plaintiff's ability to maintain a minimal standard of living. See In re Greene, 484 B.R. 98, 120 (Bankr. E.D. Va. 2013) (finding that "[t]he resulting mathematic reality is that the present required monthly payment of zero on the Student Loan does not impact [Debtor's] ability to maintain a minimal standard of living.").

This Court cannot agree that requiring no payment constitutes "repayment." This Court finds that accepting the concept of a zero payment as constituting "repayment," as asserted by the Defendant and recognized by other courts, see, e.g., id., at 111-116 (concluding that eliminating a zero repayment option would effectively preclude an analysis of the first Brunner prong and therefore the existence of the opportunity to pay zero repayment is instead considered as a factual circumstance in the application of Brunner); Booth v. United States Department of Education (In re Booth), 410 B.R. 672 (Bankr. E.D.Wash. 2009) (distinguishing the undue hardship analysis from the administrative application of the income contingent plan), effectively

eliminates the hardship discharge provision for student loans for those most likely to be entitled to it.

The debtor's choice to enter into an income based repayment plan under which she is not required to may any payments potentially affects both whether the debtor is able to maintain a minimal standard of living if she "repays" her student loans, and whether she has made a good faith effort to repay by simply agreeing to pay nothing. Recognizing that paying nothing cannot possibly affect a debtor's ability to maintain a minimal standard of living, the courts above conclude that the availability of a zero payment plan necessarily demonstrates that a debtor may repay her loans without affecting her ability to maintain a minimal standard of living. See In re Greene, 484 B.R. at 111-112; In re Markwood, 2014 WL 5573437, at *3 (N.D. W.Va 2014).

This Court refuses to jump the logical chasm necessary to conclude that no payment constitutes repayment, regardless of the title that the lenders choose to give to a program that excuses the debtor from repaying her loans. The Brunner test specifically requires that the Court determine whether the debtor would be able to maintain a minimal standard of living if forced to "repay" her student loans. Brunner, 831 F.2d at 396. Participation in such a "repayment" program in which the Plaintiff's monthly payment is zero is not repayment at all; rather, the loan continues to accrue interest on the principal without any repayment. At the end of the twenty-five year period, the Plaintiff's loans may be forgiven, but that amount, on which interest has been accruing, may become taxable as income. See 26 U.S.C. § 61(a)(12); 26 U.S.C. § 108(f); see also In re Geyer, 344 B.R. at 132-33.

Those debtors whose incomes are low enough to qualify for income-based repayments of $0.00 likely are the very individuals the undue hardship exception for student loans is meant to

assist.[6] COMM'N ON THE BANKR. LAWS OF THE U.S., REPORT OF THE COMM'N: PART II, H. DOC. NO. 93-137, at 140–41 (1st Sess. 1973). Obtaining a discharge from a loan of educational debt intentionally requires satisfaction of an unusually high bar, in order to ensure the ongoing viability of various student loan programs. COMM'N ON THE BANKR. LAWS OF THE U.S., REPORT OF THE COMM'N: PART I, H. DOC. NO. 93-137, at 176–77 (1st Sess. 1973). Nonetheless, Congress recognized that exceptional circumstances, "not reasonably within [a debtor's] power," can necessitate and permit a discharge of educational debt. COMM'N ON THE BANKR. LAWS OF THE U.S., REPORT OF THE COMM'N: PART II, H. DOC. NO. 93-137, at 135–36 (1st Sess. 1973). Qualifying for a $0.00 repayment amount certainly indicates difficult financial conditions for an individual debtor, which may be due to such extraordinary situations, which the Debtor will be entitled to demonstrate if able at trial. Regardless, the availability of a "repayment" plan with no payments does not constitute repayment of the loans without imposing an undue hardship which will entitle the Defendant to summary judgment in this case.

Alternatively, the Defendant contends that the Plaintiff could resume making monthly payments of $133.31 towards the Debts under an income-based repayment plan. The record before the Court is insufficient to establish the feasibility of such a payment as a matter of law, and the parties will be entitled to put on evidence at trial regarding these issues, primarily through a review of the Plaintiff's income, expenses, and possible future changes of both.

[6] The Commission on the Bankruptcy Laws of the United States was comprised of "three members appointed by the President of the United States . . . two Members of the Senate . . . two Members of the House of Representatives . . . [and] two [individuals] appointed by the Chief Justice of the United States." Pub. L. No. 91–354 § 2(a) (1970). The Commission "was formed to study, analyze, evaluate, and recommend changes in the substance and administration of the bankruptcy laws of the United States." Kenneth N. Klee, Legislative History of the New Bankruptcy Law, 29 DEPAUL L. REV. 941, 943 (1979).

III. Second Brunner Prong: Do Additional Circumstances Indicate that the Plaintiff's Inability to Repay the Debts is Likely to Exist for the Repayment Period of the Student Loans?

The Fourth Circuit considers the second prong to be the "heart of the Brunner test." In re Frushour, 433 F.3d at 401. It is "prospective in nature," as a court should look for "exceptional circumstances beyond the debtor's current situation" in determining the likelihood of a Plaintiff's continued inability to repay his or her student loan debts. Id. These additional circumstances must be "likely to persist" for a large portion of the Debtor's payment period. Id. (citing Brunner, 831 F.2d at 396). This prong requires the debtor to prove "a total incapacity now and in the future to pay [her] debts for reasons not within [her] control." Rappaport v. Orange Savings Bank (In re Rappaport), 16 B.R. 615, 617 (Bankr. D.N.J. 1981). The circumstances must be severe enough to "render it unlikely that the debtor will ever be able to honor [his] obligations." Burton v. Educ. Credit Mgmt. Corp. (In re Burton), 339 B.R. 856, 870 (Bankr. E.D. Va. 2006) (citing Love v. United States (In re Love), 33 B.R. 753, 755 (Bankr. E.D. Va. 1983)).

In short, the totality of a Debtor's circumstances must establish a "certainty of hopelessness" in regards to the prospect of the Debtor paying her student loan debt in the future. In re Frushour, 433 F.3d at 401 (citing Brightful v. Pa. Higher Educ. Assistance Agency, 267 F.3d 324, 328 (3d Cir. 2001)); Spence v. Educ. Credit Mgmt. Corp. (In re Spence), 541 F.3d. 538, 544 (4th Cir. 2008). Given its demanding standard, this prong requires fact-intensive analysis. Many factors can constitute an "additional circumstance" beyond the Debtor's current situation and control. These include, but are not limited to, the age of the Debtor, the number of dependents a Debtor has, medical conditions, and a lack of usable job skills. Oyler v. Educ. Credit Mgmt. Corp., 397 F.3d 382, 386 (6th Cir. 2005).

In this case, genuine issues of material fact exist regarding circumstances indicative of the Plaintiff's inability to repay the Debts in the future, including how the prognosis of the Plaintiff's health and disability impacts her employment possibilities and income potential. The Fourth Circuit specifically recognizes that "illness [or] disability" may contribute to a Debtor's inability to repay his or her loans in the future. In re Frushour, 433 F.3d at 401 (citing Oyler, 397 F.3d at 386. This standard encompasses ongoing medical issues. Id. However, "substantial and credible evidence" or "corroborating evidence" is required at trial for a Debtor to sustain his or her burden in establishing a medical issue as an additional circumstance under this prong. In re Greene, 484 B.R. at 122. In this case, the Plaintiff's current medical condition and disability comprise a genuine issue of material fact, as the last verified documentation of her health problems is from 2013.[7] In 2012, the Plaintiff's physician attested that the Plaintiff was "temporarily" and "totally disabled." [Adv. No. 13-02060, Doc. #19-8, Exhibit 47A]. Further, the Plaintiff's physical therapist explained that her "intractable pain in both feet . . . has had a very debilitating effect on her quality of life." [Adv. No. 13-02060, Doc. #19-8, Exhibit 46]. The persistence of the Plaintiff's alleged medical conditions and severity of the Plaintiff's disability remain unclear from the facts presented by the Defendant, but as alleged and evidenced by the Plaintiff, including one medical report and an attestation, the illnesses evidenced could persist and in fact worsen as a chronic condition. Therefore, the record before the Court contains sufficient evidence to establish a genuine issue of fact whether Plaintiff's current illnesses will prevent her from working indefinitely and therefore prevent her from making repayments on the Debts.

[7] Dr. Elizabeth Wanek, MD provided a Medical Report for Disability Eligibility Review on May 7, 2012 indicating that the "principal causes" of the Plaintiff's disability included obstructive sleep apnea, hypothyroidism, and fatigue. [Adv. No. 13-02060, Doc. #19-8, Exhibit 47E]. Michael T. Gross, PT, PhD, FAPTA submitted documentation of the Plaintiff's intractable foot pain and inability to walk or stand for long periods of time on August 15, 2013. [Adv. No. 13-02060, Doc. #19-8, Exhibit 46].

Plaintiff also asserts that she is at approximately sixty-six years old and does not "foresee becoming employable, not including ageism." [Adv. No. 13-02060, Doc. #19-3, Exhibit #29T, ¶17]. Age may also be considered as one factor in evaluating the second Brunner prong, although it is rare that a court will accept age as an additional circumstance hindering the debtor's ability to repay his or her loans. See, e.g., Spence v. Educ. Credit Mgmt. Corp. (In re Spence), 541 F.3d. 538, 544 (4th Cir. 2008) (denying undue hardship discharge and finding that sixty-six year old debtor's age did not constitute an additional circumstance, as "neither [the debtor's] ailments nor any other age-related health problems affect her ability to work full time."). Nevertheless, the facts offered by the Defendant are insufficient to a support judgment that the Debtor cannot demonstrate a certainty of hopelessness. The Plaintiff has no dependents and a wide range of job experience, holding both a Bachelor's and Master's degree, indicating possible employability and income potential. The facts offered by the Defendant, however, do not establish for purposes of summary judgment that the Plaintiff will not be able to demonstrate at trial that her situation currently preventing her from employment is hopeless.

IV. Third Brunner Prong: Has the Plaintiff Made Good Faith Efforts to Repay the Loans?

The third prong of the Brunner test requires a fact-intensive inquiry into whether the debtor has made good faith efforts to repay the student loan or loans. Good faith is not explicitly defined in the Code. Several factors can establish the debtor's good faith in this context, but no single factor is dispositive. In re Burton, 339 B.R. at 882 (citing Hall v. U.S. Dep't. of Educ. (In re Hall), 293 B.R. 731, 737 (Bankr. N.D. Ohio 2002) (outlining a "compendium of considerations in determining whether a debtor has made a good faith effort to repay a student loan"). This Court finds that genuine issues of material fact exist as to whether the Plaintiff has made good faith efforts to repay the loans. More precisely, the Defendant has not presented any

facts establishing as a matter of law that the Plaintiff will not be able to demonstrate at trial that she has made good faith efforts to repay the loans.

The Fourth Circuit has outlined how a court should analyze good faith under the third Brunner prong. See In re Frushour, 433 F.3d at 402; see also Educ. Credit Mgmt. Corp. v. Mosko (In re Mosko), 515 F.3d 319, 324 (4th Cir. 2008). In that case, the Fourth Circuit stated that "good faith consists of the debtor's 'efforts to obtain employment, maximize income, and minimize expenses.'" In re Frushour, 433 F.3d at 402. (citing O'Hearn v. Educ. Credit Mgmt. Corp., 339 F.3d 559, 564 (7th Cir. 2003)). Additionally, factors beyond the Debtor's control must cause the hardship. Id.

There is evidence on the record which indicates Plaintiff has made an effort to minimize expenses, including moving to New Mexico and living with a friend, contributing only $300.00 to the household. It is unclear as to the Plaintiff's efforts to find employment, if possible, and maximize her income. It appears that the Plaintiff's move to New Mexico was motivated by her desire to minimize her expenses, but it is uncertain whether this living situation is permanent. The movant has not demonstrated uncontested facts which would require a finding that the Debtor has not made an effort to minimize expenses. This initial good faith inquiry therefore comprises a genuine issue of material fact that precludes summary judgment.

Entry into a loan consolidation or repayment program can constitute evidence that the Debtor has made a good faith effort to repay her loans, and the failure to enter into such a program can indicate the lack of a good faith effort to repay. See Educ. Credit Mgmt. Corp. v. Mosko (In re Mosko), 515 F.3d 319, 324 (4th Cir. 2008). More specifically, "the debtor's effort to seek out loan consolidation options that make the debt less onerous is an important component in the good faith inquiry." In re Frushour, at 402. The participation in such a program

demonstrates the debtor's seriousness in ultimately repaying the obligation. See In re Robinson, 416 B.R. 275 (Bankr. E.D. Va. 2009). In this case, the Plaintiff applied to consolidate six of her loans into one on June 29, 2006. [Adv, No. 13-02060, Doc. # 19-11, Exhibit 5A]. She received further information about consolidation at the beginning of this Adversary Proceeding [Adv. No. 13-02060, Doc. #19-8, Exhibit 43]. The Defendant also provided the Plaintiff with information regarding income-based repayment and income-contingent repayment plans in November of 2013. [Adv. No. 13-02060, Doc. #19-8, Exhibit 44]. The Plaintiff applied to enter an income-based repayment plan in January of 2013. [Adv, No. 13-02060, Doc. # 19-11, Exhibit 5F]. She made payments of $133.31 on the Debts under said income-based repayment plan from April of 2013 until June of 2014. [Adv. No. 13-02060, Doc. #19-9, ¶25, ¶32]. Therefore, there is sufficient evidence on the record to create an issue of material fact as to the Plaintiff's good faith efforts to repay her loan due to her application to, and participation in, these loan repayment plans.

Her actual payments on the student loans serve as another factor that may evidence good faith efforts by the Debtor to repay. Thompson v. N.M. Student Loan Guarantee Corp. (In re Thompson), 329 B.R. 145, 180 (Bankr. E.D. Va. 2005) (citing Hall v. U.S. Dep't. of Educ. (In re Hall), 293 B.R. 731, 737 (Bankr. N.D. Ohio 2002)). These payments can indicate the seriousness with which a debtor takes her loans. Id. The record in this case indicates that the Plaintiff has made sixty-one payments totaling $10,349.56 prior to the filing of this Adversary Proceeding, since August of 2005. [Adv. No. 13-02060, Doc. #19-9, ¶25]. The Plaintiff paid a total of $1,066.48 following the commencement of this proceeding. These payments further indicate the existence of an issue of material fact with respect to the Plaintiff's good faith efforts to repay her loans in this case.

The Defendant claims that the Plaintiff's "substantial charitable contributions" totaling $19,749 between 2006 and 2013 "negligently contributed" to her current situation and constitute bad faith. The Defendant also asserts that the Plaintiff routinely contributed to charity while making minimal payments on the Debts. The Plaintiff explains that she "belongs to a religion" and contributes "to [her] faith on a regular basis." [Adv. No. 13-02060, Doc. #19-8, Exhibit 30E, ¶5]. Further, the Plaintiff intends to continue to donate $50.00 per month to charity. Adv. No. 13-02060, Doc. #19-5, Exhibit 30P]. Further, the Defendant asserts that the Plaintiff's retention of refunds totaling over $31,000 between May 2005 and December 2008, received while she earned a regular income from Guilford County Schools, demonstrates bad faith. While the facts regarding the Plaintiff's charitable contributions are undisputed, they are insufficient in and of themselves to establish bad faith as a matter of law for purposes of summary judgment in this case.

Finally, a Debtor's contact and negotiation with his loan servicer may indicate good faith. Floyd v. Educ. Credit Mgmt. Corp., 54 F. App'x 124 (4th Cir. 2002) (unpublished). This includes regular updates by the Debtor to the loan servicer about the Debtor's financial situation. Id. Exploring other payment options, such as partial payments, and negotiating forbearances also demonstrate that the debtor treats his obligation to repay the loan sincerely. Id. In this case, the Plaintiff claims that she "always stayed in touch with College Foundation [her loan servicer], with unfolding situations, but [she] was never informed of any further options." [Adv. No. 13-02060, Doc. #19-3, Exhibit #30I]. The record includes a letter from the Plaintiff to CFI in January of 2013 exhibiting this contact. [Adv. No. 13-02060, Doc. #19-10, Exhibit #5J]. Therefore, the Plaintiff's application to, and participation in, repayment programs, her payments on the loans, and her contact with the College Foundation, among other factors set forth herein,

are sufficient to create material issues of fact regarding the Plaintiff's good faith efforts to repay her loans.

The issue of Plaintiff's good faith is a mixed question of law and fact. See Krieger v. Educational Credit Management Corp., 713 F.3d 882, 884 (7th Cir. 2013). Moreover, "'undue hardship,' [is] a case-specific, fact-dominated standard . . . ." Id. Under these circumstances, the facts currently in the record are insufficient to establish for purposes of summary judgment that the Plaintiff lacked good faith or that the repayment of her student loans will not cause her undue hardship.

CONCLUSION

For the reasons set forth herein, the Court has entered an Order DENYING the Defendant's Motion for Summary Judgment.

[END OF DOCUMENT]

No. 14-1691

UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

In re ROBERT E. MURPHY,
Debtor

ROBERT E. MURPHY,
Debtor-Appellant
- v.-
U.S. DEPARTMENT OF EDUCATION
EDUCATIONAL CREDIT MANAGEMENT CORPORATION,
Appellee

SALLIE MAE, INC.; COLLEGE BOARD
Interested Parties

ON APPEAL FROM THE DISTRICT COURT FOR THE DISTRICT OF MASSACHUSETTS,
NO. 13-11408

BRIEF OF AMICI CURIAE NATIONAL CONSUMER LAW CENTER AND NATIONAL ASSOCIATION OF CONSUMER BANKRUPTCY ATTORNEYS IN SUPPORT OF APPELLANT AND SEEKING REVERSAL OF THE DISTRICT COURT'S DECISION

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July 29, 2015

CERTIFICATE OF INTEREST AND
CORPORATE DISCLOSURE STATEMENT

Murphy v. U.S. Dept. of Educ. – No. 14-1691

Pursuant to Rule 26.1 of the Federal Rules of Appellate Procedure *Amicus Curiae* the National Consumer Law Center makes the following disclosure:

1) For non-governmental corporate parties please list all parent corporations. **NONE.**

2) For non-governmental corporate parties please list all publicly held companies that hold 10% or more of the party's stock. **NONE.**

3) If there is a publicly held corporation which is not a party to the proceeding before this Court but which has a financial interest in the outcome of the proceeding, please identify all such parties and specify the nature of the financial interest or interests. **NONE.**

4) In all bankruptcy appeals counsel for the debtor or trustee of the bankruptcy estate must list: 1) the debtor, if not identified in the case caption; 2) the members of the creditors' committee or the top 20 unsecured creditors; and, 3) any entity not named in the caption which is an active participant in the bankruptcy proceedings. If the debtor or trustee is not participating in the appeal, this information must be provided by appellant.
NOT APPLICABLE.

/s/John Rao

Dated: July 29, 2015

CERTIFICATE OF INTEREST AND
CORPORATE DISCLOSURE STATEMENT

Murphy v. U.S. Dept. of Educ. – No. 14-1691

Pursuant to Rule 26.1 of the Federal Rules of Appellate Procedure *Amicus Curiae* the National Association of Consumer Bankruptcy Attorneys makes the following disclosure:

1) For non-governmental corporate parties please list all parent corporations. **NONE.**

2) For non-governmental corporate parties please list all publicly held companies that hold 10% or more of the party's stock. **NONE.**

3) If there is a publicly held corporation which is not a party to the proceeding before this Court but which has a financial interest in the outcome of the proceeding, please identify all such parties and specify the nature of the financial interest or interests. **NONE.**

4) In all bankruptcy appeals counsel for the debtor or trustee of the bankruptcy estate must list: 1) the debtor, if not identified in the case caption; 2) the members of the creditors' committee or the top 20 unsecured creditors; and, 3) any entity not named in the caption which is an active participant in the bankruptcy proceedings. If the debtor or trustee is not participating in the appeal, this information must be provided by appellant. **NOT APPLICABLE.**

/s/John Rao

Dated: July 29, 2015

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STATEMENT OF INTEREST OF AMICUS CURIAE

The National Consumer Law Center is a public interest, non-profit legal organization incorporated in 1971. It is a national research and advocacy organization focusing specifically on the legal needs of low income, financially distressed and elderly consumers. The National Association of Consumer Bankruptcy Attorneys (NACBA) is a non-profit organization of more than 3,000 consumer bankruptcy attorneys nationwide. NACBA's corporate purposes include education of the bankruptcy bar and larger community on the uses and misuses of the consumer bankruptcy process. Additionally, NACBA advocates nationally on bankruptcy issues affecting its members and their clients.

As described in the accompanying motion for leave to file a brief in support of appellant, both organizations have a strong interest in student loan issues and the outcome of this case, and believe that their perspective on § 523(a)(8) will assist this Court in developing an undue hardship standard.

STATEMENT UNDER FED. R. APP. P. 29(c)(5)

(a) No party's counsel authored this Amici Curiae Brief in whole or in part;

(b) No party or party's counsel contributed money that was intended to fund preparing or submitting this brief; and

(c) No person, other than the amici curiae, their members, or their counsel, contributed money that was intended to fund preparing or submitting the brief.

