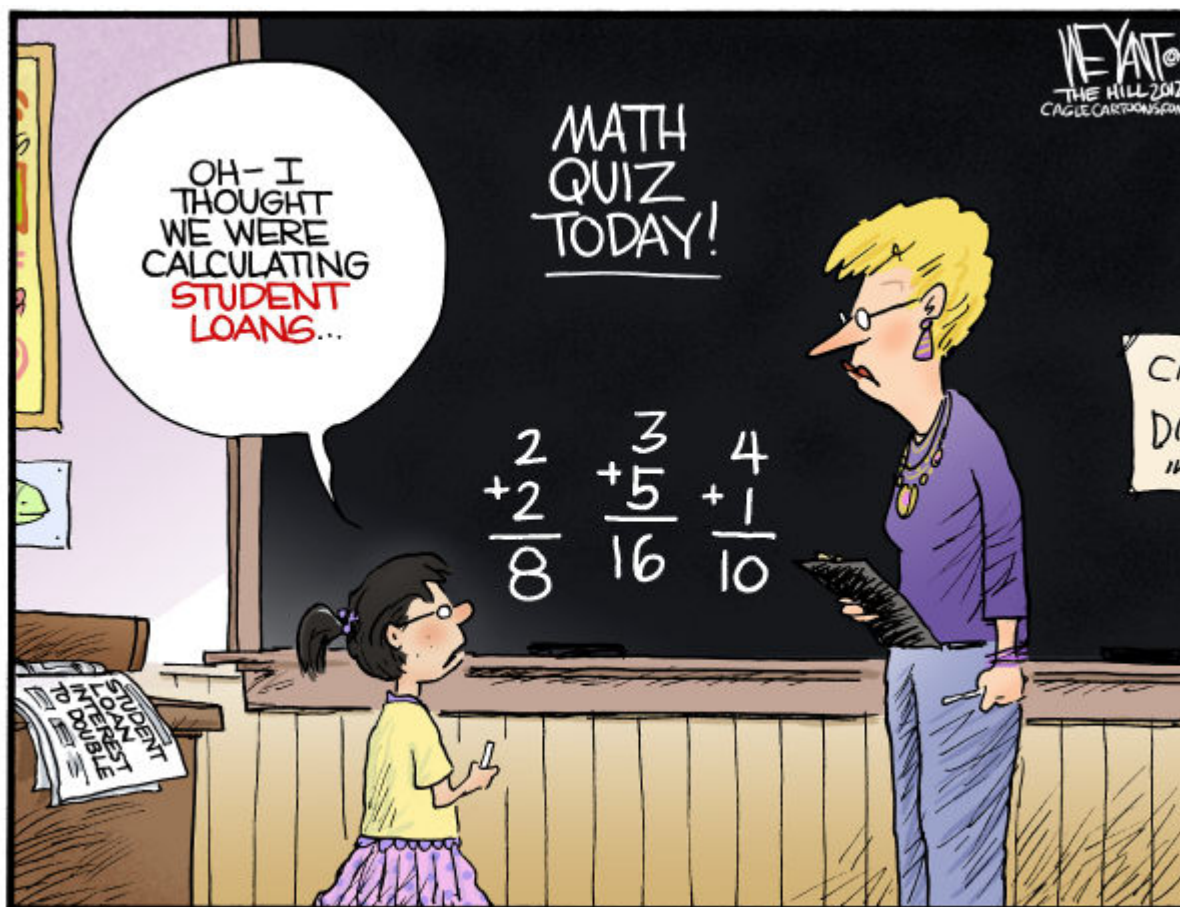


## Discharging Student Loan Debt The Easy Way:

### Administrative Discharges Through The Department of Education.



If there is an area of law that would seem to be ripe for litigation, it is student loans. The average amount of debt a student has on graduation is over \$30,000 now, and increases by several thousand dollars per year.<sup>1</sup> This growth in student loans is accompanied by equally-high default rates: 1 in 7 student loans goes into default, now.<sup>2</sup>

Despite that level of debt, there are almost no legal cases involving student loan issues, and much of what the courts do here come in the context of (often futile) attempts to discharge the debts in bankruptcy. Few, if any, lawyers see themselves as having the ability to represent student loan

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<sup>1</sup> Per CNN MONEY, extrapolating from statistics: <http://money.cnn.com/2013/12/04/pf/college/student-loan-debt/> For lawyers, the figures are even worse: the average debt owed by a lawyer who graduated from public schools in 2012 was over \$84,000 (\$122,000+ for private school graduates); those figures were nearly double what they had been just 10 years before.

