Government Student Loans, Government Debts and Bankruptcy:
A Comparative Study

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Executive Summary

An increase is projected in the number and the value of loans for post-secondary education funded by the federal and provincial governments in Canada. Given this projection and calls for reform to the treatment of these loans in bankruptcy, we identified a need for a comprehensive review of the treatment of government-funded student loans in bankruptcy in Canada. We observed that a number of other jurisdictions had recently considered the issue and enacted reforms. Accordingly, we felt that a comparative approach for this review would be ideal. As part of our initial research plan, we were interested in exploring whether any other government debts received the same treatment as student loans in bankruptcy and we sought to compare this treatment. We found that, with the exception of the United States, all the jurisdictions under review did not similarly treat student loans as other government debts. Accordingly while we note the significance of this inconsistency and detail all the consumer debts not extinguished in bankruptcy in each jurisdiction under review, the treatment of other government debts in bankruptcy is not our focus.

This research considers the treatment in bankruptcy of loans funded by the government for a post-secondary education, in a comparative context. In addition to Canada, each of Australia, England, the United States, and New Zealand, which have all experienced a rapid increase in the number of overcommitted debtors, bankruptcies and reform to existing consumer bankruptcy legislation and policy over the last two decades, are considered. While the bankruptcy system and funding structure of post-secondary education in these jurisdictions differ in certain important respects, each share some historical, institutional or procedural features with the Canadian bankruptcy regime and each jurisdiction has some form of government-funded or guaranteed student loan program. In each jurisdiction, the last two decades have seen increasing numbers of students pursuing post-secondary education, increasing tuition fees and a move from government grants to government-funded student loans as the primary mechanism employed to assist lower and middle income students to fund their post-secondary education.

The goals of this research are two-fold. First, given that a series of significant reforms with respect to the treatment of government-funded or guaranteed student loans in the bankruptcy systems under review have taken place over the last decade, this research serves as a taking stock exercise. Second, given the options for dealing with student loans in bankruptcy presented by these other jurisdictions, and Canada's willingness to reassess its own choices, a number of recommendations and issues for further exploration are put forward.

A review of the current position and historical trajectory of the treatment of government student loans in bankruptcy in Canada, Australia, England, the United States and New Zealand suggests that all five jurisdictions are converging on a model where the bankruptcy system provides limited to no relief for loans made under a program funded or guaranteed by a government unit to fund a post-secondary education. This pattern of convergence has emerged in each jurisdiction through a variation of one or more of the following measures related to the bankruptcy system:

- The implementation of more restrictive discharge provisions for student loans in bankruptcy;

- The classification of government student loans as debts that are not provable in bankruptcy;

- The move to shorten the duration of the main bankruptcy process or the use of alternative processes to achieve the same result; and

- The limiting or exclusion of government student loans from alternatives to bankruptcy.

These measures were triggered in large part by the following factors:

- The haphazard judicial decision-making process for dealing with the small number of judicial applications for relief from the restrictions on discharge of student loans;

- The ability of interest groups and political parties to influence reform efforts by putting forward: (a) allegations of students abuse of the bankruptcy process; and (b) constructing education as a private benefit with the corresponding need to protect the public interest; and

- The development of a student loan securitization market.

An evaluation of the Canadian bankruptcy system's treatment of government student loans in this comparative context suggests that the following features are unique to the Canadian system:

- Canada is the only jurisdiction that is attempting to move to a less restrictive discharge for student loans;

- Canada is the only jurisdiction that has a waiting period attached to the exception to discharge for student loans; and

- Canada is the only jurisdiction that has a relatively short bankruptcy process and a restrictive exception to discharge, yet no securitization market for government-funded student loans.

In light of the experiences of the other jurisdictions under review the following key recommendation is made for the conceptual framework for considering the Canadian model for dealing with student loans in bankruptcy:

- The two key justifications relied upon to justify the current exception to discharge for government-funded student loans, student abuse of the bankruptcy process and the need to protect the public interest, should be put to rest, as they are unsubstantiated. The evidence from Canada and from all of the other jurisdictions under review demonstrates that students are not abusing the bankruptcy process. The evidence also demonstrates that, with the exception of the United States, government-funded student loans are the only government debts that are excepted from the bankruptcy discharge in bankruptcy. This is in opposition to the trend in every jurisdiction under review to remove the special treatment previously accorded to Crown debts. Further, given the growth of securitization markets for student loans, the special treatment for government-funded student loans in bankruptcy that is justified as protecting the public interest is in fact being sold to private investors.