SUMMARY OF ARGUMENT

The undue hardship tests of other circuit courts were developed at a time when debtors sought an immediate discharge of student loans in bankruptcy without waiting five or seven years for an automatic discharge the law then provided. Today, borrowers who are seeking discharge of student loans are not jumping the gun on a future automatic discharge. On the contrary, many have already been burdened by the obligations for decades and, if denied a discharge, face a lifetime of crushing debt. Other changes to bankruptcy law and student loan programs suggest that this Court should not be restrained by decisions from other circuits that gave undue weight to concerns that are not pertinent today.

Rather than adopt one existing test over another, we urge this Court to provide a formulation of the undue hardship standard in simple terms, that restricts consideration of extraneous and inappropriate factors not consistent with the statutory language. A finding about whether a debtor's hardship is likely to persist should be based on hard facts, not conjecture and unsubstantiated optimism. Hardship should be assessed based on the debtor's ability to repay student loans based on the loan terms, not twenty-five years into the future under an administrative income-based repayment plan. Consideration of the debtor's good faith, past conduct and life choices simply has no place in an undue hardship

determination and if permitted, results in unnecessary litigation and value-laden, inconsistent judgments.

ARGUMENT

I. Changes To Section 523(a)(8) And Student Loan Programs Have Rendered The *Brunner* Test Obsolete And Compel Consideration Of A New Approach.

The nature of student loan debt, the structure of student loan programs, and the Bankruptcy Code itself have all changed significantly since the undue hardship test adopted by nine circuit courts of appeal was first developed by the Second Circuit in *Brunner v. New York State Higher Educ. Servs. Corp.*, 831 F.2d 395 (2d Cir. 1987). At that time, student loans were automatically dischargeable in bankruptcy, without proving undue hardship, if debtors simply waited five years after their loans first became due. Thus, the overarching concern expressed in virtually all of the seminal decisions was about potential abuse, that debtors may prematurely seek a discharge soon after student loans came due, without demonstrating a sustained period of inability to pay.

This concern was also described in a House Report at the time Congress enacted the five-year waiting period. *See* H.R. Rep. No. 595, 95th Cong., 1st Sess., 133, reprinted in 1978 U.S.Code Cong. & Admin.News 5787, 6094 ("Instead, 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.”).

The harshness of the *Brunner* test understandably can be seen as a reaction to this concern about impetuous filings, as demonstrated by facts of the *Brunner* case itself. Ms. Brunner filed bankruptcy approximately seven months after receiving her Master's degree, and sought to discharge her student loans two months later when they came due. Like all other debtors at the time, Ms. Brunner could have simply waited five years before filing bankruptcy and her student loans would have been discharged. This helps explain why the *Brunner* court and those following *Brunner* added a “good faith” prong to the test despite the lack of any textual basis for it in § 523(a)(8). *See In re Brunner*, 46 B.R. 752, 755 (S.D. N.Y. 1985) (hereinafter “*Brunner I*”) (“good-faith” requirement carries out the intent of § 523(a)(8) to “forestall students ... from abusing the bankruptcy system”).

Amici submit that most debtors today, like Mr. Murphy, are not seeking an undue hardship discharge soon after their student loans come due. A recent empirical study that considered the demographic characteristics of debtors who seek undue hardship discharges found that the mean age of those in the sample was 49 and the median age was 48.5. *See* Iuliano, Jason, “An Empirical Assessment of Student Loan Discharges and the Undue Hardship Standard,” 86 American

Bankruptcy Law Journal 495 (2012). The concern of Congress and courts adopting the *Brunner* test, that debtors seeking a bankruptcy discharge soon after graduating college or ending their studies, is simply no longer relevant.

The early undue hardship cases also reflected a concern about the financial stability of loan programs, particularly when a bankruptcy discharge was sought before the government had an opportunity to collect on the debt. Not only are debtors now seeking discharges long after loans have been made, but the government has been provided extraordinary collection tools that did not exist during the *Brunner* era. In 1991, the Higher Education Act was amended to permit a borrower's wages to be garnished to collect defaulted student loans in an administrative proceeding, without obtaining a court judgment. 20 U.S.C. § 1095a. A Department of Treasury procedure also can be used to collect student loans through the offset of tax refunds. 31 U.S.C. § 3720A. The Debt Collection Improvement Act of 1996 expanded these collection efforts by permitting the offset of Social Security of other government benefits. Pub. L. No. 104-134, 110 Stat. 1321 (1996); 31 U.S.C. § 3716. In 1991, the then-existing six-year statute of limitations for filing collection actions against borrowers, and all other limitation periods for student loan collection, were eliminated. *See* Pub. L. No. 102-26, 105 Stat. 123 (Apr. 9, 1991), amending 20 U.S.C. § 1091a. Collection lawsuits, tax intercepts, wage garnishments, and government benefit offsets may be done at any

time. The only end point is that collection must cease when a borrower dies. 20 U.S.C. § 1091(a)(d). The possibility of debtors avoiding collection during periods when they have an ability to repay their student loans, before seeking a bankruptcy discharge, is another factor not relevant today.

As discussed in Appellant's Supplemental Brief (p. 15), the amount of student loan debt burdening debtors today is significantly greater than in the *Brunner* era. This is caused in part by the substantial increase in the costs of education.[1] It also reflects student loan collection practices, in which interest and collection fees of 25 per cent or more are capitalized during periods of nonpayment, and payments are first applied to accrued interest and fees. A debt of $20,000 can quickly grow to over $50,000. *See*, *e.g*., *In re Martish*, 2015 WL 167154 (Bankr. E.D. N.C. Jan 12, 2015) (after making approximately $39,835 in payments on a consolidation student loan in the original amount of $11,202, debtor still owed $27,021 at time her chapter 13 case was filed).

A 2005 Code amendment expanded the scope of § 523(a)(8) to include student loans made by private lenders that are not subsidized or guaranteed by the government, and which may be denied to borrowers based on creditworthiness. The "undue hardship" language is now applicable to purely private student loans regardless of the terms of the loan or the underwriting criteria. The concern of

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[1] Data on the cost of education compiled by the National Center for Education Statistics are available at: http://nces.ed.gov/programs/digest/d13/tables/dt13_330.10.asp?referral=report.

Brunner and its progeny in protecting the "enlightened social policy" of student loan programs that promise loans to borrowers without considering creditworthiness is also of less relevance today. *Brunner I*, 46 B.R. at 756 ("In return for giving aid to individuals who represent poor credit risks, [§ 523(a)(8)] strips these individuals of the refuge of bankruptcy in all but extreme circumstances.").

The *Brunner* test may have served its purpose in a different time, but it is now obsolete and should not be adopted by this Court.

II. Existing Undue Hardship Tests Stray Too Far From The Plain Language Of Section 523(a)(8) And Test Too Much.

The *Brunner* undue hardship test, and certain incarnations of the totality of the circumstances test (hereafter "totality test"), consider matters not contemplated by the words of the statute. The Second Circuit's review of the statutory language in *Brunner* was cursory at best. Even the lower court's opinion that was largely adopted by the Second Circuit devoted little attention to statutory construction and focused more on policy considerations it believed had motivated Congress. Writing on a clean slate, this Court has the opportunity to take a fresh look at the undue hardship standard, first by considering the meaning of "undue hardship."

The ordinary meaning of "hardship" is a "condition that is difficult to endure," Random House Webster's College Dictionary (2010); "a thing or circumstance that causes ongoing or persistent suffering or difficulty," American

Heritage Dictionary of the English Language (Fifth Ed. 2011). "Undue" is defined as "exceeding what is appropriate or normal." *Id.* It conveys that a matter is significant, as opposed to *de minimis* or insignificant. Together these words refer to a significant, ongoing condition that is difficult for the debtor to endure. Read in the context of the debt dischargeability, the statutory language looks at the present and future financial condition of the debtor and the debtor's dependents and asks the question whether they will endure significant difficulty, such as being unable to maintain a normal standard of living, if the student loan must be repaid rather than discharged. At bottom, if repayment of the student loan would prevent the debtor from satisfying ordinary and necessary living expenses so that a debtor could not effectively "make ends meet," this would be an undue hardship. *See*, *e.g*., *In re Skaggs*, 196 B.R. 865, 868 (Bankr. W.D. Okla. 1996).

This meaning of "undue hardship" is consistent with its application in a similar context. In determining whether recovery of a benefit overpayment should be waived, the Veterans Administration regulations provide that one of the factors that should be considered is "undue hardship." This is defined in the regulation to be: "[w]hether collection would deprive debtor or family of basic necessities." 38 C.F.R. § 1.965(a).

Congress adopted a construct for "undue hardship" in another section of the Code, after *Brunner* was embraced by the circuit courts, that comports with its

ordinary meaning. Section 524(c) has long required that reaffirmation agreements entered into by the debtor must be reviewed, either by the court or through a certification of debtor's attorney, to ensure that the repayment obligation will not impose an "undue hardship on the debtor or a dependent of the debtor." In the 2005 Code amendments, Congress included a presumption to guide bankruptcy courts in applying this undue hardship standard:

> … it shall be presumed that such agreement is an undue hardship on the debtor if the debtor's monthly income less the debtor's monthly expenses as shown on the debtor's completed and signed statement in support of such agreement required under subsection (k)(6)(A) is less than the scheduled payments on the reaffirmed debt.

11 U.S.C. § 524(m)(1).

The test created by the presumption looks solely at the debtor's income and expenses in relation to the payment requirements under the reaffirmed debt. *See, e,g*, *In re Visnicky*, 401 B.R. 61, 63 (Bankr. D. R.I. 2009); *In re Stevens*, 365 B.R. 610, 612 (Bankr. E.D. Va. 2007). Although the context in which "undue hardship" arises under § 524(c) and (m) is different than dischargeability under § 523(a)(8), there is no escaping the fact that Congress used the identical phrase in both sections of the same statute. At a minimum, the presumptive test added in 2005 sheds light on what Congress intends when it uses the phrase "undue hardship" in a statute with respect to the impact of debt repayment on a debtor.

III. The Limited Legislative History of Section 523(a)(8) Suggests A Less Stringent View Of Undue Hardship Than Courts Have Adopted.

Numerous courts have commented that Congress said little about "undue hardship" in the Code's legislative history. *E.g.*, *In re Kopf*, 245 B.R. 731, 736, n.10 (Bankr. D. Me. 2000). The Tenth Circuit observed that "[t]he phrase 'undue hardship' was lifted verbatim from the draft bill proposed by the Commission on the Bankruptcy Laws of the United States." *ECMC v. Polleys*, 356 F.3d 1302, 1306 (10th Cir. 2004). The Commission Report provided a description of undue hardship that Congress may have relied upon in enacting § 523(a)(8). *Brunner I*, 46 B.R. at 754 ("The Commission's report provides some inkling of its intent in creating the exception, intent which in the absence of any contrary indication courts have imputed to Congress."). The Commission Report describes "undue hardship" as follows:

> 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 education debt.
>
> Report of the Comm'n on the Bankr. H.R. Doc. No. 93-137, Pt. II § 4-506 (1973).

Importantly, the Commission Report focuses on the debtor's inability to maintain a minimum standard of living while repaying the loans. It is devoid of stringent terms such as “certainty of hopelessness” or “total incapacity.” *In re Randall*, 255 B.R. 570, 577 (Bankr. D. N.D. 2000) (applying totality of circumstances test and noting that standard involves a “total incapacity both at the time of filing and on into the future to pay one's debts”); *Brunner I*, 46 B.R. at 755 (“dischargeability of student loans should be based upon the certainty of hopelessness”). The Report refers to a debtor maintaining a “minimal standard of living” based on “adequate” income, rather than suggesting the debtor must endure extreme poverty and demonstrate extraordinary circumstances. *In re Courtney*, 79 B.R. 1004, 1010 (Bankr. N.D. Ind. 1987) (suggesting that a debtor must show that an effort to repay would “strip[] himself of all that makes life worth living.”). The Report also focuses on the debtor’s present and future condition. It does not refer to any of the debtor’s pre-bankruptcy past, such as the debtor’s reasons for obtaining the student loans or attempts to repay them.

Courts that require a “certainty of hopelessness,” “total incapacity,” or virtual absence of any expectation of loan repayment by the debtor have strayed too far from the statute’s plain meaning and its legislative history. *Krieger v. Educ. Mgmt. Corp.*, 713 F.3d 882, 884 (7th Cir. 2013) (noting “it is important not to allow judicial glosses, such as the language found in *Roberson* and *Brunner*, to

supersede the statute itself”); *Kopf*, 245 B.R. at 741 (*Brunner* and other similar approaches “test too much”).

IV. This Court Should Provide A Formulation Of The Undue Hardship Standard In Simple Terms Based On The Statutory Language, That Avoids Inconsistent Results And Unnecessary Litigation.

Although the totality of circumstances test (hereafter “totality test”) has been described as a “less restrictive approach” than *Brunner*, *In re Long*, 322 F.3d 549, 554 (8th Cir. 2003), it has not always been applied in a manner that avoids the harshness of *Brunner*. Both tests consider similar financial matters under their first prongs. While the totality test does not expressly incorporate the objectionable aspects of *Brunner's* second and third prongs, they can nevertheless creep back into the totality test under its catch-all third prong that considers “any other relevant facts and circumstances.” This provides an opportunity for the parties to argue, and the court to consider, numerous factors that may not be probative of undue hardship as contemplated by the statutory language. *Polleys*, 356 F.3d at 1309 (under totality test, “courts may choose from a multitude of factors and apply any combination of them to a given case, suggesting that just about anything the parties may want to offer may be worthy of consideration”). The *Brunner* test already is unpredictable and non-uniform; a totality test is likely to be no different. *See In re Speer*, 272 B.R. 186, 191 (Bankr. W.D. Tex. 2001) (“[T]he application of [*Brunner*] standard requires each court to apply its own intuitive sense of what

‘undue hardship’ means on a case by case basis. With so many Solomons hearing the cases, it is no wonder the results have varied.”).

The existing undue hardship tests are far too complex and encourage parties opposing discharge to engage in costly, contested litigation. Rather than adopt one of the existing **tests**, amici urge this Court to describe the undue hardship **standard** in simple terms based on the statutory language. In light of the numerous decisions applying *Brunner* and totality tests, this Court should describe what the undue hardship standard is, and more importantly, what it is not.

The First Circuit B.A.P. has “distilled [undue hardship] to its essence” by noting that it “rests on one basic question: ‘Can the debtor now, and in the foreseeable near future, maintain a reasonable, minimal standard of living for the debtor and the debtor's dependents and still afford to make payments on the debtor's student loans?’” *In re Bronsdon*, 435 B.R. 791, 800 (B.A.P. 1st Cir. 2010).

To the extent the inquiry extends beyond this basic question, we urge the Court to provide guidance on the key considerations as follows.

A. Consideration of the economic factors should focus on whether the debtor can maintain a minimal standard of living while repaying the student loan.

Consideration of the debtor’s financial circumstances is at the core of the undue hardship standard. The amount of the debtor’s income is reviewed in relation to the debtor’s ability to meet necessary expenses. The standard should

not require “abject poverty” or income below a certain threshold, such as the federal poverty guideline. *In re Hornsby*, 144 F.3d 433 (6th Cir. 1998) (debtors did not need to be at poverty level to show undue hardship). In most cases, though, this is not an issue in dispute as the income of debtors who file bankruptcy is far below other Americans.[2]

It is appropriate for the bankruptcy court to consider whether the debtor’s expenses are commensurate with a reasonable, not extraordinary, standard of living. Regardless of whether this is a characterized as a “minimal” standard of living, the focus should be on whether the debtor can pay for basic necessities. Rather than becoming mired in arguments over whether a particular expense is excessive in relation to various shifting standards, a better approach is to focus on certain basic needs of the debtor’s family. The bankruptcy court’s analysis in *In re Ivory*, 269 B.R. 890, 899 (Bankr. N.D. Ala. 2001), serves as useful example of this approach. The court listed what it considered to be the elements of a minimal standard of living. These include decent shelter and utilities, communication services, food and personal hygiene products, vehicles (maintained, insured, and tagged), health insurance or the ability to pay for medical and dental expenses when they arise, some small amount of life insurance, and some funds for

[2] Median household income for debtors filing chapter 7 bankruptcy in 2007 was $23,136. This was 52% below the median household income of $48,200 for the general U.S. population. Lawless, Robert, *et al.*, Did Bankruptcy Reform Fail? An Empirical Study of Consumer Debtors, Am. Bankr. Law J. Vol. 82 , 363 (2008).

recreation. When a borrower's monthly income falls hundreds of dollars below the level at which the debtor could afford to pay for these necessities, courts need not consider arguments over much smaller expenditures for items such as cable television and Internet access. The basic purpose of this inquiry is to ensure that, after debtors have first provided for their basic needs, they do not allocate discretionary income to the detriment of the student loan creditor.

Bankruptcy courts are accustomed to evaluating debtors' expenses for reasonableness under other Code provisions. This process is done when a chapter 7 filing is challenged for abuse under § 707(b) or there is a dispute over whether all of the debtor's projected disposable income is being contributed to a chapter 13 plan in accordance with § 1325(b). In both instances, the court is guided by standards for certain basic living expenses set under the "Collection Financial Standards" used by the Internal Revenue Service in setting repayment terms for delinquent taxpayers. There is nothing unique about the undue hardship standard that warrants a different approach. If there are legitimate disputes about whether the debtor could repay a student loan by limiting unnecessary expenses, courts should make use of the Code's well-established expense standards.

The analysis of current income and expenses must also consider whether the debtor can satisfy basic living expenses while paying student loans. As discussed below, the full current monthly payment required to amortize the loan should be

considered. *In re Fecek*, 2014 WL 1329414 (Bankr. S.D. Ind. Mar. 31, 2014) (using student loan's contractual monthly payment, borrower has nothing left over for expenses typically included in IRS payment standards).

B. Additional or extraordinary circumstances may help the debtor prove undue hardship, but should not be required.

Brunner's second prong, which looks at additional circumstances showing that the hardship is likely to persist, has encouraged courts to create rigid threshold requirements. Often this includes a requirement to show a "certainty of hopelessness" or certain "unique" or "extraordinary" circumstances that look well beyond foreseeable continued financial hardship. Many courts have required that the exceptional circumstances must be something beyond the likely persistence of the debtor's financial problems, and may require proof of serious illness, psychiatric problems, incapacity or disability of a debtor or dependent. This consideration, albeit formulated differently, may appear in the totality test's first and third prongs.

The requirement to show something akin to a "certainty of hopelessness" requires debtors to prove a negative; that a virtually unpredictable course of events will not result in good fortune for the debtor. Life has many twists and turns that are unforeseen, making it impossible to forecast with precision a debtor's condition in ten or twenty years (as some courts have required). The requirement also

suggests a burden of proof much stricter than the preponderance of the evidence standard that applies to hardship determination cases. Such a proof requirement eviscerates the "fresh start" potential inherent in § 523(a)(8)'s allowance for discharge in certain circumstances. *Polleys*, 356 F.3d at1310 (courts need not require a "certainty of hopelessness").

Rather than require some degree of certainty that is simply beyond proof in most cases, the debtor should be required to show that it is more likely than not that the financial difficulties causing undue hardship will continue into the immediate, foreseeable future. The likely persistence of hardship may be due to health problems or physical or mental disability of the debtor or a dependent. But it may also stem from more mundane causes, such as financial barriers that the borrower faces in his or her economic environment. The court should evaluate only realistic expectations rather than speculate concerning improved future prospects.

Although the standard is forward-looking, looking back at the debtor's employment history can help forecast the debtor's realistic future prospects. If the debtor has been stuck in low or modest paying jobs for the past ten or fifteen years, achieved only modest pay increases over that time, maximized her income potential in her field based on education, experience and skills, and there are no more lucrative jobs available to the debtor, only some highly unusual circumstance

would suggest that the condition is not likely to persist. Debtors who despite being in good health and working hard, do not earn enough to pay for basic necessities for their family, should be not be denied a hardship discharge because they cannot show they are disabled or some additional circumstances. Age of the debtor or other factors that limit employment opportunities, or prevent retraining or relocation, are factors to be weighed.

The "future" should not exceed beyond the loan repayment period. *Bronsdon's* focus on the debtor's circumstances "in the foreseeable near future" is noteworthy. Student loan creditors have aggressively pushed courts to consider long-term repayment plans, up to twenty-five years long, as alternatives to bankruptcy discharge. This is inconsistent with bankruptcy law, as addressed below.

The evidence in this case did not support the conclusion of the lower courts that Mr. Murphy, who at trial had been unemployed for the prior thirteen years and was age 63, would have a miraculous change of circumstances allowing him to make the $2,400 per month payments on his student loans.

C. Consideration of lack of good faith or improvident decision-making from the debtor's past should not be part of the undue hardship analysis.

Brunner's third prong requires that the debtor show a good faith attempt to repay the loan. Courts have considered under this prong (as well as under the third

prong of the totality test) whether the debtor made efforts to obtain employment or maximize income, and whether the debtor willfully or negligently caused the default. This requirement looks to the debtor's past conduct.

While initially somewhat narrow in scope, the debtor's good faith has seemingly extended to all prongs of *Brunner* and the third catch-all prong of the totality test. It has morphed into a morality test in which a myriad of the debtor's life choices and past conduct are called into question. Permitting consideration of "good faith" or "other relevant facts and circumstances" has forced debtors to refute arguments by student loan creditors that they should have avoided having too many children (*In re Walker*, 406 B.R. 840, 863 (Bankr. D. Minn. 2009); *Ivory*, 269 B.R. at 911)); should not take prescription drugs to counteract the side effects of mental health medication (*In re Renville*, 2006 Bankr. LEXIS 3211 (Bankr. D. Mont. Jan. 5, 2006)); should not have taken custody of two grandchildren, one of whom was victim of physical abuse (*In re Mitcham*, 293 B.R. 138 (Bankr. N.D. Ohio 2003)); or should not have ended studies without getting a degree so as to care for elderly parents (*In re Bene*, 474 B.R. 56 (Bankr. W.D. N.Y. 2012)).