<sup>2</sup> US NEWS & WORLD REPORT, <http://www.usnews.com/education/blogs/student-loan-ranger/2014/10/01/student-loan-default-rates-fall-but-borrowers-should-still-worry>

debtors, even when those lawyers work in practices that necessarily involve considerations of other debt.

Why aren't student loan debts more effectively handled by debtors' lawyers? The answer is likely that attorneys do not understand the special nature of student debt both in how it might relate to state and federal laws that grant borrowers rights to the special rules that can help borrowers get out from under onerous financial burdens.

Student loan debt is of course not like other debt; it is federally guaranteed (and federally regulated) and administered by a variety of different actors, from the schools themselves to private lenders to guaranty agencies to the Department of Education. This can cause lawyers to shy away from investigating potential remedies for debtors, and has apparently led to a widespread belief that there is nothing that can be done about student debt.

Litigation strategies – including how to determine when state laws are pre-empted by federal regulations – are beyond the scope of this talk. Instead, the subject herein will be the steps a borrower must take to get an administrative discharge of his or her loan.

The Higher Education Act encompasses the Federal Family Education Loan Program, (28 USC subch. IV parts B), the statutory sections by which most individual, student-directed federal loans are authorized and regulated. Section 1087(c) of that part authorizes discharges of student loans by the Secretary of Education for various reasons ranging from death of the student to undue hardship to 9/11-related reasons. A discharge under this section is an administrative agency action, relieving the borrower of any liability on the loan (and assigning the rights to collect on the loan to the Department of Education). See 28 USC sec. 1087(c). While the subsection applies specifically to only loans under that part, the Department allows administrative discharge of federal Direct Loans on many of the same bases, and a limited number of administrative discharges on Perkins Loans.<sup>3</sup>

The regulations implementing section 1087(c) expanded on the 'false certification' discharge subsection, as well as providing a regulatory and administrative scheme for borrowers to make their claims for discharge.

Because the administrative discharge provisions are not widely known, many debtors may not be aware of the ability to avoid payment on loans in some circumstances. And the Department is not required to notify borrowers of the ability to discharge their loans.

### **Types of Administrative Discharges:**

The administrative discharge can be obtained in several distinct situations under 1087(c). For purposes of this article, we will focus on the ones unrelated to death or disability or hardship, The remaining administrative discharge bases are:

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<sup>3</sup> A chart of which loans are available for which discharges is available here: <https://studentaid.ed.gov/repay-loans/forgiveness-cancellation> A "Perkins Loan" is one made by the school; a Direct Loan is one made by the federal government. The other loans are made by private lenders.

- (1) When the school closes,
- (2) When the student's identity was stolen,
- (3) When the school was required to refund a portion of the loan to the lender but fails to do so
- (4) When the school falsely certified the eligibility of the student to borrow the funds,

### **School Closings:**

If a school closes during the time a student is enrolled there, a debtor can apply for an administrative discharge of loans incurred attending that school. This is part of the attempt by Congress to avoid 'fly by night' schools bilking students. This provision does not apply to schools which merely lose their accreditation. *Armstrong v. Accrediting Council for Continuing Ed.* 980 F. Supp. 53 (D.C. 1997). Not only does the discharge end any liability for future payments, but the student is entitled to a refund of payments made on the loan. 34 CFR 685.214(b).

The borrower must submit to the Department of Education a written request and sworn statement, and prove that the student was unable to complete the course of study because of closure (or that the student withdrew just prior to the school closing) and could not complete the program by transferring credits to another school. The student must also provide information about the benefits received from any claims made to other entities regarding the loans (such as tuition reimbursement programs.)

### **Identity Theft:**



"Sorry. Looks like the guy who stole your identity got here before you did."