In light of our recommendation for dispensing with the justifications for the current exception we make the following recommendations for reforming the exception:

- Further tweaking the waiting period for the exception to discharge for government-funded student loans is not advised. Rather, reform efforts should be directed at the substantive and procedural aspects of the exception. The process for making decisions about these features must be informed by empirical data.

- The current exception to discharge for government-funded student loans should be abolished. This system, that places the onus on the bankrupt to apply to the court and demonstrate good faith and financial hardship, is ineffective due to procedural obstacles relating to the onus and substantive obstacles relating to the role of bankruptcy registrars. The onus should be placed on the government to oppose a discharge where the bankrupt has not experienced financial hardship in repaying government-funded student loans and/or where there is evidence of bad faith.

The following two issues are raised for further consideration:

- If government-funded student loans continue to form an exception to the bankruptcy discharge, should they be provable in bankruptcy?

- If a no-asset low cost bankruptcy procedure is put into place in Canada, should government-funded student loans be excluded from its operation?

Part 1 of this report outlines the basic structure of government-funded student loans in Canada, the treatment of these loans in bankruptcy, and recent proposals for reform. Part 2 outlines both the measures that led to a pattern of convergence in the treatment of government-funded student loans in bankruptcy in the common law jurisdictions under review and the triggers for these measures. Situated in this comparative context, the soundness of the recommendations generated from two recent Canadian government reports on bankruptcy and Bill C-55 are considered, and recommendations and issues that need to be further explored and taken into account in considering these proposals are put forward in Part 3. Parts 4-7 are country surveys that provide a more detailed account of government-funded and guaranteed student loans and the treatment of such loans in bankruptcy in each jurisdiction under review. For the reader that is unfamiliar with the workings of these other systems under review, it may be helpful to read Parts 4-7 after reading Part 1, and before reading Parts 2 and 3. In describing the government-funded student loan programs, the country surveys draw from primary sources and a limited amount of secondary literature. A more comprehensive secondary literature review with respect to the government-funded student loan programs in New Zealand, Australia, the United Kingdom and the United States was beyond the scope of this "mini-paper."

1. Canadian Context

A central facet of the Canadian consumer bankruptcy system in its current form is the individual's right to a "fresh start" provided by the bankruptcy discharge. Following bankruptcy an individual is free from most of her debts and at the same time retains her experiences, knowledge, and values, often referred to as human capital[1], which can contribute to her becoming a productive member of society again. However, a number of exceptions to the bankruptcy discharge are provided for under existing legislation.[2] These exceptions apply to both bankruptcies and consumer proposals under the *BIA*. While a literature has developed around the justifications for a mandatory, or non-waivable, bankruptcy discharge, a comprehensive normative theory of the appropriate scope of the discharge and accompanying exceptions has eluded commentators for some time now. A common explanation for this list of debts is that they all concern fraud or similar misbehavior against creditors and excluding them from discharge is intended to deter this conduct. However, the list excludes a large number of "wrongdoers," such as bankrupts who have committed torts other than the three that are listed. In particular, bankrupts who owe tax and non-tax debts to the government, such as unemployment insurance overpayments or small business loans, are not included in the list. There is no obvious rationale for this list of debts.

Government Student Loans[3] are found in the existing list of exceptions to discharge.[4] The primary justification for the enactment of the exception to discharge for Government Student Loans in Canada was that without it a significant number of students were blatantly manipulating the bankruptcy system by finishing their post-secondary studies, and then going bankrupt to erase their Government Student Loans before profiting from professions such as law or medicine.

A. Overview of Government Student Loans

In Canada, students who cannot afford the cost of a post-secondary education rely on a range of credit products to fund their studies. Many students (and parents) use lines of credit, extended mortgages, private loans, and credit cards to fund their education. The only form of student credit that is not based on a positive past-credit history and accordingly is most accessible to students from low and middle-income families, is a Government Student Loan. Government Student Loans are made based on assessed student need, and do not charge interest while students are engaged in part- or full-time studies. In 2003, 42 per cent of all post-secondary students relied on federal Government Student Loans.[5] Out of these

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[1] "You cannot separate a person from his or her knowledge, skills, health or values the way it is possible to move financial and physical assets while the owner stays put." Gary S. Becker, "Human Capital, A Theoretical and Empirical Analysis with Special Reference to Education", National Bureau of Economic Research (University of Chicago Press, Chicago, 1993) at 16.