As previously noted, a good faith consideration lacks foundation in the words of the statute. It is also significant that other subsections of § 523 do in fact make certain debts nondischargeable based on the debtor's past bad conduct. *See,*

e.g., § 523(a)(2)(A)(debts obtained by false pretenses or representations, or actual fraud); § 523(a)(6)(debts based on willful and malicious injury of another or property of another); § 523(a)(9)(debts based on death or injury caused by debtor's operation of a motor vehicle while intoxicated). Except when Congress has expressly provided otherwise in § 523 or in some other Code section, debts are discharged in bankruptcy even when debtors have made mistakes, exercised bad judgment, and engaged in immoral actions. Congress did not make student loan dischargeability turn on questions of good faith or morality, as it did for other debts under § 523.

An open-ended inquiry into decisions the debtor made in the past, based on its subjective nature, inevitably leads to inconsistent results. Good faith should not provide the means for student loan creditors and courts to impose their own values on a debtor's decisions and life choices. To the extent there is some role for a good faith inquiry in the undue hardship standard, it should be limited to questions about the debtor's honesty in relation to the claimed hardship, such as whether the debtor has fabricated or fraudulently portrayed a hardship. Issues related to the debtor's good faith in filing bankruptcy can be addressed by the court under § 707(b) or § 1325(a)(7).

V. The Existence Of Income-Based Repayment Plans Is Irrelevant To The Undue Hardship Determination Under Section 523(a)(8).

Since the early 1990s, federal legislation has authorized various forms of income-based repayment programs for student loan borrowers. The earliest version, known as the "Income-Contingent Repayment Plan" ("ICRP"), allows for potential forgiveness of a student loan after twenty-five years.[3] For the duration of the twenty-five year period the borrower must make monthly payments set at 15% of discretionary income. Discretionary income is defined as the difference between 150% of the applicable HHS poverty guideline and the borrower's current income. If the borrower's income falls below 150% of the poverty guideline, the ICRP monthly payment would be $0.00. In order to have the outstanding student loan debt forgiven, the borrower must annually recertify and comply with all program guidelines for twenty-five years.

A later version of the long-term repayment program, known as "Income-Based Repayment" ("IBR"), has become prevalent since 2007.[4] The IBR allows forgiveness after twenty years. The IBR sets payments at 10% of discretionary income.

Student loan creditors routinely oppose undue hardship discharges by highlighting potential availability of long-term income-based repayment plans.

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[3] 20 U.S.C. § 1098e; 34 C.F.R. § 682.215 and § 685.221.
[4] 20 U.S.C. § 1098e; 34 C.F.R. ¶ § 685.221.

ECMC in this case acknowledges the lower courts' view that the availability of ICRP is not dispositive, but argues that "the undisputed availability of a $0.00 monthly payment further supports the Bankruptcy Court's determination that Murphy did not prove undue hardship." ECMC Brief, p. 13. The role, if any, that the existence of these programs should exert in a court's undue hardship determination has been the focus of extensive litigation in all circuits.

A. An undue hardship standard that appropriately implements section 523(a)(8) must focus on the debtor's ability to make the originally scheduled loan payments.

In considering whether now and in the foreseeable near future the debtor can maintain a reasonable standard of living and at the same time afford to make payments on the student loan, a critical issue any court must address is: what are the student loan "payments" that form the basis for this evaluation? Both *Brunner* and the totality test require that a court evaluate the hardship the debtor is likely to incur if the debtor actually makes payments due on the loan. Neither of these standards assesses "hardship" based on the debtor's making no payments at all. The ICRP argument that ECMC formulated in Mr. Murphy's case cannot be squared with either of the prevailing undue hardship standards.

In determining the appropriate monthly payment amount for the undue hardship assessment, the appropriate place to begin is with Congress's enactment of the operative Code provision in 1978. There were no income-based payment

programs in 1978. Congress could not have intended that courts evaluate undue hardship using payment figures derived from programs that did not exist at the time. Given the clear, absolute five-year discharge option that existed in 1978, any type of long-term repayment program running for twenty-five years would have been irrelevant to the undue hardship determination as envisioned by Congress at the time. Congress has not revisited the undue hardship standard since 1978.

The initial version of the ICRP was developed in 1993. After Congress removed the time-based automatic bankruptcy discharge option in 1998, the undue hardship standard was left as the only discharge option. The legislative history indicates that in 1998 Congress was aware that the long-term payment plans and other options could serve as fallbacks for borrowers who did not qualify for an undue hardship discharge.[5] However, Congress did not repeal the bankruptcy hardship provision; indeed, it expressly stated that it did not intend that these new payment alternatives should displace or in any way change the undue hardship standard drafted into the Code in 1978. According to the relevant 1998 Conference Report addressing the elimination of the time-based automatic discharge," [t]he conferees note that this change does not affect the current provisions allowing any student borrower to discharge a student loan during

[5] Higher Education Amendments of 1998, Conference Report 105-750 (Sept. 25, 1998); 1998 U.S. Code Cong. & Admin. News 404.

bankruptcy if they can prove undue economic hardship."[6] Finally, among the substantial revisions to the Code made in 2005, Congress added § 523(a)(8)(b) to extend the nondischargeability exception to cover private student loans. Here again, Congress did not alter the 1978 language related to the discharge for undue hardship. By this time, the income-based plans had been available for more than a decade.

When Congress created the undue hardship discharge option in 1978, there was no ambiguity about what it meant to make payments on a student loan. As is the case today, students typically executed notes with a fixed repayment period. As is true today, this period was usually ten years. In creating the undue hardship discharge option, Congress clearly referred to the hardship caused by making the payment needed to pay off the loan within the original ten-year amortization period. *See Bene,* 474 B.R. at 73 (opining that today Second Circuit would not define relevant repayment period by reference to long term payment plans); *Polleys*, 356 F.3d at 1310 (under *Brunner*, "inquiry into future circumstances should be limited to the foreseeable future, at most over term of the loan"). Today, just as in 1978, courts must evaluate hardship based on the impact that making payments due under the original note terms will have upon the debtor.

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[6] *Id.*

Courts using the totality test turn to the income-based plans under that test's catch-all third prong. *Brondson*, 435 B.R. at 801. The *Brondson* court recognized, as have all other courts, that participation in a long-term plan is not mandatory and a borrower should not be denied an undue hardship discharge solely because the borrower is not presently enrolled in a plan or did not enroll in one in the past. Instead, the *Brondson* court designated eligibility for a plan as "one of many factors to consider" in the undue hardship evaluation. The court noted that the long-term plans could be harmful for certain borrowers. *Id.* at 802. However, the court also believed that the plans "may be beneficial for a borrower whose inability to pay is temporary and whose financial situation is expected to improve significantly in the future." *Id.* For this latter class of borrowers, the availability of the plans could weigh against the undue hardship discharge.

The *Brondson* court's treatment of income-based plans is problematic. In that court's view, a judge should disregard the debtor's non-participation in long-term repayment program when the participation would harm the debtor. However, when in a court's view participation would help the debtor, such as when the debtor faces only a temporary problem and the debtor's financial situation is expected to improve, the court should give negative weight to the borrower's non-participation. Simply put, this analysis adds nothing to the application of § 523(a)(8). Debtors who face only a temporary hardship and whose financial

situation will improve do not meet the statutory undue hardship standard. There is no need for further elaboration or consideration of the long-term repayment programs. The borrower facing only temporary hardship would fail the "totality of the circumstances" test based on the first two prongs of the test alone.

B. Giving weight to long-term repayment programs conflicts with the Congressional intent to authorize the discharge of student loan debts.

Congress authorized the discharge of student loan debts in bankruptcy. The right to a discharge is limited. However, when a debtor asks to discharge a student loan in bankruptcy, the court must rule on the request by making an undue hardship determination. The court does not make this determination if instead it evaluates the consequences of the debtor's participating in a long-term repayment program. The possibility of forgiveness of debt after twenty or twenty-five years if the debtor complies with all requirements of a repayment plan does not remotely resemble a discharge under the Code. To substitute one for the other conflicts directly with the court's obligation to enforce the Code. *In re Denittis*, 362 B.R. 57, 64-65 (Bankr. D. Mass. 2007); *Kopf*, 245 B.R. at 735. In many ways, the forgiveness option under an ICRP or IBR is the antithesis of a bankruptcy discharge. *In re Booth*, 410 B.R. 672, 676 (Bankr. E.D. Wash. 2009).

Rather than removing a debt burden, the income-based programs almost invariably increase the burden. *In re Wolfe*, 501 B.R. 436, 439 (Bankr. M.D. Fla.

2013). Doubling of the indebtedness under a long-term plan, as would occur in Mr. Murphy's case, is not unusual. This is the opposite of a "fresh start." *In re Dufresne*, 341 B.R. 391 (Bankr. D. Mass. 2006); *In re Brooks*, 406 B.R. 382, 393 (Bankr. D Minn. 2009). Rather than rebuilding credit, the debtor's credit may be poisoned for life. This has a drastic impact not only on the individual's future access to credit, but also on employment opportunities and access to housing. *In re Strand*, 298 B.R. 367, 376 (Bankr. D. Minn. 2003). Decades of mounting indebtedness impose a substantial emotional burden on a person as well. *In re Barrett,* 337 B.R. 896, 903-904 (B.A.P. 6th Cir. 2006), *aff'd* 487 F.3d 353 (6th Cir. 2007); *In re Marshall*, 430 B.R. 809, 815 (Bankr. S.D. Ohio 2010). The bankruptcy discharge provides clear relief from this burden. The long-term plans offer no certainty of relief. Instead, they present a highly speculative option that may provide no relief at all.

Borrowers only obtain a forgiveness of debt if they adhere rigorously to all requirements of an income-based program for its full twenty to twenty-five year duration. Borrowers who default while in a program lose eligibility. 34 C.F.R. §§ 685.221(a)(2), 685.209(a)(ii), 682.215(a)(2). Re-defaults can occur because the income-based plans do not take expenses into account. The formulas that set payments based solely on income do not look at medical expenses, high housing costs, or expenses for any short-term emergency the borrower may encounter. For

twenty to twenty-five years a borrower is one accident away from permanently losing the "discharge" ostensibly available under a long-term repayment plan. Borrowers may also lose eligibility due to paperwork snafus that can occur during the decades of recertification procedures required to maintain participation. 34 C.F.R. §§ 685.209(a)(5)(iii), 685.221(e)(3). Once in default under a plan, the borrower can lose eligibility to participate in another income-based plan. Defaults under plans can be irreparable because the options for removing a loan from default (consolidation, rehabilitation) may be one-time only or (like rehabilitation) burdensome.[7] In sum, it is a mistake to treat commencement of a long-term repayment plan as equivalent to completion of one.

Discharge of a debt in bankruptcy is not a taxable event. However, forgiveness of a student loan debt at the end of an ICRP or IBR is taxable. 26 U.S.C. § 61(a)(12). *Brondson,* 435 B.R. at 802. This *tax* debt is generally not dischargeable in bankruptcy. 11 U.S.C. § 523(a)(1). Therefore, successful completion of a long-term plan may simply see the Internal Revenue Service replace the Department of Education as the powerful creditor pursuing the borrower for several more decades. *In re Barrett,* 487 F. 3d 353, 364 (6th Cir. 2007); *In re Durrani*, 311 B.R. 496, 508 (Bankr. N.D. Ill. 2005) *aff'd* 320 B.R. 357 (N.D. Ill. 2005). Some courts have minimized the tax consequences of non-

[7] *See e.g.* 34 C.F.R. § 685.220(d) (if all the borrower's direct loans have been consolidated, the borrower cannot re-consolidate the same loans to get out of default).

bankruptcy discharge of student loan debt by pointing out the collection of a tax debt may not flow inevitably from ICRP or IBR forgiveness. *In re Brondson*, 421 B.R. 27, 35 -36 (D. Mass. 2009) (collecting cases). These courts opine that the debtor will not suffer harmful tax consequences from the ICRP and IBR discharge decades in the future because the borrower can always claim an insolvency exception to the tax liability. Assuming that this option becomes possible for the perpetually insolvent debtor (considering debtor's equity even in exempt assets), one can only wonder what sense it made to postpone a discharge for twenty-five years. Neither the government nor the debtor benefits from this outcome.[8]

Additionally, income-based plans are not available for private student loans and certain federal student loans. Borrowers with Perkins loans are not eligible for the plans and cannot consolidate them into loans eligible for the plans. Mr. Murphy's loans originated as "Parent PLUS" loans. Bankr. Ct. Op. at 1. Income-based repayment plans are not available for these loans. 34 C.F.R. §§ 685.221(a)(2), 685.209(a)(ii); 682.215(a)(2). By consolidating nine of his twelve Parent PLUS loans to federally guaranteed loans, some of his loans became eligible for the long term plans, while others are not. Not all borrowers are able to obtain even this partial eligibility for income-based plans. Finally, based on their

[8] Courts have not considered the administrative costs to the government, and ultimately taxpayers, in servicing (and recertifying each year for twenty-five years) loans for which there will be no recovery due to borrower's $0.00 payment.

individual circumstances, many borrowers whose loans are potentially eligible for income-based plans cannot apply for them. These include borrowers currently in default, borrowers subject to wage garnishment, and borrowers against whom a judgment has entered.[9]

CONCLUSION

For the foregoing reasons, amici respectfully request that the decision below be reversed.

Respectfully submitted,

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[9] Borrowers in default may consolidate loans in order to seek eligibility for income-based plans. However, the existence of a judgment or garnishment bars consolidation. 34 C.F.R. § 685.220(d)(1)(ii)(B),(C).

CERTIFICATION OF COMPLIANCE WITH TYPE-VOLUME LIMITATION

I hereby certify that the foregoing Brief contains fewer than 6,997 words, excluding the parts of the Brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii). In preparing this certification, I relied on the word-processing system used to prepare the foregoing Brief.

The foregoing Brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because it was prepared in a proportionally spaced typeface using Microsoft Word in 14-point Times New Roman font, except for footnotes and electronic signatures.

Dated: July 29, 2015.

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CERTIFICATE OF SERVICE

I hereby certify that I served the within Brief of Amici Curiae, the National Consumer Law Center and the National Association of Consumer Bankruptcy Attorneys, on counsel for all parties, electronically through the ECF System, on this 29th day of July, 2015.

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Student Loan Options and Chapter 13 Bankruptcy

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Educational Debt Levels in 2015

- $1.18 Trillion outstanding in Q1 2015
  - Auto loans: $968 billion
  - Credit cards: $685 billion
- 43 million Americans owe educational debt

Average Debt Loads

- 2013 undergraduate: $27,300
  - 70% of 2013 graduates have student loan debt.
- 40% of student loans are borrowed for graduate or professional school.
  - 2013 law school: $141,000
  - 2013 medical school: $162,000

Average Debt at NC Law Schools: 2014 class

Charlotte	$140,528
Elon	$132,444
Duke	$125,406
Wake Forest	$107,532
UNC-CH	$ 92,475
Campbell	$ 90,065
NCCU	$ 58,061

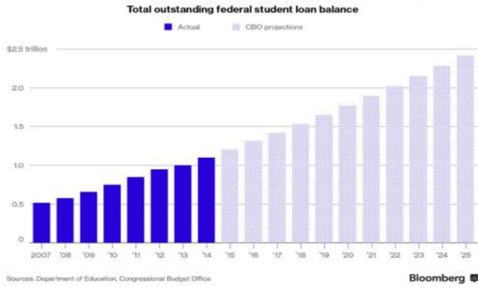
Default and Delinquency Rates

- Delinquent = borrower has missed 1 payment
- Default = status after 9 months of delinquency

- Q1 2015: 11.1% 90+ days delinquent or in default
  - 11.3% in Q3 2014
  - 11.5% in Q4 2013

Class of 2009

- 8.8% had defaulted by the end of 2010.
- Only 17% of the original debt had been paid down after five years.
- More than 20% of high balance borrowers owe more than when they graduated.



What is a Student Loan?

In the bankruptcy context, absent an "undue hardship", 11 U.S.C. § 523(a)(8)(A) makes non-dischargeable "an educational benefit overpayment or loan made, insured or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution, or … an obligation to repay funds received as an educational benefit, scholarship or stipend…

This describes the government guaranteed student loans.

What is a Student Loan?

Following BAPCPA, under 11 U.S.C. § 523(a)(8)(B) "any other educational loan that is a qualified education loan, as defined in section 221(d)(1) of the Internal Revenue Code of 1986, incurred by a debtor who is an individual.

This describes the private student loans, but those must meet the requirements of the Internal Revenue Code at 26 U.S.C. § 221(d).

When is a Private Student Loan Non-Dischargeable?

(d) Definitions For purposes of this section—

(1) Qualified education loan The term "qualified education loan" means any indebtedness incurred by the taxpayer solely to pay qualified higher education expenses—

(A)which are incurred on behalf of the taxpayer, the taxpayer's spouse, or any dependent of the taxpayer as of the time the indebtedness was incurred,

(B)which are paid or incurred within a reasonable period of time before or after the indebtedness is incurred, and

(C)which are attributable to education furnished during a period during which the recipient was an eligible student.

Such term includes indebtedness used to refinance indebtedness which qualifies as a qualified education loan. The term "qualified education loan" shall not include any indebtedness owed to a person who is related (within the meaning of section 267(b) or 707(b)(1)) to the taxpayer or to any person by reason of a loan under any qualified employer plan (as defined in section 72(p)(4)) or under any contract referred to in section 72(p)(5).

(2) Qualified higher education expenses The term "qualified higher education expenses" means the cost of attendance (as defined in section 472 of the Higher Education Act of 1965, 20 U.S.C. 1087ll, as in effect on the day before the date of the enactment of the Taxpayer Relief Act of 1997) at an eligible educational institution, reduced by the sum of—

(A)the amount excluded from gross income under section 127, 135, 529, or 530 by reason of such expenses, and

(B)the amount of any scholarship, allowance, or payment described in section 25A(g)(2).

For purposes of the preceding sentence, the term "eligible educational institution" has the same meaning given such term by section 25A(f)(2), except that such term shall also include an institution conducting an internship or residency program leading to a degree or certificate awarded by an institution of higher education, a hospital, or a health care facility which offers postgraduate training.

When is a Private Student Loan Dischargeable?

Hours could be spent parsing these section of the Bankruptcy and Internal Revenue Codes, but just few examples:

While 11 U.S.C.S. § 523(a)(8)(A)(ii) provides that a bankruptcy discharge will discharge claims received as an educational benefit, scholarship, or stipend, to be excepted from discharge under this subsection, a creditor must demonstrate that the debtor is obliged to repay a debt for **"funds received"** for the educational benefits. 11 U.S.C.S. § 523(a)(8)(A)(ii) is not a ''catch-all'' provision designed to include every type of credit transaction that bestows an educational benefit on a debtor. Instead, this subsection includes a condition, distinct from those in the other subsections of § 523(a)(8), that that funds **be received by the debtor**. *Inst. of Imaginal Studies v. Christoff (In re Christoff)*, 527 B.R. 624 (9th Cir. BAP February 19, 2015).

Or consider that 26 U.S.C. § 221(d) defines the term "qualified education loan" as "any indebtedness incurred by the taxpayer **solely** to pay qualified higher education expenses …which are incurred on behalf of the taxpayer, the taxpayer's spouse, or **any dependent of the taxpayer as of the time the indebtedness was incurred**…." (Emphasis added.) If the loan was incurred for reasons beyond only higher education or were incurred for a child that was no longer a dependent, such would not be a "qualified education loan", private or otherwise.

Types of Federal Loans

- **William D. Ford Federal Direct Loan Program ("Direct Loan")**

34 C.F.R. §685

Only option as of July 2010.

- **PLUS Loan**

34 C.F.R. §685

Credit Based Loans for Parent or Graduate Student.

- **Perkins Loan**

34 C.F.R. §674

Administered by the school for exceptional financial need.

Types of Federal Loans (Discontinued)

- **Federal Family Education Loan Program (**“FFEL”)

34 C.F.R. §682

Discontinued as of July 2010.

- **Health Education Assistance Loan Program (“HEAL”)**

42 C.F.R. §60

Discontinued in 1998.

Obtaining Information About Federal Loans

Information about federal student can best be obtained from the National Student Loan Data System, which is the central database for student aid. It receives data from schools, agencies that guarantee loans, the Direct Loan Program, the Federal Pell Grant Program, and other United States Department of Education programs.

It is available online at:

https://www.nslds.ed.gov

Obtaining Information About Federal Loans

The Department of Education has repeatedly stated that only the borrower is allowed to access this information.

Attorneys for borrowers are not exempted from this restriction, making it necessary for the borrower to either print out the information or save it as a pdf screenshot.

Obtaining Information About Federal Loans

Alternatively, borrowers can download NSLDS data into a readable file:
- Log in at StudentAid.gov.
- Click or touch "MyStudentData Download."
- Click or touch "Confirm."
- Specify a file location for saving and downloading (i.e., designate to what location on your computer you want to save the file). If you are using a mobile device, your data may open in a new window or it may download, depending on your device.
- The file will download to the specified location.