Identity theft is a subcategory of the 'false certification' discharge. Where a student can show that he or she was the victim of identity theft or a similar wrong, the Secretary can discharge the obligation. 34 CFR 685.215(1). Identity theft ranges from simple forging of signatures to applying for a loan in the student's name. A discharge for identity theft allows a borrower to avoid future payments and recover past payments.

Proof of identity theft requires sworn statements that the borrower did not take out the loan, or benefit from the proceeds of the loan; and, copy of a judgment determining that the (alleged) borrower was the victim of identity theft. The judgment must state the student loan was obtained as a result of the crime of identity theft, or the debtor must provide 'authentic specimens' of his or her actual signature as well as a statement

of facts demonstrating identity theft. A student might have to show that he or she paid for the classes using other funds, if the student was actually enrolled at the time. *Castagnola v. Educ. Credit Mgmt. Corp.* (SD Ohio, June 27, 2013).

### **Failure to refund:**

When a school closes or a student withdraws, the school must partially refund any unused or unearned student loan proceeds to the student (for payment on the loan.) If the school fails to do so, the Secretary can discharge the loans up to the amount that should have been refunded. 34 CFR 685.216.

The borrower must first try to work out the unpaid refund with the school, and then the Secretary will attempt to do so. This section allows a discharge by the Secretary without an application, although the Secretary is not required to do so and is not even required to notify the debtors of the possibility of a refund discharge. *Salazar v Duncan*, SD NY 2015.

### **False Certifications:**

By far the most ambiguous of the discharges is the ‘false certification’ discharge. 34 CFR 685.215 applies to more than just identity theft claims. Students may also receive a discharge of loans if the school falsely certified the student’s ‘ability to benefit’ from the school, or falsely certifies that the student meets eligibility requirements for a student loan.<sup>4</sup> A borrower also may qualify for a discharge if the borrower at the time of taking out the loan was not eligible to meet the requirements for employment in the occupation for which the training program was intended, in the State of residence (for reasons such as age, physical or mental condition, criminal record, ‘or other reason accepted by the Secretary’). This discharge entitles the borrower to avoid future payments and get reimbursed for past payments.

A student can demonstrate that he or she did not have the “ability to benefit” from a loan by proving they did not have a high school diploma or GED, did not have remedial education classes, or did not pass a standardized basic skills test. Students who do not meet one of those criteria as of the loan origination do not have the ability to benefit from the education the loan funds, by statute. The Secretary may not add additional qualifications to the ‘ability to benefit’ test. *Jordan v. Secretary of Education of The United States*, 194 F.3d 169 (1999).

The ability to benefit from the training by becoming employed in the field requires that the coursework be for more than just general studies. *Johnson v. Duncan*, 746 F.Supp.2d 163 (D.C. 2010)(Fact that convicted felon took several courses in paralegal studies did not demonstrate inability to benefit even though student was admittedly ineligible for many legal or law enforcement careers.)

### **Procedures:**

The Higher Education Act and implementing regulations do not create a private right of action. *In re Barton*, 266 B.R. 922 (BK SD GA, 2001). Instead, review of a decision by the Secretary is through the Administrative Procedures Act, which requires that the debtor receive a final determination from the Secretary before commencing any actions. *In re Bega*, 180 B.R. 642 (D. Kan 1995). This also means that the regulations cannot be used defensively in civil actions to

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<sup>4</sup> The eligibility requirements are numerous and are general found under 34 CFR 668.31-668.40,

collect on the loan. Id. Great deference will be given to the Secretary's determination. *Castagnola v. Educ. Credit Mgmt. Corp.* (SD Ohio, June 27, 2013).

The HEA pre-empts, at least in part, state laws that otherwise would grant the right to sue for a false certification. See *Wilson v. Chism*, 279 Ill. App. 3d 934, 665 N.E.2d 446 (Ill. App. 1. Dist., 1996)(Illinois consumer protection laws did not allow debtor to sue for false certification of ability to benefit from loan.)

**Conclusion:**

The expansive nature of the 'false certification' discharge, coupled with the growth of private, for-profit schools may mean that there are substantial numbers of debtors with student loans that are arguably subject to administrative discharge. Any practitioner whose clients have student loans should be familiar enough with the requirements for such a discharge to at least advise the client to seek that sort of remedy