[2] *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, s. 178(1) [*BIA*]. The debts identified in this section include fines imposed by a court; alimony, maintenance or support payments owing; damages awards arising from civil proceedings for bodily harm, sexual assault or wrongful death; debts and liabilities arising out of fraud; and government student loans.

[3] A "Government Student Loan" is any debt or obligation in respect of a loan made under the *Canada Student Loans Act*, the *Canada Student Financial Assistance Act* or any enactment of a province that provides for loans or guarantees of loans to students. This includes loans made by private banks participating in government student loan programs.

[4] *BIA, supra* note 2, s.178(1)(g).

[5] Human Resources and Skills Development Canada, "Student Loans Program Annual Report 2002-2003" (2004), online: Student Loans Program Annual Report 2002 – 2003

students, 58.8 per cent were women and 41.2 per cent were men.[6] Approximately 16.8 per cent of the student borrowers were high-need part-time students, high-need students with permanent disabilities, females pursuing doctoral studies or students with dependents.[7]

Government Student Loans are provided to students based on federal-provincial partnerships in nine provinces and the Yukon.[8] In these participating provinces and the Yukon, provincial and territorial student assistance offices administer the front end of both provincial and federal student loans. Generally, students hold two separate Government Student Loans: a provincial loan and a federal loan. However, pursuant to Canada-Provincial Integrated Student Loan Agreements,[9] four provinces – Ontario, Saskatchewan, New Brunswick, and Newfoundland - have integrated their student loan programs with the federal program such that students receive only one loan funded by both the federal and provincial governments. This loan is subject to the terms of the federal student loan program.

The federal government directly finances all federal student loans issued on or after August 1, 2000 through the National Student Loans Service Centre (NSLSC).[10] Provincial or territorial student assistance offices review both federal and provincial loan applications, confirm eligibility, assess financial need, and determine the amount of funding students will receive. The NSLSC processes loan documents, arranges for loan funds to be deposited to the student's bank account, keeps track of the total amount of the loan throughout the student's studies and the amount she will have to repay, sets up a loan repayment schedule, and administers debt-relief programs. Under the current scheme, there is no maximum repayment period, but a typical repayment period is 9.5 years.[11] Students are entitled to a six-month grace period after leaving part or full-time studies before having to make payments on their loan.[12] However, interest accrues on the loan during the grace period.[13]

<http://www.hrsdc.gc.ca/en/hip/cslp/publications/12_pu_AnnualReport20022003.pdf> at 2 [hereinafter Annual Report].

[6] *Ibid.* at 3.

[7] *Ibid.* at 20. These are students who are eligible to receive Canada Study Grants (CSGs) from the federal government. Information on the specific per cent of students falling in each category is not provided in the CSLP 2002-3 Annual Report. CSGs are non-repayable and accordingly a detailed discussion of their operation is beyond the scope of this report.

[8] Quebec, Northwest Territories, and Nunavut have opted out of the federal student loan program and receive alternative payments to operate their own programs.

[9] Edulinx, online: Canada-Provincial Integrated Student Loans <http://www.edulinx.ca/index.php?option=com_content&task=view&id=57&Itemid=58> (date accessed: 19 July 2005).

[10] The government, through the NSLSC, contracts out the administration of the program, including debt-relief options, to two private service providers. Edulinx administers loans issued to students attending not-for-profit universities and colleges and BDP administers loans issued to students enrolled in for-profit training companies. Nelnet, Inc. acquired Edulinx from CIBC for an undisclosed price on November 30, 2004. Edulinx services approximately one million Government Student Loans totaling approximately $7 billion. The company was originally established in 1999. CIBC became the sole owner of Edulinx in January 2002. A significant part of Nelnet's business is the securtization of education finance assets. See www.shareholder.com/Common/ Edgar/1258602/930413-05-3765/05-00.pdf. Edulinx sub-contracts with Canada Post to handle the processing of loan documents and the depositing of funds into students' accounts. See Canadian Federation of Students, Membership Advisory, "Latest Changes to the Canada Student Loan Program" (March 2001), online: Membership Advisory <http://www.cfs-fcee.ca/html/english/research/factsheets/ma-200103-cslp.pdf> (date accessed: 20 July 2005) at 1 [hereinafter Membership Advisory].

[11] Interview of L. Wanczycki, Policy Advisor (27 June 2005) CSLP, Human Resources and Skills Development Canada. This information was not available on the NSLSC website or guide.

[12] *Canada Student Loans Act*, R.S.C. 1985, c. S-23, s. 5.

[13] *Ibid.*, s. s. 4(2)(b).