Sample Information

- File Source:U.S. DEPARTMENT OF EDUCATION, NATIONAL STUDENT LOAN DATA SYSTEM (NSLDS)
- File Request Date:2014-07-01-10.51.27.075
- Student First Name:YPSILANTI
- Student Middle Initial:A
- Student Last Name:CURRUTHERS
- Student Street Address 1:123 WINDING WAY
- Student Street Address 2:APT. 1014
- Student City:BEDFORD FALLS
- Student State Code:NY
- Student Country Code:US
- Student Zip Code:55501
- Student Email Address:yacurruthers@ns.edu
- Student Home Phone Country Code:001
- Student Home Phone Number:7035551212

Sample Information

- Student Home Phone Preferred:No
- Student Cell Phone Country Code:001
- Student Cell Phone Number:7035551313
- Student Cell Phone Preferred:Yes
- Student Work Phone Country Code:001
- Student Work Phone Number:7035551414
- Student Work Phone Preferred:No
- Student SULA MEP Program School Name:NORTH SOUTH UNIVERSITY
- Student SULA MEP Program Enrollment Status:FULL TIME
- Student SULA MEP Program CIP Title:Urban Forestry.
- Student SULA MEP Program Credential Level:BACHELOR'S DEGREE
- Student SULA MEP Program Begin Date:08/15/2013
- Student SULA MEP Program Length In Years:4.0
- Student SULA Maximum Eligibility Period:6.0

Sample Information

- Student SULA Subsidized Usage Period:1.0
- Student SULA Remaining Eligibility Period:5.0
- Student Enrollment Status:FULL TIME
- Student Enrollment Status Effective Date:08/15/2013
- Student Total All Loans Outstanding Principal:$30,476
- Student Total All Loans Outstanding Interest:$99
- Student Pell Lifetime Eligibility Used:4.511%
- Student Total All Grants:$553
- Total DIRECT STAFFORD SUBSIDIZED (SULA ELIGIBLE) Outstanding Principal:$12,000
- Total DIRECT STAFFORD SUBSIDIZED (SULA ELIGIBLE) Outstanding Interest:$200
- Loan Type:DIRECT STAFFORD SUBSIDIZED (SULA ELIGIBLE)
- Loan Award ID:*****6789012345678901
- Loan Attending School Name:NORTH SOUTH UNIVERSITY
- Loan Attending School OPEID:00301000

Sample Information

- Loan Date:08/15/2013
- Loan Repayment Begin Date:12/01/2018
- Loan Period Begin Date:08/15/2013
- Loan Period End Date:05/20/2014
- Loan Amount:$8,500
- Loan Disbursed Amount:$8,500
- Loan Canceled Amount:$0
- Loan Canceled Date:
- Loan Outstanding Principal Balance:$8,500
- Loan Outstanding Principal Balance as of Date:07/01/2014
- Loan Outstanding Interest Balance:$100
- Loan Outstanding Interest Balance as of Date: 07/01/2014
- Loan Interest Rate Type:VARIABLE

Sample Information

- Loan Repayment Plan Begin Date: 12/01/2018
- Loan Repayment Plan Scheduled Amount:$8,500
- Loan Confirmed Subsidy Status:Subsidized
- Loan Subsidized Usage In Years:1.0
- Loan Status:ID
- Loan Status Description:IN SCHOOL OR GRACE PERIOD
- Loan Status Effective Date:08/20/2013
- Loan Disbursement Date:08/15/2013
- Loan Disbursement Amount:$7,000
- Loan Contact Type:Current ED Servicer
- Loan Contact Name:DEPT OF ED/SERVICER
- Loan Contact Street Address 1:633 SPIRIT DRIVE
- Loan Contact City:CHESTERFIELD
- Loan Contact State Code:MO
- Loan Contact Zip Code:63005

Obtaining Information About Private Loans

Information about private student loans can be obtained from credit reports or through a FDCPA verification letter.

Differences Between Federal & Private Student Loans

Statute of Limitations	
Federal	Private
There is no Statute of Limitations for Federal Student Loans.	Private Student Loans are subject to a Statute of Limitations. This may be determined by the contract or by state law.

Differences Between Federal & Private Student Loans

Debt Collection	
Federal	Private
The federal government and its debt collectors can collect through: • Intercept Tax Refunds • Administrative Wage Garnishment • Lawsuit and Judgment Collection	Private Student lenders can collect through: • Lawsuit and Judgment Collection

Differences Between Federal & Private Student Loans

Debt Collection	
Federal	Private
The federal government has a limited list of debt collection agencies that can be found at: https://studentaid.ed.gov/sa/about/data-center/business-info/contracts/collection-agency	Private Student lenders can hire any collection agency.

Differences Between Federal & Private Student Loans

Repayment Options	
Federal	Private
The federal government has panoply of repayment options, including standard, extended and assorted income drive plans.	Private Student lenders have not mandatory repayment options other than the contract or a negotiated settlement.

Differences Between Federal & Private Student Loans

Forbearance	
Federal	Private
Federal loans may be placed in forbearance for a variety of reasons, including economic hardship, unemployment, military service, etc.	Private Student lenders generally do not have explicit forbearance programs, but can agree to such.

Differences Between Federal & Private Student Loans

Bankruptcy Discharge	
Federal	Private
Both federal and private student loans are subject to discharge if repayment would constitute an "undue hardship", generally under the *Bruner* test. (Which is beyond the scope of this talk.)	

Differences Between Federal & Private Student Loans

Bankruptcy Discharge	
Federal	Private
It is worth noting that while 11 U.S.C. § 523(a)(8) did not define "undue hardship", a definition was provided by BAPCPA in 11 U.S.C. § 524(m): It shall be presumed that such agreement is an undue hardship on the debtor if the debtor's monthly income less the debtor's monthly expenses as shown on the debtor's completed and signed statement in support of such agreement required under subsection (k)(6)(A) is less than the scheduled payments on the reaffirmed debt. This presumption shall be reviewed by the court.	

Differences Between Federal & Private Student Loans

Bankruptcy Discharge	
Consequences	
Federal	Private
Student loans discharged in bankruptcy are not included taxable income. *See* IRS Form 982.	

Differences Between Federal & Private Student Loans

Cancellation	
Death	
Federal	Private
The obligation to repay federal loans ends with the borrower's death or, for Parent Plus loans, the death of the student.	Private loans are also discharged by the death of the borrower, but not necessarily for the co-borrower.
Federal loans cannot collect from the decedent's estate.	Private student loans can collect from the decedent's estate.

Differences Between Federal & Private Student Loans

Cancellation	
Disability	
Federal	Private
A determination by the Social Security or Veteran's Administrations that the borrower is "totally and permanently disabled" can result in an administrative discharge, if the condition persist for at least 3 years.	Private loans have no requirement of forgiveness due to disability.

OMB No. 1845---0065
Form Approved
Exp. Date 6/30/2016

DISCHARGE APPLICATION: TOTAL AND PERMANENT DISABILITY
IMPORTANT INFORMATION

TPD---APP

- **William D. Ford Federal Direct Loan Program**
- **Federal Family Education Loan Program**
- **Federal Perkins Loan Program**
- **TEACH Grant Program**

READ THIS FIRST

- This is an application for a total and permanent disability discharge of your William D. Ford Federal Direct Loan (Direct Loan) Program, Federal Family Education Loan (FFEL) Program, and/or Federal Perkins Loan (Perkins Loan) Program loan(s), and/or your Teacher Education Assistance for College and Higher Education (TEACH) Grant Program service obligation.
- You only need to submit a single application to the U.S. Department of Education to apply for discharge of all of your Direct Loan, FFEL, and/or Perkins Loan program loans and your TEACH Grant service obligations. **Throughout this application, the words "we," "us," an "our" refer to the U.S. Department of Education.**
- To qualify for this discharge, you must meet **one** of the following requirements:
  1. You are a veteran who has been determined by the U.S. Department of Veterans Affairs (VA) to be **unemployable due to a service---connected disability**, and you provide documentation from the VA of that determination;

     OR
  2. You have received a Social Security Administration (SSA) notice of award for Social Security Disability Insurance (SSDI) or Supplemental Security Income (SSI) stating that **your next scheduled disability review will be 5 to 7 years or more from the date of your last SSA disability determination**, and you provide a copy of that SSA notice of award.

     OR
  3. You provide a certification from a physician in Section 4 of this Discharge Application that you are unable to engage in any substantial gainful activity (see definition in Section 5) by reason of a medically determinable physical or mental impairment that:
     - Can be expected to result in death;
     - Has lasted for a continuous period of not less than 60 months; or
     - Can be expected to last for a continuous period of not less than 60 months.
- If you do not meet requirement #1 or requirement #2, you may qualify for discharge by obtaining a certification from a physician in Section 4 of this application, as described above for requirement #3. If you can provide the documentation to show that you meet requirement #1 or #2 above, you are **not** required to have a physician complete Section 4.

Differences Between Federal & Private Student Loans

Cancellation	
Closed School	
Federal	Private
If the school the borrower attended closed while the borrower enrolled or within 120 days of withdrawal, the loans **may** be cancelled.	Private loans have no obligation to be cancelled if the school closes.

Differences Between Federal & Private Student Loans

Cancellation	
False Certification	
Federal	Private
Federal loans may be cancelled under some circumstances for false certification by the school of the borrower's ability to benefit from training or other identity theft.	Private loans are subject to identity theft protections, but do not have to cancel loans for training that could not provide any benefit.

Differences Between Federal & Private Student Loans

Cancellation	
Consequences	
Federal	Private
Cancellation of both federal and private student loans will result in a the cancelled amount of the loan being reported as income for tax purposes.	

Differences Between Federal & Private Student Loans

Forgiveness	
Public Service Loan Forgiveness	
Federal	Private
An borrower employed by the government or a 501(c)(3) can have Direct Loans forgiven after making 120 payments, including under an IDR.	None.

Differences Between Federal & Private Student Loans

Forgiveness	
Teacher Loan Forgiveness	
Federal	Private
A full-time teacher at a low-income school can have $17,500 of Direct or FFEL loans forgiven.	None.

Differences Between Federal & Private Student Loans

Forgiveness	
Consequences	
Federal	Private
Forgiven loans are not reported as taxable income.	Not applicable.

Defaulted Federal Loans

Default
Definition
No Payments for more than 270 days.
Consequences
• The entire unpaid balance is due and payable. • Loss of eligibility for *deferment*, *forbearance*, and repayment plans. • Loss of eligibility for additional *federal student aid*. • Loan is assigned to a collection agency. • The loan will be reported in default to credit bureaus • Intercept of tax refunds. • Balance will increase because of the late fees, additional interest, court costs, collection fees, attorney's fees, and any other costs associated with the collection process. • Administrative wage garnishment. • Commencement of legal action. • Possible Suspension of Professional or Driver's Licenses.

Solutions for Defaulted of Federal Loans

Settlement
The Department of Education, its Guaranty Agencies and Debt Collectors **may** accept a lump sum settlement but are not **required** to accept such a settlement.
Settlement of student loans will result in the cancelled amount being reported as taxable income.

Solutions for Defaulted of Federal Loans

Settlement
FFEL and Perkins Loans
Collection costs can be waived.
30% of principal and interest can be waived.
If a guaranty agency chooses to compromise more than 30%, it cannot waive the Department's right to collect the rest.

Solutions for Defaulted of Federal Loans

Settlement

Direct Loans

- Waiver of Collection Costs: Payment of the current principal and interest (waiver of collection costs/fees).

Example: Borrower owes $2500.00 Principal, $ 1000.00 Interest, and $875.00 projected collection fees. The collector may offer the borrower a settlement as low as $3500.00 (Principal and Interest) to fully satisfy the account.

- Principal and Half Interest: Payment of at least the current principal and 50% of interest.

Example: Borrower owes $2000.00 Principal, $1000.00 Interest and $730.20 projected collection costs. The collector may offer the borrower a settlement as low as $2,500.00 (principal + 50% interest) to fully satisfy the account.

- 90% principal and interest: Payment of at least 90% of the current principal and interest balance.

Example: Borrower owes $2000.00 Principal, $400.00 Interest and $584.16 projected collection costs. The collector may offer the borrower a settlement as low as $2160.00 (90% of principal + interest) to fully satisfy the account.

Solutions for Defaulted of Federal Loans

Settlement

The examples were taken directly from the 2009 Department of Education Private Collection Agency ("PCA") Manual and in all three, appear to authorize waiver of collection costs.

In addition to these standard compromises, the PCA Manual authorizes discretionary compromises for financial hardship with the prior approval of the Department of Education.

Solutions for Defaulted of Federal Loans

Consolidation

Consolidation is essentially a refinancing of all existing student loans into one Direct Loan.

In something of an oxymoron, a single loan can be consolidated.

The borrower must agree to repay the consolidated loan under an Income Driven Repayment Plan.

The Interest Rate for the new consolidated loan will be a weighted average of the previous loans.

Consolidation may include collection costs of up to 18.5% of the principal and interest outstanding on the defaulted loan.

Default on Student Loans can only be cured once through consolidation, unless other loans are later consolidated.

Consolidation generally takes 30-90 days.

Solutions for Defaulted of Federal Loans

Rehabilitation
Rehabilitation requires the borrower to make nine (9) payments in ten (10) months.
Payments must be reasonable and affordable, based on review and IDR.
Payments made through Administrative Wage Garnishment do not count.
Nor does the Administrative Wage Garnishment stop until five (5) payments have been made.
Consolidation may include collection costs of up to 18.5% of the principal and interest outstanding on the defaulted loan.
Default on Student Loans can only be cured once through consolidation, unless other loans are later consolidated.

Solutions for Defaulted of Federal Loans

Chapter 13
11 U.S.C. § 1322(b)(3) provides that "the plan may … provide for the curing or **waiving** of **any default**." (Emphasis added.)
"Any default" should include student loan or even a default under a rehabilitation.
"Curing", which generally means catching up on missed payments, must mean something different from "waiving", which implies forgiving of missed payments.
11 U.S.C. § 1322(b)(5), which routinely is used to allow the cure and maintenance of mortgage payments, specifically allows the same treatment for "any unsecured claim … on which the last payment is due after the date on which the final payment under the plan is due", which would include non-dischargeable student loans.
Such a cure or waiver could avoid the assessment of collection costs of up to 18.5% of the outstanding principal and interest.
It should be expected that such a plan would face vigorous opposition from the Department of Education and heightened judicial scrutiny.

Federal Loan Repayment Options

- Standard Repayment
  - Term of up to 10 years
- Graduated Repayment
  - Term of 10 years
  - Amount steps up every two years.
- Extended Repayment
  - Balance of over $30k
  - Term of up to 25 years
- Extended Graduated Repayment
  - Balance of over $30k
  - Term of up to 25 years
  - Amount steps up every two years.

Federal Loan Repayment Sample

Original Loan Amount (3.4% Interest Rate)	$25,000	$50,000	$100,000
Standard	$246	$492	$984
Graduated	$159	$318	$636
Extended	N/A	$248	$743
Extended Graduated	N/A	$142	$283

Federal Loan Repayment Options Income Driven Repayment Plans

- Income Contingent Repayment (ICR)
- Income Based Repayment (IBR)
- Pay As You Earn (PAYE)

Federal Loan Repayment Options Income Contingent Repayment Plans

- Based solely on 15% of disposable income and loan balance.
- Assets are not relevant.
- Direct Loans only.
- Parent Plus cannot have ICR, unless consolidated.
- Economic Hardship Deferments count towards 25 years.
- Balance cancelled after 25 years.
- Cancelled amount may be taxable income.

Federal Loan Repayment Options
Income Based Repayment Plans

- Based solely on 15% of disposable income and loan balance.
- Family size includes all people supported at least half-time regardless of tax status or physical custody.
- If married and file joint tax return, both incomes are used in the calculation, if separate tax returns, only the borrower's income is used in the calculation.
- Assets are not relevant.
- IBR Repayment must be less than Standard Repayment to qualify.
- Direct Loans only.
- Parent Plus cannot have IBR, even if consolidated.
- Economic Hardship Deferments count towards 25 years.
- Balance cancelled after 25 years.
- Cancelled amount may be taxable income.

Federal Loan Repayment Options
PAYE Plans

- Based solely on 10% of disposable income and loan balance.
- Family size includes all people supported at least half-time regardless of tax status or physical custody.
- If married and file joint tax return, both incomes are used in the calculation, if separate tax returns, only the borrower's income is used in the calculation.
- Assets are not relevant.
- IBR Repayment must be less than Standard Repayment to qualify.
- Direct Loans originated after October 2011 only.
- Economic Hardship Deferments count towards 25 years.
- Balance cancelled after 20 years.
- Cancelled amount may be taxable income.
- Recently revised with the REPAYE Plan.

Federal Loan Repayment Options
Public Service Loan Forgiveness

- Work for a "qualifying employer" specifically a governmental unit or a 501(c)(3) non-profit.
- Make 120 "qualifying payments" under IBR/ICR/PAYE or Standard Repayment after July 2007.
- Balance forgiven, tax-free, after 120 payments.
- Teachers can have $17,500 in loans forgiven after teaching math, science or special ed in qualifying schools for 5 consecutive years. Other teachers can have $5,000 forgiven.

Federal Loan IBR Repayment Sample

	Total Household Income		
Household Size	$25,000	$50,000	$100,000
1	$50	$420	$1,050
2	$0	$350	$970
3	$0	$280	$900
4	$0	$210	$830

Federal Loan Repayment Calculation

- To calculate the various student loan repayment options, go to:

https://studentloans.gov/myDirectLoan/mobile/repayment/repaymentEstimator.action

Participation in IDR and Chapter 13

- Previously the Department of Education, its Guaranty Agencies and Student Loan Servicers would place all student loans for Chapter 13 Debtors in administrative forbearance.
- This meant that no collection actions were taken, but interest continued to accrue.
- Accordingly, $100,000 of student loans at 8% interest will grow to $148,984.57 at the end of a 60-month Chapter 13 Plan.
- The “fresh start” becomes a “false start.”

Participation in IDR and Chapter 13

- The Department of Education had refused to allow Chapter 13 Debtors to participate in the various income driven repayment plans.
- When pressed with the argument that 11 U.S.C. § 525(c) prohibited such discrimination, the Department of Education consented to allowing Chapter 13 Debtors to participate in IDRs if Chapter 13 Plans contained the following provisions from the *Buchanan* case:

Buchanan Provisions

- The Debtor is not seeking nor does this Plan provide for any discharge, in whole or in part, of her student loan obligations.
- The Debtor shall be allowed to seek enrollment in any applicable income-driven repayment ("IDR") plan with the U. S. Department of Education and/or other student loan servicers, guarantors, etc. (Collectively referred to hereafter as "Ed"), without disqualification due to her bankruptcy.
- Ed shall not be required to allow enrollment in any IDR unless the Debtor otherwise qualifies for such plan.
- The Debtor may, if necessary and desired, seek a consolidation of her student loans by separate motion and subject to subsequent court order.
- Upon determination by Ed of her qualification for enrollment in an IDR and calculation of any payment required under such by the Debtor, the Debtor shall, within 30 days, notify the Chapter 13 Trustee of the amount of such payment. At such time, the Trustee or the Debtor may, if necessary, file a Motion to Modify the Chapter 13 Plan to allow such direct payment of the student loan(s) and adjust the payment to other general unsecured claims as necessary to avoid any unfair discrimination.
- The Debtor shall re-enroll in the applicable IDR annually or as otherwise required and shall, within 30 days following a determination of her updated payment, notify the Chapter 13 Trustee of such payment. At such time, the Trustee or the Debtor may, if necessary, file a Motion to Modify the Chapter 13 plan to allow such direct payment of the student loan(s) and adjust the payment to other general unsecured claims as necessary to avoid any unfair discrimination.
- During the pendency of any application by the Debtor to consolidate her student loans, to enroll in an IDR, direct payment of her student loans under an IDR, or during the pendency of any default in payments of the student loans under an IDR, it shall not be a violation of the stay or other State or Federal Laws for Ed to send the Debtor normal monthly statements regarding payments due and any other communications including, without limitation, notices of late payments or delinquency. These communications may expressly include telephone calls and e-mails.
- In the event of any direct payments that are more than 30 days delinquent, the Debtor shall notify her attorney, who will in turn notify the Chapter 13 Trustee, and such parties will take appropriate action to rectify the delinquency.
- The Debtor's attorney may seek additional compensation by separate applications and court order for services provided in connection with the enrollment and performance under an IDR.

Buchanan Provisions

- The Debtor is not seeking nor does this Plan provide for any discharge, in whole or in part, of her student loan obligations.

An over-arching concern by the Department of Education appears to be that, following *United Student Aid Funds, Inc. v. Espinosa*, 559 U.S. 260 (2010), "unscrupulous debtors [will] abuse the Chapter 13 process by filing plans proposing to dispense with the undue hardship requirement in the hopes the bankruptcy court will overlook the proposal and the creditor will not object." *Id.* at 16.

It is best to address this concern directly, both by specifically disavowing any present attempt at discharge and by asking that the Plan be specially set for a Confirmation Hearing.

Buchanan Provisions

- The Debtor shall be allowed to seek enrollment in any applicable income-driven repayment ("IDR") plan with the U. S. Department of Education and/or other student loan servicers, guarantors, etc. (Collectively referred to hereafter as "Ed"), without disqualification due to her bankruptcy.

This is a fundamental change in practice by Ed. and its servicers, which previously refused to consider applications by Chapter 13 debtors for IDRs, instead placing student loans into an "administrative forbearance."

The basis for this provision is the prohibition in 11 U.S.C. § 525 (c) which provides that a "A governmental unit that operates a student grant or loan program … may not deny a student grant, loan, loan guarantee, or loan insurance to a person that is or has been a debtor under this title … because the debtor … is … a debtor under this title…."

Buchanan Provisions

- Ed shall not be required to allow enrollment in any IDR unless the Debtor otherwise qualifies for such plan.

This is meant to prevent the debtor from asserting the confirmation of the plan on its own enrolled the Debtor in an IDR or that the Debtor was given any special preference.

Buchanan Provisions

- The Debtor may, if necessary and desired, seek a consolidation of her student loans by separate motion and subject to subsequent court order.

Consolidation of several student loans may be necessary for enrollment in a specific IDR or if the debtor was in default on her student loans. The plan provides that this will be approved by separate motion.

Buchanan Provisions

- Upon determination by Ed of her qualification for enrollment in an IDR and calculation of any payment required under such by the Debtor, the Debtor shall, within 30 days, notify the Chapter 13 Trustee of the amount of such payment. At such time, the Trustee or the Debtor may, if necessary, file a Motion to Modify the Chapter 13 Plan to allow such direct payment of the student loan(s) and adjust the payment to other general unsecured claims as necessary to avoid any unfair discrimination.

This provides that once the monthly payment under an IDR is determined, the debtor will notify the Chapter 13 Trustee, who would then have an opportunity to decide whether that requires a higher dividend to unsecured creditors and if the IDR should be made directly or by "conduit."

Buchanan Provisions

- The Debtor shall re-enroll in the applicable IDR annually or as otherwise required and shall, within 30 days following a determination of her updated payment, notify the Chapter 13 Trustee of such payment. At such time, the Trustee or the Debtor may, if necessary, file a Motion to Modify the Chapter 13 plan to allow such direct payment of the student loan(s) and adjust the payment to other general unsecured claims as necessary to avoid any unfair discrimination.

This provides a bit of a "carrot" for the Chapter 13 Trustee in consenting to the plan, in that the debtor will annually notify the Trustee of changes in the monthly IDR, which could result in a higher dividend to other unsecured creditors.

Buchanan Provisions

- During the pendency of any application by the Debtor to consolidate her student loans, to enroll in an IDR, direct payment of her student loans under an IDR, or during the pendency of any default in payments of the student loans under an IDR, it shall not be a violation of the stay or other State or Federal Laws for Ed to send the Debtor normal monthly statements regarding payments due and any other communications including, without limitation, notices of late payments or delinquency. These communications may expressly include telephone calls and e-mails.

The second greatest concern by Ed. appears to be that this plan is a devious attempt to trick student loan servicers into violating the automatic stay. The communications allowed are patterned on those with mortgage servicers, but stop short of allowing non-bankruptcy garnishment or other involuntary collection.

Buchanan Provisions

- In the event of any direct payments that are more than 30 days delinquent, the Debtor shall notify her attorney, who will in turn notify the Chapter 13 Trustee, and such parties will take appropriate action to rectify the delinquency.

This is to allow for monitoring of the IDR payments if made directly by the debtor.

It is important to remember that in regards to student loans, "delinquent" may not be the same as "default", which requires that no payments have been made for more than 270 days. *See* 34 C.F.R. § 685.102.

Buchanan Provisions

- The Debtor's attorney may seek additional compensation by separate applications and court order for services provided in connection with the enrollment and performance under an IDR.

This clearly the most important provision in this plan, allowing separate and additional compensation for these services.

Options for Chapter 13 Allowance of IDR

- Separate Classification
- Co-Sign Protection
- Above-median debtor pays student loan from discretionary income, i.e. Social Security or belt-tightening, earned in excess of PDI
- Below-median debtor extends plan to five years
- Pro Rated Distribution to Other General Unsecured Claims
- Chapter 20

Separate Classification in Chapter 13

§ 1322. Contents of plan

* * *

(b) Subject to subsections (a) and (c) of this section, the plan may—

(1) designate a class or classes of unsecured claims, as provided in section 1122 of this title, but may not discriminate unfairly against any class so designated; however, such plan may treat claims for a consumer debt of the debtor if an individual is liable on such consumer debt with the debtor differently than other unsecured claims;

Reasons for Separate Classification

- Reasons for classifying student loan creditors separately from other unsecured creditors in chapter 13 plan:
  - Stay current on IDR.
  - Make progress towards 20/25 year cancellation or 10 year PSLF.
  - Maximize payment toward non-dischargeable debt.
  - Avoid accrual of post-petition interest: *In re* Kielisch, 258 F.3d 315 (4th Cir. 2001).

Judicial Standards

- *In re* Leser, 939 F.3d 669 (8th Cir. 1991):
  - (1) whether the discrimination has a rational basis;
  - (2) whether classification is necessary to debtor's rehabilitation under chapter 13;
  - (3) whether the discrimination is proposed in good faith; and
  - (4) whether there is meaningful payment to class discriminated against

Separate Classification Allowed

- Permitting Public Service Forgiveness eligibility advances debtor's fresh start
- Less discriminatory approach would leave the debtor or creditors worse off
- Concurrent payment of student loans and secured debts, followed by payment in full of unsecured debt
- Unsecured creditors receive at least as much as they would in chapter 7 proceeding

Separate Classification Not Allowed

- Nondischargeability, by itself, does not justify discrimination
- Public policy favoring student loan repayment or debtor's fresh start is not reasonable justification
- Avoiding harm to the debtor is not a reasonable basis for discrimination
- No proof that discrimination is necessary or reasonable

Co-Sign Protection

- Does the co-debtor stay under § 1301 protect parents or other family members who may have co-signed the debtor's student loan?
- Does the "however clause" eliminate or qualify the fairness requirement?
- Do student loans co-signed by parents for children fall into the § 1322(b)(1) consumer debt exception, permitting separate classification?

Documents

This Presentation and document are available at:
www.ncbankruptcyexpert.com
- Click on Student Loan Options and Chapter 13 Bankruptcy
- Password: IDR13

- Thanks to Prof. Susan Hauser for statistics, John Rao for case law and Joshua Cohen for details regarding student loan programs.

Speaker Biographies

D. Sims Crawford was appointed as the Chapter 13 Standing Trustee for the United States Bankruptcy Court, Northern District of Alabama, Southern Division in 2004, after serving as the Trustee's Staff Attorney for 7 years. Before that, he was engaged in the private practice of law in Birmingham, Alabama. He earned his B.A. from the University of Alabama and his J.D. from Cumberland School of Law. He served as Chair for the Bankruptcy & Commercial Law Section of the Birmingham Bar Association in 2007 and served on the Board of the Birmingham Bar Foundation in 2008-2009. Mr. Crawford currently serves as Treasurer of the National Association of Chapter 13 Trustees (NACTT), as well as a member of its Due Process Committee, STACS Committee, and Staff Symposium Committee. He is on the Advisory Board for Epiq Systems, Inc., is certified as a Professional in Human Resources (PHR), and is certified in Training and Development. Mr. Crawford is also a member of the American Bar Association.

Edward C. Boltz is a member of the Law Offices of John T. Orcutt, P.C., where he has managed the firm's office in Durham, North Carolina since 1998, representing clients in not only Chapter 13 and Chapter 7 bankruptcies, but also in related consumer rights litigation, including fighting abusive mortgage practices. Mr. Boltz received his B.A. from Washington University in St. Louis in 1993 and his J.D. from George Washington University in 1996. He is a member of the North Carolina State Bar, where he has been certified as a specialist in consumer bankruptcy law. He is admitted to practice before the Districts Courts in both the Eastern and Middle Districts of North Carolina. Mr. Boltz is the current President of the National Association of Consumer Bankruptcy Attorneys (NACBA). Previously, he has served as the Secretary of NACBA, and has jointly responsible for directing the NACBA State Chair program, Mr. Boltz has also served on the Bankruptcy Council for the North Carolina Bar Association and previously served as the Bankruptcy Chair for the North Carolina Association of Trial Lawyers.

11:35 - 12:35 **Life After the National Mortgage Settlement**: Mortgage and secured claims issues.

Moderator: William Mark Bonney, Chapter 13 Standing Trustee for the Eastern District of Oklahoma (Muskogee)
Michael T. Bates, Linquist and Vennum, LLP (Minneapolis, MN)
John Rao, National Consumer Law Center (Boston, MA)

INDEX OF MATERIALS

1. **Excerpts from the Transmittal to the Supreme Court on the Rule 3002.1 Changes**
2. **Application of CFPB Mortgage Periodic Statement Rule to Borrowers in Bankruptcy**
3. **Link to Treasury HAMP Supplemental Directives SD 16-02**
4. **Link to Treasury HAMP Supplemental Directives SD 16-03**
5. **Proposed Rule 3015.1**
6. ***Zair* Decision**
7. **PDF of PowerPoint Presentation**
8. **Speaker Biographies**

JUDICIAL CONFERENCE OF THE UNITED STATES

WASHINGTON, D.C. 20544

THE CHIEF JUSTICE
OF THE UNITED STATES
Presiding

JAMES C. DUFF
Secretary

October 9, 2015

MEMORANDUM

To: The Chief Justice of the United States and
Associate Justices of the Supreme Court

From: James C. Duff

RE: TRANSMITTAL OF PROPOSED AMENDMENTS TO THE FEDERAL RULES OF BANKRUPTCY PROCEDURE

By direction of the Judicial Conference of the United States, pursuant to the authority conferred by 28 U.S.C. § 331, I transmit herewith for consideration of the Court proposed amendments to Rules 1010, 1011, 2002, 3002.1, and 9006, and new Rule 1012 of the Federal Rules of Bankruptcy Procedure, which were approved by the Judicial Conference at its September 2015 session. The Judicial Conference recommends that the amendments be approved by the Court and transmitted to the Congress pursuant to law.

For your assistance in considering the proposed amendments, I am transmitting: (i) "clean" copies of the affected rules incorporating the proposed amendments and accompanying Committee Notes; (ii) a redline version of the same; (iii) an excerpt from the September 2015 Report of the Committee on Rules of Practice and Procedure to the Judicial Conference; and (iv) an excerpt from the May 2015 Report of the Advisory Committee on the Federal Rules of Bankruptcy Procedure.

Attachments

Rule 3002.1. Notice Relating to Claims Secured by Security Interest in the Debtor's Principal Residence

(a) IN GENERAL. This rule applies in a chapter 13 case to claims (1) that are secured by a security interest in the debtor's principal residence, and (2) for which the plan provides that either the trustee or the debtor will make contractual installment payments. Unless the court orders otherwise, the notice requirements of this rule cease to apply when an order terminating or annulling the automatic stay becomes effective with respect to the residence that secures the claim.

* * * * *

Committee Note

Subdivision (a) is amended to clarify the applicability of the rule. Its provisions apply whenever a chapter 13 plan provides that contractual payments on the debtor's home mortgage will be maintained, whether they will be paid by the trustee or directly by the debtor. The reference to § 1322(b)(5) of the Code is deleted to make clear that the rule applies even if there is no prepetition arrearage to be cured. So long as a creditor has a claim that

is secured by a security interest in the debtor's principal residence and the plan provides that contractual payments on the claim will be maintained, the rule applies.

Subdivision (a) is further amended to provide that, unless the court orders otherwise, the notice obligations imposed by this rule cease on the effective date of an order granting relief from the automatic stay with regard to the debtor's principal residence. Debtors and trustees typically do not make payments on mortgages after the stay relief is granted, so there is generally no need for the holder of the claim to continue providing the notices required by this rule. Sometimes, however, there may be reasons for the debtor to continue receiving mortgage information after stay relief. For example, the debtor may intend to seek a mortgage modification or to cure the default. When the court determines that the debtor has a need for the information required by this rule, the court is authorized to order that the notice obligations remain in effect or be reinstated after the relief from the stay is granted.

Rule 3002.1. Notice Relating to Claims Secured by Security Interest in the Debtor's Principal Residence

(a) IN GENERAL. This rule applies in a chapter 13 case to claims (1) that are ~~(1)~~secured by a security interest in the debtor's principal residence, and (2) for which the plan provides that either the trustee or the debtor will make contractual installment payments~~provided for under § 1322(b)(5) of the Code in the debtor's plan~~. Unless the court orders otherwise, the notice requirements of this rule cease to apply when an order terminating or annulling the automatic stay becomes effective with respect to the residence that secures the claim.

* * * * *

Committee Note

Subdivision (a) is amended to clarify the applicability of the rule. Its provisions apply whenever a chapter 13 plan provides that contractual payments on the debtor's home mortgage will be maintained, whether they will be paid by the trustee or directly by the debtor. The reference to § 1322(b)(5) of the Code is deleted to make

clear that the rule applies even if there is no prepetition arrearage to be cured. So long as a creditor has a claim that is secured by a security interest in the debtor's principal residence and the plan provides that contractual payments on the claim will be maintained, the rule applies.

Subdivision (a) is further amended to provide that, unless the court orders otherwise, the notice obligations imposed by this rule cease on the effective date of an order granting relief from the automatic stay with regard to the debtor's principal residence. Debtors and trustees typically do not make payments on mortgages after the stay relief is granted, so there is generally no need for the holder of the claim to continue providing the notices required by this rule. Sometimes, however, there may be reasons for the debtor to continue receiving mortgage information after stay relief. For example, the debtor may intend to seek a mortgage modification or to cure the default. When the court determines that the debtor has a need for the information required by this rule, the court is authorized to order that the notice obligations remain in effect or be reinstated after the relief from the stay is granted.

EXCERPT FROM THE SEPTEMBER 2015
REPORT OF THE JUDICIAL CONFERENCE

COMMITTEE ON RULES OF PRACTICE AND PROCEDURE

TO THE CHIEF JUSTICE OF THE UNITED STATES AND MEMBERS OF THE JUDICIAL CONFERENCE OF THE UNITED STATES:

* * * * *

FEDERAL RULES OF BANKRUPTCY PROCEDURE

Rules * * * * * Recommended for Approval and Transmission

The Advisory Committee on Bankruptcy Rules submitted proposed new Rule 1012, proposed amendments to Rules 1010, 1011, 2002, 3002.1, and 9006(f) * * * * * with a recommendation that they be approved and transmitted to the Judicial Conference. The proposed amendments were circulated to the bench, bar, and public for comment in August 2013 * * * * *, and were offered for approval as published except as noted below.

Rules 1010, 1011, and 2002, and New Rule 1012

The proposed amendments to Rules 1010, 1011, and 2002, and proposed new Rule 1012 are intended to improve procedures for international bankruptcy cases. Shortly after chapter 15 (Ancillary and Other Cross-Border Cases) was added to the Bankruptcy Code in 2005, the Bankruptcy Rules were amended to insert new provisions governing cross-border cases. Among the new provisions were changes to Rules 1010 and 1011, which previously governed only involuntary bankruptcy cases, and Rule 2002, which governs notice. The proposed new rule and amendments would: (1) remove the chapter 15-related provisions from Rules 1010 and 1011; (2) create a new Rule 1012 (Responsive Pleading in Cross-Border Cases) to govern responses to a chapter 15 petition; and (3) augment Rule 2002 to clarify the procedures for giving notice in cross-border proceedings. One comment received will be treated as a suggestion for later

consideration. The Advisory Committee determined to recommend approval of the amended rules as published.

Rule 3002.1

Rule 3002.1 applies only in chapter 13 cases and requires creditors whose claims are secured by a security interest in the debtor's principal residence to provide the debtor and the trustee notice of any changes in the periodic payment amount or the assessment of any fees or charges during the bankruptcy case. This rule intended to ensure that debtors who attempt to maintain their home mortgage payments while they are in chapter 13 will have the information they need to do so.

The proposed amendments seek to clarify three matters on which courts have disagreed: (1) the rule applies whenever a debtor will make ongoing mortgage payments during the chapter 13 case, whether or not a prepetition default is being cured; (2) the rule applies regardless of whether it is the debtor or the trustee who is making the payments to the mortgagee; and (3) the rule generally ceases to apply when an order granting relief from the stay becomes effective with respect to the debtor's residence.

Four comments were submitted on the proposed amendments. Two of them addressed the difficulty of applying the rule to home equity lines of credit, for which changes in payment amount are frequent and often de minimis. The other comments were supportive of the amendments. The Advisory Committee determined to recommend approval of the amended rule as published.

Rule 9006(f)

The amendment to Rule 9006(f) would eliminate the 3-day extension to time periods when service is made electronically. The amendment was initially proposed by the CM/ECF

Subcommittee and was published simultaneously with similar amendments to Civil Rule 6(d), Appellate Rule 26(c), and Criminal Rule 45(c) as part of the 3-day rule package. Five comments were submitted on the proposed bankruptcy rule amendment, including one by the Department of Justice similar to its comments on the other Advisory Committees' parallel amendments. To maintain uniformity with the Committee Notes of the other rules in the 3-day rule package, the Advisory Committee agreed to the addition of language to the Committee Note to address the concerns raised by the Department of Justice. The Standing Committee concurred with the minor modification.

* * * * *

The Standing Committee concurred with the Advisory Committee's recommendations above.

Recommendation: That the Judicial Conference:

a. Approve the proposed amendments to Bankruptcy Rules 1010, 1011, 2002, 3002.1, 9006(f), and new Rule 1012, and transmit them to the Supreme Court for consideration with a recommendation that they be adopted by the Court and transmitted to Congress in accordance with the law;

* * * * *

Respectfully submitted,

Jeffrey S. Sutton, Chair

Dean C. Colson
Brent E. Dickson
Roy T. Englert, Jr.
Gregory G. Garre
Neil M. Gorsuch
Susan P. Graber
David F. Levi
Patrick J. Schiltz
Amy J. St. Eve
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Jack Zouhary

Application of CFPB Mortgage Periodic Statement Rule to Borrowers in Bankruptcy

John Rao
National Consumer Law Center, Inc.

Rulemaking authority over the two key federal statutes that apply to mortgage servicing, the Real Estate Settlement Procedures Act (RESPA) and the Truth in Lending Act (TILA), was transferred to the Consumer Financial Protection Bureau. Following an extensive notice and comment period, the CFPB issued new mortgage servicing regulations under these statutes affecting a wide variety of servicer duties.[1] These regulations, added to Regulation Z for TILA and Regulation X for RESPA, became effective on January 10, 2014.

Included in the mortgage servicing regulations is a rule dealing with monthly or periodic mortgage statements. Before the rule was adopted, mortgage servicers typically provided consumers with either monthly statements or preprinted coupon books containing payment information. However, federal law had never required such statements or regulated their content. Even when servicers did provide monthly statements, they often stopped providing them when the borrower was in default or in a bankruptcy proceeding, times when the information is potentially most needed.[2] Information that would assist a borrower in discovering account errors and avoiding default, such as the assessment of fees or diversion of payments into suspense accounts, also generally had not been provided by servicers on monthly statements. An amendment to the Truth in Lending Act and the related rule adopted by the CFPB changed this by requiring that periodic statements be sent to borrowers on most residential mortgage loans.[3]

Periodic statements that are prepared under the new rule give homeowners significant information about their mortgage accounts. The disclosures provided on the statements should assist in determining whether an account is actually in default and whether a servicer has

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[1] 78 Federal Register 10902 (Feb. 14, 2013)(TILA) and 78 Federal Register 10696 (Feb. 14, 2013)(RESPA).
[2] *See In re* Monroy, 650 F.3d 1300 (9th Cir.2011)(approving local form plan language requiring secured creditors to continue sending periodic statements to debtors if they were provided pre-petition).
[3] 15 U.S.C. § 1638(f); Reg. Z, 12 C.F.R. § 1026.41.

properly applied payments or improperly charged unauthorized fees. The regulation requires that the statements contain information in the following categories: amount due for the billing period, explanation of amount due on the account including fees imposed, past payment breakdown, transaction activity, partial payment information, contact and account information, and delinquency information if applicable. Several of these categories include disclosure of a partial payment that is sent to a suspense or unapplied funds account.

If the consumer is more than forty-five days delinquent, the statement must include: (i) date when the consumer became delinquent; (ii) notification of possible risks, such as foreclosure, and expenses, that may be incurred if the delinquency is not cured; (iii) account history for the previous six months or the period since the last time the account was current showing the amount remaining past due from each billing cycle; (iv) notice indicating any loss mitigation program to which the consumer has agreed, if applicable; (v) notice of whether the servicer has initiated foreclosure by making the first notice or filing required by state law; (vi) total payment amount needed to bring the account current; and (vii) either the CFPB list or the HUD list of homeownership counselors and counseling organizations and the HUD toll-free telephone number to obtain contact information for homeownership counselors or counseling organizations.

The regulation does not require that periodic statements be provided if the mortgage is a fixed rate loan and the servicer gives the borrower a coupon book that contains information substantially similar to that required by the regulation. Even if this coupon book exclusion otherwise applies, if the borrower is more than forty-five days delinquent, the servicer must still provide the required delinquency information separately in writing, including an account history for the delinquency period.

Servicers are also not required to provide periodic statements to borrowers with reverse mortgages, and timeshare plans. The regulation applies only to closed-end mortgage loans, so open-end home loans such as HELOCs are exempted from coverage of the regulation. In addition, mortgage loans that are serviced by small servicers (servicers that service 5,000 or fewer mortgage loans) and state housing finance agencies are exempt from the periodic statement requirements.