Following the grace period, for provinces that have not reached Canada-Provincial Integrated Student Loan Agreements, students are required to consolidate their provincial and federal student loans and to decide on a fixed or floating rate of interest to repay their loans.[14]

Following the 1998 federal budget, a number of forms of relief were introduced, or expanded, for students having trouble repaying their Government Student Loans due to financial hardship. These forms of relief are still in place today. Prior to regulatory changes enacted in 2004 and 2005, these options were extremely limited as they were only available to borrowers with loans in good standing and also imposed very low income thresholds. The 2004 Amendments replaced the good standing requirement for obtaining relief with more lenient specific eligibility requirements and also increased the amount of available relief.[15] The 2005 Amendments increased the income thresholds for obtaining relief by five per cent and also further increased the amount of available relief.[16] While the 2004 and 2005 Amendments have extended eligibility and increased the amount of assistance provided through the government's debt relief programs, the requirements for obtaining relief remain complex and the income thresholds remain relatively low. It is still too early to determine the impact of these amendments.

The central form of relief is Interest Relief.[17] Interest does not accrue while a borrower is receiving Interest Relief. This form of relief is based on gross family income, family size, and the principal owing on student loans. Interest Relief is typically granted for six-month periods, up to a maximum of 30 months, throughout the lifetime of the loan. Extended Interest Relief,[18] which is available to students who are unable to make payments within five years of leaving school, extends Interest Relief benefits for up to an additional 24 months. The government may also agree to a revision of terms[19] and extend the loan repayment period or reduce monthly payments for a short period of time.

Two other "last resort" forms of debt-relief are available to students: the Debt Reduction in Repayment Program and the Permanent Disability Benefit. Under the Debt Reduction in Repayment Program, where a student has exhausted all other avenues and has been out of school for five years, she may apply to have her loan principal reduced. If approved for the program, she could be eligible to receive an initial reduction of up to $10,000; and if she continues to experience financial difficulty, she may apply for a second and a third reduction in amounts of up to $10,000 and $6,000 respectively.[20] The total availability of

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[14] The current federal fixed interest rate is Prime plus 5 per cent, while the floating rate is Prime plus 2.5 per cent. Students have the option to change to a fixed rate at any time. See HRDC Evaluation of the Canada Student Loans Program, 1.0 Introduction, (23 February 1999), online: Human Resources Development Canada <http://www11.hrdc-drhc.gc.ca/pls/edd/CSL_55028.htm> (date accessed: 21 April 2005) at para. 11 [hereinafter HRDC]. .

[15] S.O.R./2004-120 (effective May 11, 2004) [hereinafter 2004 Amendments].

[16] S.O.R./2005-152 (effective August 1, 2005) [hereinafter 2005 Amendments].

[17] *Canada Student Financial Assistance Act*, s.7 and *Canada Student Financial Assistance Regulations*: S.O.R./95-329, s. 19. See also National Student Loans Service Centre, online: Integrated Interest Relief <http://www.canlearn.ca/NSLSC/support/new/nlwhanew3.cfm?langnslsc=en> (date accessed: 25 April 2005) [hereinafter Integrated Interest Relief].

[18] *Canada Student Financial Assistance Act*, *ibid.* and *Canada Student Financial Assistance Regulations*, *ibid.*, ss. 19 & 20. See also Integrated Interest Relief, *ibid.*

[19] National Student Loans Service Centre, online: Revision of Terms <http://www.canlearn.ca/nslsc/repay/On/nlObtRepAss.cfm?LANGNSLSC=en&IT=PUBLIC&row=3> (date accessed: 25 April 2005).

[20] *Supra* note 17, s. 42.1. See also National Student Loans Service Centre, online: Debt Reduction in Repayment

$26,000 in debt reduction represents an increase from the $10,000 maximum that was in place prior to the 2004 and 2005 Amendments. In order to qualify for benefits under the Debt Reduction in Repayment Program, a student must have used all 30 months of benefits under the Interest Relief Plan; must be in good standing with the NSLSC and/or her financial institution, with not more than two months in arrears owing on her debt; and her loan payments must exceed a given percentage of her income, as established by the Debt Reduction in Repayment Income Table appended to the *Canada Student Financial Assistance Regulations*.[21] If a student has a permanent disability, and is experiencing exceptional financial hardship in repaying her loan due to the disability, she may also qualify for the Permanent Disability Benefit, where all or a portion of her Government Student Loan is forgiven.[22]

For provinces that have not reached Canada-Provincial Integrated Student Loan Agreements, there are some variations between the federal debt-relief options and the provincial debt-relief options for repayment of Government Student Loans. For example, under the Alberta Loan Relief Program, enacted on August 1, 2001, students who receive more than $5000 per year in combined Alberta and federal loans may qualify for relief. Financial assistance above $5000 may be provided as a Loan Relief benefit, which is not repayable.[23] In Manitoba, the maximum amount of debt reduction is $6667 compared to $26,000 now available for federal loans.[24] In Nova Scotia, students must apply for debt reduction within three months of graduation. The percentage of debt reduction is graduated based on completed year of study and ranges from 15 per cent to 45 per cent. In addition, borrowers may qualify for an Employment Bonus Award or Repayment Bonus Award and receive an additional 25 per cent or 10 per cent, respectively, of the amount of debt reduction they received at graduation.[25]

Until May 11, 2004, when the 2004 Amendments came into effect, students who filed a proceeding under the *BIA* were not eligible for new federal Government Student Loans and they could not obtain the benefits of the federal governments' debt relief programs for existing Government Student Loans. A student who files a proceeding under the *BIA* may now be eligible to obtain Government Student Loans for a maximum of three years, provided he/she remains in the same program of study and continues in full-time status; and he/she may also be eligible for the government's debt relief programs.[26]

<http://www.canlearn.ca/nslsc/repay/On/nlObtRepAss.cfm?LANGNSLSC=en&IT=PUBLIC&row=5> (date accessed: 25 April 2005).

[21] *Ibid.*

[22] *Supra* note 17, s. 43.1(1)(b). See also National Student Loans Service Centre, online: Permanent Disability Benefit <http://www.canlearn.ca/nslsc/repay/On/nlObtRepAss.cfm?LANGNSLSC=en&IT=PUBLIC&row=6> (date accessed: 25 April 2005).

[23] Edulinx Canada Corporation, online: Repayment Assistance – Provincial and Territorial Loans <http://www.edulinx.com/index.php?option=com_content&task=view&id=55&Itemid=64> (date accessed: 20 July 2005) [hereinafter Edulinx].

[24] *Ibid.*

[25] Nova Scotia Department of Education – Student Loans (Student Assistance), online: Debt Reduction Program Information <http://studentloans.ednet.ns.ca/student_debt_reduction.shtml> (date accessed: 20 July 2005).

[26] 2004 Amendments, *supra* note 15. See also, Office of the Superintendent of Bankruptcy Canada, "Notice of Changes to the Regulations Under the Canada Student Loan Program" online: Office of the Superintendent of Bankruptcy <http://strategis.ic.gc.ca/epic/internet/inbsf-osb.nsf/en/br01439e.html> (date accessed: 4 August 2005).

B. Proposals and Reforms

In the last five years a number of proposals have been put forward to increase the number and the value of student loans provided by the federal and provincial governments as well as to amend the current legislation on the treatment of these loans in bankruptcy.

The most recent recommendation to increase the number and the value of government-funded student loans came out of a report commissioned by the Ontario government. In the 2004 Ontario budget the government announced a review of the design and funding of postsecondary education in Ontario. Premier Dalton McGuinty appointed the Honourable Bob Rae as the advisor to the Premier and the Ministry of Training, Colleges and Universities, who with the support of a seven-member advisory panel was asked to advise on two issues: the design of a publicly funded postsecondary system and funding models for this system. The Rae Review was released in February 2005.[27] The report, which has attracted significant attention around the country, recommended that the current freeze on tuition fees in place in Ontario should be lifted and that individual institutions should be free to set their own tuition.[28] The position of the Rae Review was justified by a condition precedent for tuition fees to be raised: more students should be eligible for government-subsidized financial assistance.[29]

The status of Government Student Loans in bankruptcy received significant attention in the two recent Canadian government reports on bankruptcy: the Personal Insolvency Task Force Report published in December 2002[30] and the Senate Report published in November

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[27] B. Rae, "Postsecondary Review: Higher Expectations for Higher Learning" (Report & Recommendations submitted to the Premier by the Minister of Training, Colleges and Universities, February 2005) at 23 [Rae Review].