Interim Final Rule

The CFPB initially stated that is the "complexities" of the bankruptcy scenario "necessitate" the periodic statement information be provided to consumers,[4] and the final rule as originally promulgated did not contain a bankruptcy exemption. However, the CFPB subsequently issued an Interim Final Rule, effective January 10, 2014, that created a broad exemption for consumers who are debtors in a bankruptcy proceeding or for any portion of a mortgage debt that is discharged in bankruptcy.[5] As discussed below, this exemption was intended as an interim rule and the CFPB has proposed a final rule that significantly would change the exemption.

Section 1026.41(e)(5) provides that a servicer is exempt from the periodic statement requirements for a mortgage loan while the borrower is a debtor in a bankruptcy case.[6] The CFPB's Official Interpretations for this section provide that the exemption applies for any portion of the mortgage debt that is discharged in bankruptcy.[7] The exemption does not address the fact that many consumers file under chapter 7 for non-mortgage related reasons and continue to maintain payments on their mortgage after receiving a discharge. For a variety of reasons, these consumers often do not enter into a reaffirmation agreement with the mortgage holder. Section 524(j) of the Bankruptcy Code provides an exception to the discharge injunction in this situation, permitting the mortgage holder to accept payments and service the loan in the ordinary course.[8]

In addition, the CFPB's Official Interpretations provide that if there are joint obligors on a mortgage, the exemption applies if any of the borrowers is in bankruptcy. An example is given of a husband and wife who jointly own a home, stating that if "the husband files for bankruptcy, the servicer is exempt from providing periodic statements to both the husband and the wife."[9] If the husband in this example filed a chapter 7 bankruptcy case, the automatic stay in his case does not apply to his spouse or any other joint obligors as there is no co-obligor stay in chapter 7. The commentary would appear to prevent the wife in the example provided by the

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[4] *See* Section-by-Section Analysis, § 1026.41(d)(2), 78 Fed. Reg. 10966 (Feb. 14, 2013).
[5] Reg. Z, 12 C.F.R. § 1026.41(e)(5).
[6] 12 C.F.R. § 1026.41(e)(5).
[7] *See* Official Interpretations, Supplement 1 to Part 1026, ¶ 41(e)(5) - 2(ii).
[8] 11 U.S.C. § 524(j).
[9] *See* Official Interpretations, Supplement 1 to Part 1026, ¶ 41(e)(5) - 3.

Bureau from receiving periodic statements even if the husband filed a chapter 7 case years after the couple were separated or divorced and the wife has been making the ongoing mortgage payments.

Proposed Final Rule

The CFPB has proposed a final rule that would revise the exemption.[10] If the consumer is a debtor in a bankruptcy case, the consumer is a primary obligor on a mortgage for which another primary obligor is a debtor in a chapter 12 or 13 case, or the consumer has discharged personal liability for the mortgage loan, periodic statements must be provided unless one of the following conditions applies:

- The consumer requests in writing that the servicer cease providing periodic statements or coupon books;
- The consumer's confirmed plan provides that the consumer will surrender the dwelling, provides for the avoidance of the lien securing the mortgage, or otherwise does not provide for payment of prepetition arrearage or maintenance of payments due under the mortgage loan;
- The bankruptcy court enters an order providing for the avoidance of the lien securing the mortgage loan, lifting the automatic stay with respect to the mortgage, or requiring the servicer to cease providing periodic statements or coupon books; or
- The consumer files with the bankruptcy court a Statement of Intention identifying an intent to surrender the dwelling securing the mortgage loan.

[10] *See* Amendments to the 2013 Mortgage Rules under the Real Estate Settlement Procedures Act (Regulation X) and the Truth in Lending Act (Regulation Z), Docket No. CFPB-2014-0033, 79 Fed. Reg. 74176 (Dec. 15, 2014).

1 **Rule 3015.1. Requirements for a Local Form for Plans**
2 **Filed in a Chapter 13 Case**

3 Notwithstanding Rule 9029(a)(1), a district may
4 require that a Local Form for a plan filed in a chapter 13
5 case be used instead of an Official Form adopted for that
6 purpose if the following conditions are satisfied:

7 (a) a single Local Form is adopted for the district
8 after public notice and an opportunity for public comment;

9 (b) each paragraph is numbered and labeled in
10 boldface type with a heading stating the general subject
11 matter of the paragraph;

12 (c) the Local Form includes an initial paragraph for
13 the debtor to indicate that the plan does or does not:

14 (1) contain any nonstandard provision;

15 (2) limit the amount of a secured claim based on
16 a valuation of the collateral for the claim; or

17 (3) avoid a security interest or lien;

18 (d) the Local Form contains separate paragraphs
19 for:
20 (1) curing any default and maintaining payments
21 on a claim secured by the debtor's principal residence;
22 (2) paying a domestic-support obligation;
23 (3) paying a claim described in the final
24 paragraph of § 1325(a) of the Bankruptcy Code; and
25 (4) surrendering property that secures a claim
26 with a request that the stay be terminated as to the
27 surrendered collateral; and
28 (e) the Local Form contains a final paragraph for:
29 (1) the placement of nonstandard provisions, as
30 defined in Rule 3015(c), along with a statement that
31 any nonstandard provision placed elsewhere in the
32 plan is void; and
33 (2) certification by the debtor's attorney or by
34 an unrepresented debtor that the plan contains no

35 nonstandard provision other than those set out in the

36 final paragraph.

Committee Note

This rule is new. It sets out features required for all Local Forms for plans in chapter 13 cases. If a Local Form does not comply with this rule, it may not be used in lieu of the Official Chapter13 Plan Form. *See* Rule 3015(c).

Under the rule only one Local Form may be adopted in a district. The rule does not specify the method of adoption, but it does require that adoption of a Local Form be preceded by a public notice and comment period.

To promote consistency among Local Forms and clarity of content of chapter 13 plans, the rule prescribes several formatting and disclosure requirements. Paragraphs in such a form must be numbered and labeled in bold type, and the form must contain separate paragraphs for the cure and maintenance of home mortgages, payment of domestic support obligations, treatment of secured claims covered by the "hanging paragraph" of § 1325(a), and surrender of property securing a claim. Whether those portions of the Local Form are used in a given chapter 13 case will depend on the debtor's individual circumstances.

The rule requires that a Local Form begin with a paragraph for the debtor to call attention to the fact that the plan contains a nonstandard provision, limits the amount of a secured claim based on a valuation of the collateral, or avoids a lien. The last paragraph of a Local Form must be for the inclusion of any nonstandard provisions, as defined by Rule 3015(c), and must include a statement that nonstandard

provisions placed elsewhere in the plan are void. The form must also require a certification by the debtor's attorney or unrepresented debtor that there are no nonstandard provisions other than those placed in the final paragraph.

FILED
CLERK
4/12/2016 2:58 pm
U.S. DISTRICT COURT
EASTERN DISTRICT OF NEW YORK
LONG ISLAND OFFICE

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK
---x
HSBC BANK USA, N.A.,

Appellant,

-against-

RAYMOND E. ZAIR, CHRISTINE M. ZAIR, and MARIANNE DEROSA, TRUSTEE,

Appellees.
---x

MEMORANDUM OF DECISION AND ORDER
15-cv-4958 (ADS)

APPEARANCES:

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SPATT, District Judge:

When a debtor files for Chapter 13 bankruptcy protection, the United States Bankruptcy Code strictly regulates the manner in which the debtor's secured creditors are repaid. In particular, under the provisions of 11 U.S.C. § 1325(a)(5), a repayment plan is only confirmable if, with respect to each secured creditor, one of the following is true: (1) the creditor consents to the plan, id. § 1325(a)(5)(A); (2) the plan provides for the creditor to retain his security interest in his collateral and receive periodic payments equaling the present value of the collateral, id. § 1325(a)(5)(B); or (3) the debtor agrees to surrender the collateral so that the creditor may pursue any legal remedies he may have, id. § 1325(a)(5)(C).

These are the exclusive methods of repaying a secured creditor, and a proposed Chapter 13 plan which, as to each secured claim, does not satisfy one of these three requirements, cannot be confirmed, even if the plan complies with the Bankruptcy Code in all other respects.

Against this backdrop, the present case calls for the Court to enter an ongoing debate over the answer to the following question: Is the surrender option found in § 1325(a)(5)(C) satisfied by a Chapter 13 plan that purports to "vest" title to collateral in a secured creditor pursuant to § 1322(b)(9) over that creditor's objection? Posed differently, can a confirmable Chapter 13 plan both "vest" title to real property *and* "surrender" that property to a common secured lender? If so, can the creditor refuse to accept the vesting in satisfaction of its claim? Can a court nevertheless compel the transfer over the creditor's objection?

In this case, confronted with an apparent division in the relevant caselaw, the United States Bankruptcy Court for the Eastern District of New York (Trust, *J.*) (the "Bankruptcy Court") on August 13, 2015 confirmed the Chapter 13 plan (the "Plan") of the Appellees Raymond E. Zair and Christine M. Zair (together, the "Debtors"), which provided that: (i) certain real property of the Debtors, which secured a mortgage loan issued by the Appellant HSBC Bank USA, N.A. ("HSBC" or the "Bank"), would be surrendered to the Bank in satisfaction of its secured claim pursuant to § 1325(a)(5)(C); <u>and</u> (ii) over the Bank's objection, title to the property would also vest in the Bank pursuant to § 1322(b)(9), thereby divesting the Debtors of their interest in the property, and creating a present possessory ownership interest in HSBC.

On August 24, 2015, the Bank appealed from the Bankruptcy Court's decision, arguing principally that, with respect to a common secured lender, the legal concepts of "surrender" and "vesting" are inherently incompatible. Thus, to the extent the Debtors' Plan in this case provided for both; and because the Plan did not satisfy any of the other requirements for plan confirmation found in § 1325(a)(5); the Bankruptcy Court erred in determining that the Plan was confirmable. For the reasons that follow, this Court agrees, and finds that the weight of persuasive authority supports a finding that a secured creditor's rights under § 1325(a)(5) are impermissibly compromised by a Chapter 13 plan that provides for non-consensual vesting under § 1322(b)(9).

Thus, the Court reverses the underlying decision of the Bankruptcy Court; vacates the subject confirmation order; and remands this matter for further proceedings consistent with this Opinion.

I. Background

Unless otherwise noted, the following facts are drawn from the underlying order of the Bankruptcy Court, see In re Zair, 535 B.R. 15 (Bankr. E.D.N.Y. 2015) ("Zair I"), and are not in dispute.

In October 2013, Superstorm Sandy destroyed the principal residence of the Debtors, located at 88 Nebraska Street in Long Beach (the "Long Beach Residence"). Due to the storm damage, the Debtors moved to a new home in Melville, and did not return to the Long Beach Residence.

On or about September 30, 2014, the Debtors filed for Chapter 13 bankruptcy protection. Schedule "A" to their bankruptcy petition, which relates to real property in the bankruptcy estate, identified the vacant Long Beach Residence as having a value of $255,000, and as being encumbered by two mortgages. The first-priority mortgage was held by HSBC and had an outstanding balance of $387,185.41. A junior mortgage was held by Bank of America, N.A. ("Bank of America") and had an outstanding balance of $30,437.51.

On or about November 26, 2014, HSBC filed a proof of claim in the amount of $440,380.68, representing the principal unpaid balance on its mortgage, plus interest, fees and pre-petition arrearages. Bank of America, through its servicing

agent, Green Tree Servicing LLC, also filed a proof of claim for the amount due on its mortgage.

On April 27, 2015, the Debtors filed and served a second amended Chapter 13 plan (previously defined as the "Plan"), which is at issue in this appeal. As described by the Bankruptcy Court, the Plan provided, in relevant part, that: (i) the Debtors would surrender the Long Beach Property to HSBC in full satisfaction of the secured portion of the Bank's mortgage loan; (ii) to the extent that the outstanding balance on the Bank's loan exceeded the value of the Long Beach Residence, the Bank would have thirty days to file an unsecured deficiency claim; and (iii) upon confirmation of the Plan, title to the Long Beach Residence would vest in the Bank. See Zair I, 535 B.R. at 17 (quoting Plan ¶¶ 2, 7).

The Debtors and the assigned Chapter 13 Trustee Marianne DeRosa (the "Trustee") supported confirmation of the Plan. However, HSBC objected, arguing, as it does here, that, although the Long Beach Residence can and should be surrendered under § 1325(a)(5)(C), so that the Bank may pursue state foreclosure proceedings as it deems appropriate, it would be improper to transfer title to the Long Beach Residence – and all of the concomitant carrying costs – to the Bank without its consent. In this regard, the Bank contends that the Plan is legally untenable because the concepts of surrender and vesting cannot coexist relative to a common piece of secured property.

The Bankruptcy Court disagreed with the Bank's position, and held that "while surrender and vesting are different, they are not mutually exclusive, and the

Bankruptcy Code's plain language permits a debtor to deploy both options in a plan." Id. at 21. As noted above, HSBC appealed the Bankruptcy Court's decision to this Court.

II. Discussion

A. The Standard of Review

This Court is vested with appellate jurisdiction over "final judgments, orders, and decrees" of the Bankruptcy Court. See 28 U.S.C. § 158(a); see also Fed. R. Bankr. P. 8013; KLG Gates LLP v. Brown, 506 B.R. 177, 189 (E.D.N.Y. 2014) (Spatt, J.). The Court reviews the Bankruptcy Court's legal conclusions, including determinations on matters of statutory construction, *de novo*. See In re Bethlehem Steel Corp., 02-cv-2854, 2003 U.S. Dist. LEXIS 12909, at *20 (S.D.N.Y. 2003) (citing In re Air Crash Off Long Island, New York, 209 F.3d 200, 202 (2d Cir. 2000)).

B. The Relevant Statutory Framework

As noted above, two statutory provisions are at the heart of this appeal. The first is 11 U.S.C. § 1325(a)(5), which provides that, as to each secured creditor, a Chapter 13 plan may only be confirmed:

> (1) when the secured creditor accepts the plan; (2) when the debtor surrenders the secured property; or (3) in an option known as a cramdown, when the debtor, over the creditor's objection, retains the secured property, "yet pay[s] only the present value of the collateral to the creditor . . . over the life of the plan," with "[t]he remaining balance of the debt [becoming] a general unsecured claim."

AmeriCredit Fin. Servs. v. Tompkins, 640 F.3d 753, 756 (2d Cir. 2010) (quoting Capital One Auto Finance v. Osborn, 515 F.3d 817, 820 (8th Cir. 2008)).

Thus, where, as here, "a secured creditor does not accept a debtor's Chapter 13 plan, the debtor has two options for handling allowed secured claims: surrender the collateral to the creditor, see § 1325(a)(5)(C); or, under the cram down option, keep the collateral over the creditor's objection and provide the creditor, over the life of the plan, with the equivalent of the present value of the collateral, see § 1325(a)(5)(B)." Assocs. Commer. Corp. v. Rash, 520 U.S. 953, 962, 117 S. Ct. 1879, 138 L. Ed. 2d 148 (1997). This case involves the "surrender" option.

The second relevant Code provision is 11 U.S.C. § 1322(b)(9), which provides that "the plan may . . . provide for the vesting of property of the [bankruptcy] estate, on confirmation of the plan or at a later time, in the debtor or in any other entity."

Although the Bankruptcy Code does not define "surrender" or "vesting," the parties agree, and the law is well-settled, that these terms are not synonymous. For example, "surrender does not require the debtor to physically transfer the collateral to the secured creditor, [but] does require the debtor to make the collateral available to the secured creditor." In re Higley, 539 B.R. 445, 449 (Bankr. D. Vt. 2015); accord In re Williams, 542 B.R. 514, 518 (Bankr. D. Kan. 2015) (noting that "surrender . . . has a well defined meaning," namely, "the relinquishment of all rights in property, including the right to possess the collateral. Surrender does not transfer ownership. Rather, surrender means only that the debtor will make the collateral available so the secured creditor can, if it chooses to do so, exercise its state law rights in the collateral" (internal citations omitted)); Wiggins v. Hudson City Sav. Bank, 2015 Bankr. LEXIS 2606, at *9 (Bankr. D.N.J. Aug, 4, 2015)

("Although not defined in the Bankruptcy Code, 'surrender' refers to the 'act of a debtor surrendering collateral to a lienholder who then disposes of the property pursuant to the requirements of state law' " (quoting In re Behanna, 381 B.R. 631, 640 (Bankr. W.D. Pa. 2008))); In re Sagendorph, 2015 Bankr. LEXIS 2055, at *6 (Bankr. D. Mass. June 22, 2015) (" 'Surrender' in the present context is that a debtor agreed to make the collateral *available* to the secured creditor – *viz.*, to cede his possessory rights in the collateral"); In re Ware, 533 B.R. 701, 712 (Bankr. N.D. Ill. 2015) ("Put simply, surrender under 1325 requires at a minimum the surrender of all of the rights that the debtor has").

By contrast, "vesting" is a more "consequential event" than surrender. See Williams, 542 B.R. at 518. Whereas "[s]urrender means making the property available to be taken; vesting means transferring title." Id.; see, e.g., In re Tosi, 2016 Bankr. LEXIS 690, at *12-*13 (Bankr. D. Mass. Mar. 4, 2016) ("[T]o vest property in another, as contemplated in 11 U.S.C. § 1322(b)(9) . . . is to effect a transfer of ownership of that property from the [bankruptcy] estate to another person or entity. Vesting means transferring title" (internal quotation marks and citations omitted)); Williams, 542 B.R. at 518 (" 'Vesting' is also not defined in the Code. But its plain meaning 'includes a present transfer of ownership.' " (quoting In re Rosa, 495 B.R. 522, 523 (Bankr. D. Haw. 2013))); Sagendorph, 2015 Bankr. LEXIS 2055, at *6-*7 (" '[v]esting' . . . plainly means to place one in legal possession or ownership of property"); Bank of N.Y. Mellon v. Watt, 14-cv-2051, 2015 U.S. Dist. LEXIS 54041, at *11-*12 (D. Or. Apr. 22, 2015) ("[V]esting is the mechanism that,

in the context of real property, transfers title and, by extension" extinguishes the debtor's continuing obligations and liabilities).

C. Summary of the Arguments

As noted above, HSBC argues principally that the legal concepts of "surrender" and "vesting" are mutually exclusive, and therefore, with respect to a secured claim, a Chapter 13 plan that provides for one must not provide for the other. Applied here, HSBC argues that, to the extent the Plan invokes § 1322(b)(9) to non-consensually vest title to the Long Beach Residence in the Bank, it cannot also provide for the Long Beach Residence to be "surrendered" under § 1325(a)(5)(C). Under this scenario, because compliance with § 1325(a)(5) is mandatory; and because the Plan does not satisfy any of the other requirements for plan confirmation found in that provision; the Plan is not confirmable, as a matter of law, and the Bankruptcy Court erred in concluding otherwise.

As a practical matter, the Bank seeks to avoid the "vesting" option because, as one bankruptcy court in this Circuit noted, being "stuck with the collateral" means being "responsible for the maintenance, taxes, and other obligations that come with owning property." In re Sherwood, 2016 Bankr. LEXIS 263, at *9 (Bankr. S.D.N.Y. Jan. 28, 2016) (quoting In re McCann, 537 B.R. 172, 179 (Bankr. S.D.N.Y. 2015)). Ordinarily, "until the property is actually sold pursuant to a foreclosure sale, title to the property [and all of the attendant carrying costs] remain[ ] vested in the debtor." In re Sneijder, 407 B.R. 46, 52-53 (Bankr. S.D.N.Y. 2009). However, "vesting" the Long Beach Residence in the Bank would force it to

assume immediate ownership of the property, which was destroyed in a storm in 2013, and has since remained vacant and in disrepair.

As a mortgage holder, HSBC would understandably prefer to leave the Debtors in possession of the Long Beach Residence, while it takes whatever steps it deems are appropriate to enforce its lien through foreclosure proceedings. Or, if the Bank sees fit, it could take no steps at all. See In re Rose, 512 B.R. 790, 793-94 (Bankr. W.D.N.C. 2014) ("Although 'surrender' envisions a debtor relinquishing his or her rights in the collateral, there is no corresponding requirement that the lender [ ] do anything with the property"). In this regard, the Bank's position is that it has the right to "control its remedies," id. at 794, and the Court may not, over its objection, require HSBC to either "accept a surrender of property or take possession of or title to it through repossession or foreclosure." Id. (quoting In re Arsenault, 456 B.R. 627, 630 (Bankr. S.D. Ga. 2001), aff'd, 2012 U.S. Dist. LEXIS 128412 (S.D. Ga. Aug. 20, 2012))).

In this regard, HSBC's argument is rooted in principles of state law. In particular, relying on the Supreme Court's opinion in Butner v. United States, 440 U.S. 48, 55, 99 S. Ct. 914, 59 L. Ed. 2d 136 (1979), which recognized that "[p]roperty interests are created and defined by state law," the Bank contends that New York is a so-called "lien theory state," meaning that, as the mortgagee, the Bank has only a lien on the Debtors' property, not legal or equitable title. According to the Bank, the Debtors' Plan interferes with this legal status by imposing an ownership interest in the Long Beach Residence for which the Bank did not bargain.

Also, the Bank asserts that the Plan violates New York's Statute of Frauds because, by vesting in the Bank a present possessory ownership interest in the Long Beach Residence, it materially alters the parties' contract rights under the applicable mortgage documents, and there is no signed writing to that effect.

The Debtors and the Trustee respond by arguing that the Bank's interpretation of the relevant Code provisions runs counter to the overarching goal of Chapter 13, which is to provide a "fresh start" to debtors. Counsel for the Debtors in this case explained their position lucidly:

> Congress enacted Chapter 13 of the Bankruptcy Code to "provide expanded relief to a debtor" and an adequate opportunity for a "fresh start . . . essential to modern bankruptcy law.' " In re Sher, 12 B.R. 258, 265 (Bankr. S.D.N.Y. 1981 (citing House Report No. 95-595, 95th Cong., 1st Sess. 117 (1977)). For a debtor burdened by the ownership costs of property that the debtor cannot live in – costs that may include real estate taxes, maintenance, and insurance – §§ 1322(b)(8) and (9) are critical to the debtor's fresh start. They allow the debtor to pay a claim secured by the property through transferring the property to the creditor holding the security interest. This not only removes ongoing ownership costs for the debtor, it allows the creditor to obtain the property more quickly and at less cost than a foreclosure would require.

See Br. for Debtors at 9; see also Br. for Trustee at 8 ("Without being able to vest the property, as is specifically permitted under Section 1322(b)(9), the Debtors are at the whim of the [Bank] and will be incurring expenses associated with the Property, such as real estate taxes, until if and when the [Bank] completes a state court foreclosure. . . . Allowing debtors to be saddled with this debt and other related debt or to continue to be burdened with ownership of property they cannot manage goes against the 'fresh start' policy of the Bankruptcy Code").

Thus, it is the Appellees' position that § 1322(b)(9) provides a mechanism by which debtors can offload property that they can no longer afford, and secured creditors may not frustrate that process by refusing the transfer of the collateral. See Br. for Debtors at 6 (arguing that the Bank's interpretation "makes it impossible for a Chapter 13 plan to pay a debt by transferring surrendered property unless the creditor consents").

As for the Bank's arguments concerning the application of state law, the Debtors and the Trustee contend, as a matter of Constitutional law, that the Bankruptcy Code preempts these principles.

With these contentions in mind, the next step in the Court's analysis is to determine whether and to what extent § 1325(a)(5)(C) and § 1322(b)(9) have been understood to coexist in a valid Chapter 13 plan.

D. The Interplay of § 1325(a)(5)(C) and § 1322(b)(9)

1. The State of the Law at the Time of the Underlying Decision

At the time of the Bankruptcy Court's decision below, two divergent lines of cases had emerged. One line of cases, exemplified by In re Rosa, 495 B.R. 522 (Bankr. D. Haw. 2013), supports the Debtors' position. It holds that a Chapter 13 plan may vest title to real property in a secured creditor under § 1322(b)(9) and still be confirmable under the surrender option found in § 1325(a)(5)(C).

For example, in In re Rosen, 2015 Bankr. LEXIS 4448 (Bankr. D. Kan. Feb. 24, 2015), the bankruptcy court permitted the debtors to amend their Chapter 13 plan to provide for real property to vest in a secured creditor, in addition to being

surrendered to that creditor. The court noted that the debtors had "patiently waited for [the mortgagee] to take legal steps to foreclose the[ ] security interests in good faith," while at the same time remaining liable for property taxes, maintenance, upkeep, and municipal fees and penalties. See id. at *3, *6. Thus, the court reasoned that allowing the debtors to divest themselves of the burdens of owning this property was consistent with the plain language of § 1322(b)(9) and "the broader principal purpose of the Bankruptcy Code, which is to grant a fresh start to the honest but unfortunate debtor." Id. at *5 (internal quotation marks and citations omitted).

Similarly, in In re Sagendorph, 2015 Bankr. LEXIS 2055, the bankruptcy court found nothing inherently inconsistent between § 1325(a)(5)(C) and § 1322(b)(9), and held that "[a] plan which contains a provision for transferring or vesting in the secured creditor the property that is its collateral would be confirmable under § 1325(a)(5)(C) because a transfer of property presupposes its surrender by the transferor." Id. *13. Stated otherwise, consistent with an argument advanced by the Trustee in this case, the court reasoned that "[s]urrendering, or ceding possessory rights is a preliminary step in the process of transferring title." Id. (internal quotation marks and citation omitted); see Br. for Trustee at 7 (arguing that "surrender is a condition precedent to vesting property" because "Debtors cannot vest the property without surrendering it first").

Consistent with Rosen, the Sagendorph court also emphasized debtors' need

for a "fresh start," referring to that policy rationale as the "paramount federal interest" behind its decision.

However, the Court notes that Rosa, the fountainhead of this line of cases, is materially distinguishable from this case. Unlike here, in Rosa, the mortgagee did not object to the proposed vesting. See Rosa, 495 B.R. at 522-23, 525. The court specifically noted that the "surrender" option in § 1325(a)(5)(C) would not have "fully validate[d]" the plan in that case precisely "*because* the debtor propose[d] vesting in addition to surrender." Id. at 524 (emphasis supplied). Indeed, the Rosa court hypothesized situations where a "mortgagee may have legitimate reasons to object" to such a plan, for example, where the subject property "is contaminated by hazardous waste or subject to exorbitant [homeowners'] association fees"; or where "the property is subject to other liens or co-ownership interests," in which case "vesting plus the doctrine of merger might extinguish the mortgage." Id. at 525. However, unlike in this case, in Rosa, "the fact remain[ed] that the first mortgagee received adequate notice . . . and did not object" to the proposed plan. Id.

Thus, critically, the Rosa case was not decided under § 1325(a)(5)(C). Rather, the court there determined that the secured creditor had consented to its treatment, and the plan was confirmed under § 1325(a)(5)(A). See id. Under these circumstances, the Court is of the view that the Rosa decision is not analogous to the present case, and indeed, forms a questionable foundation for the line of subsequent cases, relied upon by the Appellees, which purport to extend the holding of Rosa to situations, like the present case, involving § 1325(a)(5)(C).

By contrast, the second line of cases, exemplified by In re Malave, 2014 Bankr. LEXIS 5383 (Bankr. S.D.N.Y. 2014), supports the Bank's position. It holds that "[w]hen a secured creditor timely objects to the confirmation of a plan that proposes to vest title in that creditor, the court cannot confirm the plan" under § 1325(a)(5)(C). See id. at *3-*4.

For example, in In re Rose, 512 B.R. 790 (Bankr. W.D.N.C. 2014), the bankruptcy court confirmed a plan under which the debtors surrendered encumbered property to the mortgagee. However, for more than a year the mortgagee took no action to foreclose on the property, and the debtors remained liable for continuing post-petition obligations, including taxes and maintenance costs. The "[f]rustrated" debtors sought permission from the bankruptcy court to transfer the property by quitclaim deed to the mortgagee over its objection. The Rose court recognized that, although "the creditor's failure to foreclose might leave the debtors with continued liabilities, these are by-products of property ownership," and the debtors' preference to "walk away from the property . . . does not justify shifting these burdens to the lender." Id. The court noted that "[m]ost courts that have considered the matter agree [that] . . . the 'secured creditor . . . has the prerogative to decide whether to accept or reject the surrendered collateral.' " Id. (citations omitted).

In oft-cited language, the court found that forcing a lender to take title to property "opens up a Pandora's box of possible injuries to lenders":

> First, and obviously, forcing a lender to take title causes it to assume burdens of ownership for which it did not contract. The costs of foreclosure or repossession, coupled with ongoing obligations to insure the property and to pay *ad valorem* taxes, may well exceed any present net realizable value.
>
> Second, if the property is subject to multiple encumbrances, requiring a senior lender to accept title to its collateral would destroy that lender's priority lien position vis a vis junior mortgages, liens, and accrued [homeowners' association] obligations. . . . [T]he quitclaim scenario makes the lender owner of the property and, under the doctrine of merger, it takes title subject to these interests.
>
> A worse fate awaits the lender if the quitclaimed property is subject to environmental contamination. Making the lender the record owner [of] its collateral potentially subjects it to personal liability for existing environmental contamination . . .
>
> The potential for personal liability also exists if the collateral property is dilapidated, damaged, or otherwise a public nuisance.

Id. at 795-96 (internal citations omitted).

A similar result was reached in the case of Bank of N.Y. Mellon v. Watt, 14-cv-2051, 2015 U.S. Dist. LEXIS 54041 (D. Or. Apr. 22, 2015). In that case, the district court reversed a bankruptcy court decision confirming a Chapter 13 plan that proposed surrendering an encumbered townhouse to the mortgagee under § 1325(a)(5)(C), *and* vesting title to the townhouse in the same creditor under § 1322(b)(9). The court noted that, despite the authority in § 1322(b)(9) to vest property of the bankruptcy estate in other persons, in order to be confirmable, the plan must nevertheless comply with the requirements found in § 1325(a)(5), specifically, the surrender option found in § 1325(a)(5)(C).

Consistent with Rose, the court noted that "surrender" implies a degree of freedom on the part of secured creditors to accept or reject collateral. Thus, if the debtors had "surrendered" the townhouse in satisfaction of the mortgage, it would not extinguish their continuing liability for homeowners' association fees. By contrast, "vesting" the townhouse in the mortgagee would operate as a complete transfer of ownership, thereby cutting off the debtors' liability for post-petition assessments, and transferring that obligation to the lender. See id. at *14 (noting that the debtors' plan "did not merely propose the cessation of their interest in the Property, it also forcibly transferred that interest, and the attendant liabilities, to [the bank]").

The court in Watt, emphasized the rights afforded to secured creditors under the Bankruptcy Code, finding that by "confirming a Chapter 13 plan that advanced non-consensual vesting in conjunction with surrender, the bankruptcy court [had] read language into the bankruptcy Code that does not exist, as well as frustrated the purpose of the statute, which is to provide protection to creditors holding allowed secured claims." Id. at *15-*16. Further, the court found that "the bankruptcy court's interpretation impermissibly transform[ed] the secured creditor's right into an obligation, thereby rewriting both the Bankruptcy Code and the underlying loan documents . . ." Id. at *16-*17.

Of particular note, the court in Watt specifically addressed, and rejected, the overreliance the Rosen line of cases had placed on the "fresh start" argument, which is advanced by the Debtors and the Trustee in this case:

> Debtors assert repeatedly on appeal that a balance must be struck between the rights of creditors on the one hand, and the policy of affording the debtor a fresh start on the other. Their second amended plan, however, effectuated no such balance; it wholly eliminated their financial responsibility in relation to the Property, at the sole expense of a secured creditor.

Id. at *19 n.6 (internal quotation marks and citation omitted).

On August 13, 2015, confronted with this apparent split in the relevant authority, the Bankruptcy Court issued the underlying decision in this case, which explicitly departed from the Malave-Rose-Watt line of cases, and followed the Rosa-Rosen-Sagendorph line in concluding that the Debtors' Plan should be confirmed. See Zair I, 535 B.R. at 21 (noting that the Bankruptcy Court "disagree[d] with Watt and to some extent, with Malave" and "agree[d] for the most part with Sagendorph").

However, while this appeal was on submission, several other courts weighed in on this question, deepening the divide between the two emerging philosophies.

2. Recent Developments in the Law

Less than one month after Zair I issued, a bankruptcy court sitting in the District of Minnesota decided In re Stewart, 536 B.R. 273 (Bankr. D. Minn. 2015). There, the court expressly adopted the reasoning of both Sagendorph and Zair I in concluding that "[w]hile the 'surrender' concept found in § 1325(a)(5)(C), and the 'vesting' concept embodied in § 1322(b)(9) are different, they may nonetheless be used in tandem when providing for the treatment of a secured claim in a chapter 13 plan." Id. at 277. However, the court in Stewart did not answer the central question presented here, namely, whether these provisions may be used in tandem

where, as here, *the creditor objects to the plan*. As in Rosa, discussed supra, the secured creditor in Stewart did not object to the debtors' proposed Chapter 13 plan before it was confirmed. Therefore, the court relied upon an unrelated provision of the Bankruptcy Code, namely, 11 U.S.C. § 1327(a), to hold that the creditor was bound by the terms of the already-confirmed plan. In the Court's view, like Rosa, the Stewart case is of limited usefulness to the instant appeal.

Nonetheless, two months after Stewart, another bankruptcy court sitting in the District of Kansas decided In re Williams, 542 B.R.514 (Bankr. D. Kan. Dec. 2, 2015). In that case, the court confirmed an initial plan by the debtor whereby his former residence would be surrendered to Wells Fargo, the mortgagee, under § 1325(a)(5)(C). To that end, the debtor abandoned the property, allowing Wells Fargo to enter the premises, change the locks, and generally maintain the property. However, several months passed without the mortgagee taking any steps to foreclose its security interest, and so the debtor made a motion to amend the plan to provide for the property to "vest" in Wells Fargo under § 1322(b)(9). The bank objected.

Upon reviewing the relevant caselaw, including Zair I, the bankruptcy court found in favor of the mortgagee, holding that § 1325(a)(5) "does not permit confirmation of a plan vesting title to collateral in the secured creditor over that creditor's objection." Id. at 521.

In reaching this conclusion, the court acknowledged the familiar argument that allowing a debtor to vest encumbered property in a secured lender may

alleviate certain burdens of ownership and promote the idea of a "fresh start." See id. (noting that "[i]t is tempting to hold that a plan providing for vesting may be confirmed over the secured creditor's objection" because, among other things, "[s]uch a holding would remove the burdens of property ownership" and "promote the debtor's fresh start"). However, explicitly agreeing with the Watt decision, discussed supra, the court found these considerations to be outweighed by the reality that "[v]esting the title over Well Fargo's objection would force it to accept the title and impose unbargained for obligations on it to pay taxes and other costs associated with the Property." Id.

Shortly after Williams, in January of this year, another decision addressing this issue was rendered in In re Weller, 2016 U.S. Bankr. LEXIS 108 (Bankr. D. Mass. Jan. 13, 2016). Of note, the Weller decision originated in the bankruptcy court for the District of Massachusetts, namely, the same district from which the Sagendorph decision issued. However, although decided less than a year apart, the Weller court broke with the reasoning and conclusion in Sagendorph, and fell in line with the Malave-Rose-Watt-Williams line of cases.

In Weller, the debtors owned real property that was encumbered by a mortgage held by Wells Fargo. The outstanding balance on the mortgage loan was approximately twice the value of the property. Thus, when the debtors sought protection under Chapter 13, they proposed a plan whereby the property would be surrendered to Wells Fargo in satisfaction of the secured claim. This plan was confirmed, but the bank refrained from foreclosing on the property for three years

after confirmation, during which time the debtors continued to pay the applicable carrying costs.

Eventually, the debtors became unable to continue meeting these expenses, and, "[w]ishing to relieve themselves of the burden of maintaining and insuring the Property, the Debtors decided to take another approach," namely, "propos[ing] that title to the Property vest in Wells Fargo upon confirmation of the Proposed Amended Plan." Id. at *3-*4. The bank objected.

In passing on the bank's objection, the Court held plainly that "[a] plan which 'vests' property in a secured creditor does not fulfill the requirements of § 1325(a)(5)(C) and may not be confirmed over that secured creditor's objection." Id. at *10. In reaching this conclusion, the Court conceded that § 1325(a)(5) and § 1322(b)(9) "are not in conflict," and hypothesized situations where a plan invoking both provisions might be confirmed:

> [F]or example, a debtor could propose a plan which would vest property in a grantee that has consented (or from whom the debtor plans to seek consent). Or could propose a plan which would vest property in a grantee in the hopes that such party will not object, and that its silence might be deemed consent.

Id. at *9.

However, the court clarified that, ultimately, § 1325(a)(5) outlines the exclusive methods of satisfying a secured claim, and "vesting" property in an unwilling lender is not one of them. Therefore, "[w]hat a Chapter 13 debtor may *not* do . . . is substitute the *options* which may be proposed by a plan under § 1322 for

requirements mandated by § 1325 for confirmation of a plan." Id. (emphasis in original).

Although sensitive to the fact that the debtors had "been left in limbo by Wells Fargo's failure to act," the court in Weller nevertheless held that the debtors' proposed plan to vest the property in Wells Fargo could not be confirmed over the bank's objection.

Two weeks later, a bankruptcy court in this Circuit took up the issue in a case called In re Sherwood, 2016 Bankr. LEXIS 263 (Bankr. S.D.N.Y. Jan. 28, 2016). In that case, the mortgagee bank objected to a plan that would both surrender real property of the debtor in satisfaction of its secured claim, *and* vest title to the property in the bank.

Similar to HSBC in this case, the mortgagee in Sherwood argued that, although "the Debtor [wa]s entitled to surrender property through her plan pursuant to section 1325(a)(5)(C)," "she [could] not compel [the bank] to accept title to the property under section 1322(b)(9) so long as [the bank] objects to such treatment." The bankruptcy court agreed, rejecting "[c]ases such as Watt I, Sagendorph, Zair [I], and Stewart [which] take the position that surrender and vesting are not mutually exclusive and that a provision vesting title in a secured creditor may be used in tandem with surrender in accordance with section 1325(a)(5)(C)," and instead finding "persua[sive] the emerging line of cases, exemplified by Rose, Malave, Watt[ ], Williams, and Weller, which hold that a chapter 13 plan may not be confirmed over the objection of a secured creditor where

the plan proposes to vest title to surrendered property in that creditor." Id. at *18-*19 (internal quotation marks and citations omitted).

The court in Sherwood recognized that "[w]here property is surrendered in a chapter 13 plan, there is often an 'expectation' that the creditor will promptly enforce its rights to recover and sell the property in order to satisfy its claim." Id. at *9 (quoting McCann, 537 B.R. at 179). The court further recognized that "at times, creditors may fail to exercise these rights, leaving debtors ' 'stuck with' the collateral' and 'responsible for the maintenance, taxes and other obligations that come with owning property.' " Id. However, this reality, though unfortunate, could not, in the view of the court, justify interpreting § 1322(b)(9) to "override the rights of a secured creditor under § 1325(a)(5)," which, as noted above, "includ[es] the option to do nothing to recover its collateral." Id. at *19-*21.

Of particular note, the Sherwood court was "not persuaded" by the conclusion in Zair I that "preventing a creditor from vesting surrendered property in a secured creditor over that creditor's objection 'essentially eliminates the usefulness of [section] 1322(b)(9).' " Id. at *20 (quoting Zair I, 535 B.R. at 21). On the contrary, the court noted that this conclusion incorrectly "assumes that section 1322(b)(9) can only be used to vest property in secured creditors, and that Congress must have intended for debtors to be able to vest surrendered property in secured creditors with or without their consent." Id. In this regard, the court noted several "permissible uses of section 1322(b)(9)" that either do not conflict with the surrender option, or do not implicate § 1325(a)(5) at all. For example:

> [A] debtor might retain property under section 1325(a)(5)(B) while providing for title to vest in a nondebtor spouse, child, or wholly-owned entity for tax or estate planning purposes . . . Or, as the court suggested in Weller, a debtor might provide for the vesting of property in some other third party 'that has consented (or from whom the debtor plans to seek consent) . . . or in the hopes that such party will not object, and that its silence might be deemed consent.' . . . Or a debtor might provide for the vesting of completely unencumbered property, which would not implicate section 1325(a)(5) because there would be no allowed secured claim subject to that section.

Id. at *20-*21.

Most recently, on March 4, 2016, a bankruptcy court in the District of Massachusetts decided the case of In re Tosi, 2016 Bankr. LEXIS 690 (Bankr. D. Mass. Mar. 4, 2016). In that case, the debtor's plan proposed a two-tiered approach to dispose of encumbered property: "In the first instance, the Debtor would retain the Property, [the mortgagee's] collateral, for a period of up to ninety days in which he would attempt to broker a sale of the Property and, from the proceeds, pay [the mortgagee's] claim . . . [But] if a sale [wa]s not consummated within ninety days of confirmation . . . the debtor's interest in the property [would] be surrendered pursuant to section 1325(a)(5)(C) and [would] immediately vest in [the mortgagee] pursuant to sections 1322(b)(8) and (9) without further order of the court." Id. at 3 (internal quotation marks omitted). As in this case, the plan in Tosi was "predicated on the assumption . . . that vesting is a form of surrender and that surrendering and vesting are not mutually exclusive." Id. at *5.

The court rejected this notion, and held, in relevant part, that the proposed plan was not confirmable because: "[T]hough it use[d] the nomenclature of surrender, in fact it merely vest[ed] the property in [the mortgagee], an act that

substantially modifies [the mortgagee]'s rights as to its collateral, [wa]s thus inconsistent with surrender, and therefore effect[ed] no true surrender at all, merely a vesting." Id. at *12.

The court departed from the conclusion reached in Sagendorph, a prior decision of the same court, that "surrender, as a ceding of possessory rights, is merely 'a preliminary step in the transferring of title.' " Id. at *13. Rather, the Tosi court acknowledged that the legal distinction between surrendering and vesting affects the rights of the secured creditor, not just the debtor:

> [The Sagendorph court's] reasoning understates the meaning of surrender, which is not merely to cede [the debtor's] possessory rights, *but to permit the creditor to exercise its preexisting property rights as to the collateral*. The vesting of title in the mortgagee goes well beyond surrender of the collateral by altering the mortgagee's rights as the holder of a mortgage. . . . Upon the debtor's vesting of his interest in the secured creditor . . . [n]o longer would the secured creditor have the substantial prerogatives of a mortgagee. Among other things, it could not sell the property at foreclosure. In a foreclosure sale, unsatisfied junior liens are automatically discharged, but the vesting of title in the mortgagee would leave junior liens in place, meaning that the value of the mortgagee's interest would be diminished by the value of any such liens. In addition, the secured creditor would now be saddled with new responsibilities that arise from its new form of ownership, including real estate taxes, maintenance, the avoidance of nuisances, and environmental remediation responsibilities.