[28] See, for example, a sample of the numerous newspaper articles on the topic following the release of the Rae Review: "Rae Review's Funding Flaw" *The Toronto Star* (21 February 2005) A17; I. Robertson, "Students Fight Fees; Even Rae Comes Under Fire" *The Toronto Sun* (4 February 2005) 4; B. Whitwham, "Summerlee Doesn't Expect Surprises in Rae Review" *The Guelph Mercury* (5 February 2005) A1; P. George, "Value of Universities Reflected in Many Ways" *The Hamilton Spectator* (5 February 2005). See also Ontario, Legislative Assembly, "Excellence Accessibility Responsibility: Report of the Advisory Panel on Future Directions for Postsecondary Education" by D. C. Smith (Chair) (1996), online: Ministry of Education and Ministry of Training, Colleges and Universities <http://www.edu.gov.on.ca/eng/document/reports/futuree.html#sharing> (date accessed: 20 July 2005). Historically, Newfoundland, Nova Scotia, Prince Edward Island, Saskatchewan and Alberta have not regulated tuition fees. New Brunswick and Manitoba occasionally imposed tuition regulations. Prior to the 1990s, Ontario, British Columbia, and Quebec regulated tuition fees. See, Canadian Federation of Students, Fact Sheet 1998 5:5, "Deregulation of Tuition Fees" (November 1998), online: Deregulation of Tuition Fees <http://www.cfsontario.ca/policy/factsheets/fs-5(5)-deregulation.pdf> (date accessed: 20 July 2005) at 3-4. Similar to Ontario, British Columbia deregulated tuition fees in 2002. However, in the 2005 Throne Speech, the government announced that they would be re-regulating tuition fees, after fees more than doubled during the period of deregulation. Tuition fees will be capped at the rate of inflation. See, Canadian Federation of Students, Media Release, "Campbell Second-Guesses BC Tuition Fee Policy" (9 February 2005), online: Media <http://action.web.ca/home/cfs/en_alerts.shtml?x=72136> (date accessed: 20 July 2005). The Ontario example, which is demonstrative of national tuition fee trends and debates, is used to develop the context for the focus of this report on student loans in bankruptcy. The Ontario example is chosen because it recently provoked significant national scrutiny. A detailed review of tuition trends around the country is beyond the scope of this report.

[29] Rae Review, *supra* note 27, at 23.

[30] Office of Superintendent of Bankruptcy Canada, Personal Insolvency Task Force Final Report (August 2002), online: <http://www.strategis.ic.gc.ca/epic/internet/inbsf-osb.nsf/en/h_br01225e.html> (date accessed: 5 August 2005).

2003.[31] Both reports indicated that reforms were in order to deal with the current exception to the bankruptcy discharge for Government Student Loans, which provides for limited relief on financial hardship grounds, on an all-or-nothing basis, following a costly court application that is only possible 10 years after the bankrupt or former bankrupt has ceased to be a full- or part-time student.[32] Both reports referenced empirical data[33] that detailed the dire financial circumstances of bankrupts with student loans relative to those without student loans and demonstrated that such bankrupts where generally not high-income professionals attempting to defraud the system. Further, the reports indicated that the existing legislation was ill-equipped to address intervening life events such as illness, disability, and family breakdown which often accounted for unpaid Government Student Loans and warranted a fresh start. To this end, both reports recommended that the exception to discharge for Government Student Loans should be amended to apply only in situations where it had been less than five years since the bankrupt completed full or part-time studies that the loans had funded. As well, both reports recommended an amendment that would provide courts with the discretion to confirm the discharge of all or a portion of a Government Student Loan before the five-year period has lapsed where the bankrupt could establish that the burden of maintaining the liability for some or all of the debt would result in financial hardship.

In addition to the government reports on bankruptcy, the 10-year exception to discharge has also been met with a great deal of criticism by bankruptcy trustees and student groups. Bankruptcy trustees, who are concerned with the impact the 10-year exception has on their ability to come up with a reasonable solution to debtors' financial distress, have criticized the exception as unduly harsh.[34] Student groups supported what was ultimately an unsuccessful legal action to challenge the exception under the equality provisions of the *Canadian Charter of Rights and Freedoms*.[35]

In the last year, two bills have been introduced that attempt to vary the timing of the exception to discharge for Government Student Loans. One of these two bills has been

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[31] Canada, Standing Senate Committee on Banking, Trade and Commerce, *Debtors and Creditors Sharing the Burden: A Review of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (Ottawa: 2003), online: Senate of Canada < http://www.parl.gc.ca/37/2/parlbus/commbus/senate/com-e/bank-e/rep-e/bankruptcy-e.pdf> (date accessed: 4 August 2005).

[32] Where a student returns to school after the 10-year period has commenced, the clock is restarted.

[33] See S. Schwartz, "The Dark Side of Student Loans: Debt Burden, Default, and Bankruptcy" (1999) 37 Osgoode Hall L.J. 317, for a summary of this data at 329:
"The economic situation of all those declaring bankruptcy suggests that bankruptcy is used primarily as a last resort. The economic situation of those seeking bankruptcy protection with student loans among their debts, or whose student loans were critical in their bankruptcy, is even worse than the already desperate situation of the whole group. To be sure, they are younger and have more education, but they have lower annual household income and lower monthly income at the time of filing for bankruptcy. More than 40 per cent had received income assistance in the two years previous to filing, and about 30 per cent had received unemployment insurance. A surprisingly large portion – more than one-third – had occupations that were unskilled."

[34] See for example, Hoyes and Michalos, online: Canada and Ontario Student Loans in Bankruptcy <http://www.hoyes.com/student_loan_bankruptcy_Canada.htm> (date accessed: 4 August 2005).

[35] See Canadian Federation of Students, "Bankruptcy Charter Challenge" (April 2005), online: Campaigns & Lobbying <http://www.cfs-fcee.ca/html/english/campaigns/bankruptcy_charter.php> (date accessed: 26 April 2005). The decision was released on June 30, 2005: *Chenier v. Canada (Attorney General)*, 2005 CanLII 23125 (Ont. Sup. Ct.) (CanLII) [*Chenier*]. Justice Sedgwick held that the exception was "not based on an individual's "needs, merits or capacities." He was not convinced that the exception does anything more than distinguish between Government Student Loan debtors and other debtors on the grounds of the nature of the debt. Justice Sedgwick described outstanding Government Student Loans as reflecting an economic condition and not a personal characteristic.

defeated. On October 20, 2004,[36] Alexa McDonough (Halifax, NDP) introduced Bill C-236,[37] which would have amended the *BIA* to "reduce, from ten to two years after a bankrupt leaves school, the period of time during which an order of discharge does not release the bankrupt from the reimbursement of his or her student loan."[38] The bill was subsequently defeated in a motion held on April 13, 2005.[39]

Most recently, on June 3, 2005, the federal government unveiled a package of long awaited amendments to Canadian bankruptcy legislation in Bill C-55 titled: *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts.*[40] Bill C-55 would reduce the period for the exception to discharge for Government Student Loans from 10 years to seven years following the completion of full or part-time studies.[41] The bill would also reduce the period of time before an application for relief from the exception to discharge could be made from 10 years to five years.[42] Like Bill C-236 and the government reports recommending a change in the timing of the exception, Bill C-55 does not propose a principled amendment to the substance of the exception. For example, the requirement of making a judicial application for relief following the waiting period in order for any relief from the exception to be granted is left intact.

1. Measures Towards Convergence and Triggers

A. More Restrictive Discharge Provisions

In all the countries considered, it has become increasingly more difficult or impossible to discharge government-funded student loans. Only in New Zealand and, in a more limited way, Australia, can government-funded student loans still be discharged in bankruptcy.

Out of the countries considered, the United States (U.S.) was the first to create an exception to discharge for government-funded or guaranteed student loans. In 1976, Congress enacted the nondischargeability provision in response to claims that recent graduates were abusing the bankruptcy system by eradicating their debts immediately upon graduation.[43] Originally, there were two exceptions to the nondischargeability provision that applied to student loans. A debtor could discharge the loans in a Chapter 7 bankruptcy proceeding if

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[36] *House of Commons Debates*, 012 (20 October 2004) at 1525 (Ms. Alexa McDonough).
[37] *Canada* Bill C-236, *An Act to amend the Bankruptcy and Insolvency Act (student loan)*, 1st Sess., 38th Parl., 2004.
[38] *House of Commons Debates*, 065 (25 February 2005) at 1300 (Ms. Alexa McDonough).
[39] *House of Commons Debates*, 081 (13 April 2005) at 1525 (Hon. Peter Milliken).
[40] *Canada* Bill C-55, *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, 1st Sess., 38th Parl., 2005 (first reading in House of Commons 3 June 2005) [hereinafter Bill C-55].
[41] *Ibid.*, cl. 107(2): "Subparagraph 178(1)(g)(ii) of the Act is replaced by the following: (ii) within seven years after the date on which the bankrupt ceased to be a full- or part-time student".
[42] *Ibid.*, cl. 107(3): "Subsection 178(1.1) of the Act is replaced by the following: (1.1) At any time after five years after a bankrupt who has a debt referred to in paragraph 1(g) ceases to be a full- or part-time student, as the case may be, under the applicable Act or enactment, the court, may on application, order that subsection (1) does not apply to the debt if the court is satisfied that (a) the bankrupt has acted in good faith in connection with the bankrupt's liabilities under the debt; and (b) the bankrupt has and will continue to experience financial difficulty to such an extent that the bankruptcy will be unable to pay the debt."
[43] B. Hennessy, "The Partial Discharge of Student Loans: Breaking Apart the All or Nothing Interpretation of 11 U.S.C. 523 (A)(8)" (2004) 77 Temp. L. Rev. 71 at 73.