Id. at *13-*14 (emphasis supplied).

In perhaps the most forceful rejection of the debtors' position in recent decisional law, the court stated that:

> [V]esting precludes surrender: a debtor cannot permit a mortgagee to exercise its preexisting rights where, by vesting the mortgaged property in the mortgagee, it has altered those rights out of existence. Surrender of collateral to a mortgagee and vesting of the same collateral in the mortgagee are thus mutually exclusive. A plan cannot

> do both while giving full and proper meaning to each term; and a plan that purports to do both at once must be denied confirmation as internally inconsistent.
>
> *   *   *
>
> Some debtors, as part of the fresh start they seek in bankruptcy, want to rid themselves of the burdens of property ownership. Where the mortgagee is not willing to simply take title or cannot or will not foreclose fast enough to provide the relief the debtors seek, debtors invoke the nomenclature of surrender to satisfy § 1325(a)(5). But where vesting occurs, there is no true surrender. The surrender is illusory, and therefore the plan does not satisfy § 1325(a)(5)(C).

Id. at *15-*16.

With these authorities in mind, the Court now turns to the merits of the present dispute, and in doing so, adds its voice to the growing majority of courts to interpret the Bankruptcy Code as prohibiting debtors from forcing secured lenders to accept title to encumbered property against the lenders' will.

E. As to Whether the Bankruptcy Court Erred in Confirming the Debtors' Plan

This Court is persuaded that the clear weight of authority – including the position unanimously adopted by other bankruptcy courts within this Circuit – supports the conclusion that the right of HSBC to control its own remedies respecting the Long Beach Residence cannot be subordinated to the Debtors' interest in achieving a fresh start in bankruptcy.

Initially, as a matter of statutory interpretation, the Court finds the position advanced by the Debtors and the Trustee in this case to be legally untenable. The plain language of § 1322(b)(9) provides that a Chapter 13 plan may, but is not required to, include one or more of a menu of optional features. However, nothing

in the language of the statute indicates that including one of these optional features *guarantees* the confirmability of the overall plan. See Watt, 2015 U.S. Dist. LEXIS 54041, at *13 (the fact that "section 1322(b)(9) permits inclusion of a nonstandard provision that vests property in a secured creditor does not resolve whether the plan can be confirmed with a nonstandard provision" (internal brackets omitted)); see also Williams, 542 B.R. at 521 ("Section 1322(b)(9) includes vesting as a discretionary term of a plan, but it does not assure confirmation of a plan providing for vesting"). Thus, the flaw in the Appellees' argument is the misapprehension that simply because the Code authorizes the use of vesting under some circumstances, that vesting *must* be appropriate in all circumstances. Such a construction is patently at odds with the permissive nature of § 1322(b)(9), which allows a plan to be confirmed with or without its inclusion. By contrast § 1325(a)(5) is not permissive. It is mandatory. A plan which does not strictly conform to one of its enumerated requirements is not confirmable.

Thus, it is true, as the Bankruptcy Court suggested, that § 1325(a)(5)(C) and § 1322(b)(9) are not, in all instances, mutually exclusive. However, in some situations, like this one, where its inclusion disrupts the mandatory treatment of a secured creditor under § 1325(a)(5), they *are* mutually exclusive, and the Plan's inclusion of both defeats confirmability.

In the Court's view, such a disruption is obvious in this case. Contrary to the position set forth by the Appellees, the Court finds that the Bank is entitled to the full array of property rights that accompany its position as first-priority lienholder,

including and especially the right to foreclose its security interest, or to refrain from doing so, as the case may be. See Tosi, 2016 Bankr. LEXIS 690, at *13-*14 (observing that the concept of surrender necessarily contemplates "permit[ting] the creditor to exercise its preexisting property rights as to the collateral"); Sherwood, 2016 Bankr. LEXIS 263, at *19-*21 (noting the right of a secured creditor "to do nothing to recover its collateral"); Rose, 512 B.R. at 793-94 (noting that there is no "requirement that the lender [ ] do anything with the property").

There can be no dispute that wielding the option of vesting under § 1322(b)(9) as a method of forcing the lender's hand to take some action with respect to the collateral that it would not otherwise take is a material curtailment of these rights. Thus, although the statutory language at issue does not expressly foreclose the possibility that real property may, under appropriate circumstances, be surrendered to and vested in the same secured creditor, in the Court's view, the incompatibility of these concepts in situations where the creditor withholds its consent is self-evident. See Tosi, 2016 Bankr. LEXIS 690, at *15-*16 ("[W]here vesting occurs, there is no true surrender. The surrender is illusory").

In this regard, the Court finds no support in the language of § 1322(b)(9) for concluding that, simply by virtue of its position as a mortgagee, the Bank is somehow susceptible to non-consensual reformation of its mortgage contract, or that its lien operates as a waiver of property rights under state law. Certainly that provision cannot be read as the Bank's assumption of liability for unbargained-for

carrying costs and exposure to the rights and obligations of junior lienholders with whom HSBC was not otherwise in privity.

In reaching this conclusion, the Court respectfully disagrees with the Bankruptcy Court's determination that § 1322(b)(9) would serve no conceivable purpose if not to facilitate debtors' repayment of secured claims with estate property. See Zair I, 535 B.R. at 21 (finding that "[r]eading § 1325 narrowly . . . essentially eliminates the usefulness of § 1322(b)(9)"). Since the issuance of that decision, other courts have written persuasively that this optional provision may, where appropriate, serve numerous functional purposes that do not conflict with the requirements of § 1325(a)(5)(C). See Weller, 2016 U.S. Bankr. LEXIS 108, at *9; Sherwood, 2016 Bankr. LEXIS 263, at *20-*21.

The Court also rejects the Appellees' argument that surrender is simply a natural first step in the broader act of transferring property out of the bankruptcy estate, namely, vesting. See Br. for Trustee at 7 (arguing that "surrender is a condition precedent to vesting property" because "Debtors cannot vest the property without surrendering it first"). As other courts have recognized, such an approach ignores the irreconcilable legal implications that arise when both surrender and vesting are included in a plan without the secured creditor's consent. See, e.g., Tosi, 2016 Bankr. LEXIS 690, at *12-*13 (determining that "[a] plan cannot do both while giving full and proper meaning to each term"); Williams, 542 B.R. at 522 (finding that "to construe surrender to include vesting would impair the state law rights of the secured creditor without providing any corresponding protective

limitation in the confirmation standards"); Rose, 512 B.R. at 795 (finding that non-consensual vesting "could impair a lender's rights in the collateral, subject it to ownership liabilities that never would have voluntarily assumed, and contravene state property law").

In this regard, contrary to the Appellees' contention, surrender is generally not followed in the ordinary course by the mortgagee taking title to the collateral. Nor does the mortgagee's right to receive surrendered collateral contemplate its responsibility for ongoing carrying costs pending disposal of the property. Nor does it potentially diminish the value of the mortgagee's first-priority lien by the amount of any junior liens which otherwise would have been extinguished by a foreclosure. On the contrary, these are unique consequences of vesting. By contrast, the concept of surrender "means only that the debtor will make the collateral available so the secured creditor can, *if it chooses to do so*, exercise its state law rights in the collateral." Id. at 518 (emphasis supplied). Therefore, in the Court's view, the imposition of the far more "consequential event" of vesting upon a non-consenting lender, who is entitled to the specific benefits and limitations of surrender, is inherently inconsistent with, and impermissibly impedes upon the creditor's rights sought to be preserved in § 1325(a)(5).

In the Court's view, this result is particularly warranted in this case because the property at issue, namely, the Long Beach Residence, was abandoned almost three years ago after being destroyed and rendered uninhabitable by a hurricane. Other courts – including some which have ultimately ruled in favor of the debtors –

have suggested that such circumstances may provide valid reasons for a mortgagee to resist accepting a conveyance of encumbered real property. See, e.g., Rose, 512 B.R. at 795-96 (noting that forcibly vesting property "could significantly injure the lender" if, for example, "the collateral property is dilapidated, damaged, or otherwise a public nuisance"); Rosa, 495 B.R. at 525 (observing that a mortgagee may justifiably object to vesting where the subject property "is contaminated by hazardous waste").

Finally, the Court rejects the theory that the Debtors' pursuit of a fresh start in bankruptcy should be elevated above the other interests of the parties in this case. Given the very clear delineation of secured creditors' rights in § 1325(a)(5); and the fact that Congress saw fit to fortify those rights by conditioning the confirmability of all Chapter 13 plans upon comformance with them; the Court can discern no principled basis for exalting the policy rationale in favor of "fresh starts" for debtors over the Code's obvious goal of preserving the well-settled property rights of secured lenders. Other courts are in accord. E.g., Watt, 2015 U.S. Dist. LEXIS 54041, at *19 n.6 (finding that a plan which purports to surrender and vest the same property in a secured lender failed to effect any meaningful balance of interests insofar as it "wholly eliminated [the debtors'] financial responsibility in relation to the Property, at the sole expense of a secured creditor"); see also Williams, 542 B.R.at 521 (finding the "tempt[ation] to . . . promote the debtor's fresh start," to be outweighed by the fact that "[v]esting the title over [the lender's]

objection would force it to accept the title and impose unbargained for obligations on it to pay taxes and other costs associated with the Property").

Accordingly, the Court finds that the underlying decision supplanted one of the requirements for confirmation found in § 1325(a)(5) with an optional nonstandard provision found in § 1322(b)(9). As in Watt, the result was the creation of a "fourth option" under § 1325(a)(5), which, in the Court's view, materially impaired the well-settled property rights of the Bank, requiring reversal.

III. Conclusion

Based on the foregoing, the Court reverses the underlying decision of the Bankruptcy Court; vacates the subject confirmation order; and remands this matter for further proceedings consistent with this Opinion.

The Clerk of the Court is directed to close this case.

Dated: Central Islip, New York
April 12, 2016

/s/ Arthur D. Spatt
ARTHUR D. SPATT
United States District Judge

RULE 3002.1 AMENDMENTS

Amendments effective Dec. 1, 2016 seek to clarify three matters:

(1) rule applies whenever plan provides for payment of ongoing mortgage payments, regardless of whether a prepetition default is being cured;

(2) rule applies regardless of whether it is the debtor or the trustee who makes the mortgage payments; and

(3) unless court orders otherwise, rule ceases to apply when an order granting relief from the stay becomes effective with respect to debtor's residence

Rule 3002.1. Notice Relating to Claims Secured by Security Interest in the Debtor's Principal Residence

(a) IN GENERAL. This rule applies in a chapter 13 case to claims (1) that are secured by a security interest in the debtor's principal residence, and (2) for which the plan provides that either the trustee or the debtor will make contractual installment payments. Unless the court orders otherwise, the notice requirements of this rule cease to apply when an order terminating or annulling the automatic stay becomes effective with respect to the residence that secures the claim.

LIFE AFTER HAMP

HAMP will sunset at the end of 2016 -
Supplemental Directives 16-02 and 16-03:

- Applications (Initial Package) must be submitted on/before 12/31/16
- Modification effective date must be on/before Sept. 30, 2017
- Trial plans should be converted to permanent mod. by Dec. 1, 2017
- Servicers will no longer be required to proactively solicit borrowers for HAMP as of Sept. 1, 2016
- MHA Help will no longer accept or escalate new cases effective December 1, 2017 – **all cases must be resolved by May 1, 2018**

LIFE AFTER HAMP

Consumer recommendations for a mortgage loan modification framework after HAMP:

- Start with an automatic streamlined modification offer
- Preserve a modification option tied to affordability
- Promote transparency with an online calculator
- Promote one-step modifications
- Use smart servicer compensation and data reporting to drive modifications

PERIODIC STATEMENT BANKRUPTCY EXEMPTION

- Interim Final Rule
  - Statements not required for any borrower in bankruptcy or for any portion of debt discharged in bankruptcy
  - For joint borrowers, exemption applies if any of the borrowers are in bankruptcy
- Proposed Rule to Modify Exemption
  - Comment period ended March 16, 2015
  - Final rule expected mid-2016

PROPOSED RULE ON PERIODIC STATEMENTS

Periodic statements must be provided unless one of these conditions applies:

- Consumer requests in writing that servicer stop sending periodic statements;
- Consumer's confirmed plan provides that:
  - consumer will surrender the dwelling,
  - lien securing the mortgage will be avoided , or
  - otherwise does not provide for payment of prepetition arrearage or maintenance of payments due under mortgage loan;

PROPOSED RULE ON PERIODIC STATEMENTS

Periodic statements must be provided unless one of the below conditions applies:

- Bankruptcy court enters an order providing for avoidance of mortgage lien, lifting automatic stay with respect to mortgage, or requiring servicer to cease providing periodic statements; **OR**
- Consumer files a Statement of Intention identifying an intent to surrender dwelling securing the mortgage loan

CFPB TESTING OF BANKRUPTCY PERIODIC STATEMENT FORMS

Participants generally expressed positive views about forms:

- "I don't know why anybody would *not* want to receive these notices." — Chapter 7
- "I would want to know how I could recover. If I wasn't keeping the home, it wouldn't matter." — Chapter 7
- "I would rather get this. It would help. I would be able to keep up with it a lot more… It would alleviate me calling my trustee a lot." — Chapter 13
- "This would be wonderful. I see some of the things I was trying to avoid with foreclosure. This would help a lot." — Chapter 13

LIFE AFTER NMS

How are lenders/servicers handling:

- Levels of review for POC and MFR accuracy?
- MFR affidavits/declarations?
- "Right to Foreclose" language?
- Filing amended POCs?
- Account reconciliations?

SURRENDER OF COLLATERAL

Q: Is surrender defined in the Bankruptcy Code?

A. No.

Q: What does surrender mean?

A. Chapter 7 cases: §521(a)(2)(A)
Chapter 13 cases: §1325(a)(5)(C)

SURRENDER OF COLLATERAL

Surrender means:

- "[Making] the collateral available to the secured creditor." ***In re Highly***, 539 B.R. 445, 449 (Bankr. D. Vt. 2015).
- "[T]he relinquishment of all rights in property, including the right to posses the collateral…." ***In re Williams***, 542 B.R. 514, 518 (Bankr. D. Kan. 2015).
- "Put simply, surrender under 1325 requires at a minimum the surrender of all of the rights the debtor has." ***In re Ware***, 533 B.R. 701, 712 (Bankr. N.D. Ill. 2015).
- "[N]ot taking an overt act to prevent the secured creditor from foreclosing its interest in the secured property." ***In re Metzler***, 530 B.R. 894, 899 (Bankr. M.D. Fla. 2015). *See In re Townsend*, 2015 WL 5157505 (Bankr. M.D. Fla. 2015).

Surrender <u>does not</u> mean:

- Delivery of collateral. *See* ***In re Plummer***, 513 B.R. 135 (Bankr. M.D. Fla 2014).
- Vesting title in the collateral. *See* ***In re* Zair**, 2016 WL 1448647 (E.D.N.Y. 2016).
- "Put simply, surrender under 1325 requires at a minimum the surrender of all of the rights the debtor has." ***In re Ware***, 533 B.R. 701, 712 (Bankr. N.D. Ill. 2015).
- "[N]ot taking an overt act to prevent the secured creditor from foreclosing its interest in the secured property." ***In re Metzler***, 530 B.R. 894, 899 (Bankr. M.D. Fla. 2015).

"FORCED VESTING"

- "Forced vesting" refers to the situation where a Chapter 13 debtor uses the plan confirmation process to transfer ownership of property to a secured creditor without that creditor's consent.
- Statutory Framework
  - § 1325 (a)(5)(C)
  - § 1322 (b)(9)

"FORCED VESTING"

Cases permitting forced vesting:

- ***In re Rosa***, 495 B.R. 522 (Bankr. D. Haw. 2013)*
- ***In re Rosen***, 2015 Bankr. LEXIS 4448 (Bankr. D. Kan.)
- ***In re Sagendorph***, 2015 WL 3867955 (Bankr. D. Mass.)
- ***In re Stewart***, 536 B.R. 273 (Bankr. D. Minn. 2015)*

Cases not permitting forced vesting:

- ***HSBC Bank USA, N.A. v. Zair***, 2016 WL 1448647 (E.D.N.Y.)
- ***In re Weller***, 2016 WL 164645 (Bankr. D. Mass.)
- ***In re Cormier***, 434 B.R. 222 (Bankr. D. Mass.)
- ***Bank of New York Mellon v. Watt***, 2015 WL 1879680 (D. Or.)
- ***In re Williams***, 542 B.R. 514 (Bankr. D. Kan. 2015)
- ***In re Rose***, 512 B.R. 790 (Bankr. W.D.N.C. 2014)
- ***In re Sherwood***, 2016 WL 355520 (Bankr. S.D.N.Y.)
- ***In re Tosi***, 546 B.R. 487 (Bankr. D. Mass.)*
- ***In re Malave***, 2014 Bankr. LEXIS 5383 (Bankr. S.D.N.Y.)

COMPETING PROBLEMS WITH "FORCED VESTING"

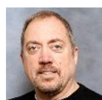
Debtor Problems

- Frustrates the debtor's ability to obtain a "fresh start"
- Debtor remains liable for taxes, insurance, HOA fees and other carrying costs on abandon/ vacant property

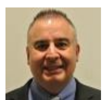
Creditor Problems

- Forced to assume burdens of ownership not contracted for
- Potential to destroy lien priority status
- Possible environmental contamination issues
- Potential for personal liability claims

Speaker Biographies



William Mark Bonney was born in Oklahoma City, Oklahoma and attended the University of Oklahoma where he received a B.A. in Economics in 1984, and his juris doctorate in 1987. He was admitted to practice law by the Oklahoma Supreme Court in 1987 and by the Texas Supreme Court in 1992. He began his legal career in Muskogee, Oklahoma with the firm of Cate and Harrison. In 1989 he was appointed to the panel of Chapter 7 Trustees for the Eastern District of Oklahoma and was also appointed the Standing Chapter 13 Trustee for the Eastern District of Oklahoma. He continues to maintain a private solo practice only taking referrals from other attorneys. Since being admitted to practice law he has served or been a member of the following organizations: Oklahoma Bar Association, Bankruptcy Section, Diversity Committee, Lawyers Helping Lawyers Committee, Law Related Education Committee, Young Lawyers Division, Oklahoma Mock Trial Committee and Coordinator and Judge; Muskogee County Bar Association, President 1990-91, Law Day Chair. He is a member of the American Bar Association, American Bankruptcy Institute, National Association of Bankruptcy Trustees National Association of Consumer Bankruptcy Attorneys, National Association of Consumer Advocates American Board of Certification, Consumer Bankruptcy Law. He is an active member of the National Association of Chapter 13 Trustees serving on its Government Relations Committee (Past Chair), Editorial Board, Bankruptcy Rules Committee (Chair), and Staff Symposium (Chair). He is a member of The NACTT Academy. He also serves his community in non-profit service to: Oklahomans For Equality, President 2005 to 2007; New Hope Camp, Inc., Treasurer 2009 to 2011; Neighbors Building Neighborhoods, Inc. Treasurer2010 to 2012; Legal Aid Servicers of Oklahoma, Inc., Current Finance Committee.



Michael T. Bates is a partner the Minneapolis, Minnesota law firm of Lindquist & Vennum where he provides legal advice on consumer regulatory and legal compliance issues to financial institutions and other businesses. Prior to joining Lindquist & Vennum, Mike served over 21 years as a Senior Vice President and Senior Company Counsel for Wells Fargo & Company. In this capacity, Mike provided legal advice to all consumer bankruptcy groups and consumer collections groups within Wells Fargo. Mike is a graduate of Iowa State University and Hamline University School of Law (*cum laude*) and is currently admitted to practice law in Iowa and Minnesota.

John Rao is an attorney with the National Consumer Law Center, Inc. Mr. Rao focuses on consumer credit and bankruptcy issues and has served as a panelist and instructor at numerous bankruptcy and consumer law trainings and conferences. He has served as an expert witness in court cases and has testified in Congress on consumer matters. Mr. Rao is a contributing author and editor of NCLC's *Consumer Bankruptcy Law and Practice*; co-author of NCLC's *Foreclosures*; *Bankruptcy Basics*; *Guide to Surviving Debt*; and NCLC Reports: *Bankruptcy and Foreclosures Edition*. He is also a contributing author to *Collier on Bankruptcy* and the *Collier Bankruptcy Practice Guide*. Mr. Rao serves as a member of the federal Judicial Conference Advisory Committee on Bankruptcy Rules, appointed by Chief Justice John Roberts in 2006. He is a conferee of the National Bankruptcy Conference, fellow of the American College of Bankruptcy, vice-president of the National Association of Consumer Bankruptcy Attorneys, member of the editorial board of *Collier on Bankruptcy*, and former board member for the American Bankruptcy Institute. He is an adjunct faculty member at Boston College School of Law. Mr. Rao is a graduate of Boston University and received his J.D. in 1982 from the University of California (Hastings).