five years had lapsed after the loan matured or if the debtor could establish undue hardship.[44] These exceptions were included in response to criticisms regarding the lack of empirical evidence of abuse and to preserve the spirit of the *Bankruptcy Code*.[45] The five-year exception was later extended to seven years, but was subsequently abolished by *The Higher Education Amendments* in 1998.[46] Today, the only remaining relief from the exception to discharge for student loans is the undue hardship provision. This is the case for both a Chapter 7 and a Chapter 13 proceeding. Most recently, on April 20, 2005, the government passed an amendment that extends the nondischargeability provision.[47] The provision previously applied only to government and non-profit student loans and now includes student loans issued by for-profit entities.[48] The U.S. is the only jurisdiction under review to have extended the application of the exception to discharge to non-government funded or guaranteed student loans.

The U.S. congress did not define what constitutes "undue hardship," but rather left it open to the judiciary to construct an appropriate definition. The American courts have developed increasingly more complex tests for what constitutes "undue hardship" that have provided limited relief to applicants and have been described by Jennifer Frattini as resulting in "the formation of various stringent judicial interpretations of 'undue hardship' which have the effect of undermining the first goal of bankruptcy – providing the honest, overburdened debtor with a fresh start."[49] A recent empirical study of the 261 reported undue hardship decisions issued by U.S. bankruptcy courts within the 10 year period beginning on October 7, 1994 and ending on October 6, 2003, demonstrated that there were few statistically significant differences in the factual circumstances of the debtors who were granted a discharge versus those who were not.[50] The authors of this empirical study were less concerned with the frequency with which relief was granted and more concerned with the judicial process and the small number of debtors who had the financial wherewithal to litigate a claim of undue hardship.[51] The authors observed that nearly half of the discharge determinations analyzed concluded that failing to discharge a debtor's student loans would impose undue hardship on the debtor.[52] However, the authors were critical of the haphazard fashion in which courts determined whether a debtor's circumstances supported a claim of undue hardship.[53]

In Canada, in 1997, Government Student Loans were made nondischargeable in bankruptcy if they had been incurred within two years of the bankrupt leaving school.[54] A debtor could apply to the court for a discharge of her debts after the two-year period if she could demonstrate that she had acted in good faith and could not repay her loan due to financial difficulty.[55] Government Student Loans incurred outside the two-year period were treated

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[44] *Ibid.* at 118.
[45] *Ibid.*
[46] C. Morea, "Student Loan Discharge in Bankruptcy – It is Time for a Unified Equitable Approach" (1999) 7 Am. Bankr. Inst. L. Rev. 193 at n 2.
[47] *The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*, Pub. L. No. 109-8 § 220, 119 Stat. 23, 59 (to be codified at 11 U.S.C. § 523(a)(8)(B)).
[48] *Ibid.*
[49] J. Frattini, "The Dischargeability of Student Loans: An Undue Burden?" (2001) 17 Bank. Dev. J. 537 at 541.
[50] R. Pardo and M. Lacey, "Undue Hardship in the Bankruptcy Courts: An Empirical Assessment of the Discharge of Educational Debt" (Tulane University School of Law, Public Law and Legal Theory Research Paper Series, Research Paper No. 05-06 (August, 2005)).
[51] *Ibid.*
[52] *Ibid.*
[53] *Ibid.*
[54] *An Act to Amend the Bankruptcy and Insolvency Act*, 1997, c. 12 (Bill C-5).
[55] *Ibid.*

in the same way as other unsecured debts and discharged. In 1998, this two-year exception to discharge was increased to 10 years making it even more difficult for students to discharge their student loans.[56] A critique similar to the critique levelled against the manner in which U.S. courts have dealt with judicial applications for relief has been put forward in the Canadian context.[57]

The most recent jurisdiction to exempt government-funded student loans from the bankruptcy discharge is the United Kingdom (U.K.). In 2004, the U.K. enacted the *Higher Education Act 2004*,[58] which took government-funded student loans outside of the bankruptcy realm.[59] Prior to 2004, student loans were provable and could be discharged in bankruptcy.

B. Government Student Loans Not Provable

In Australia, prior to the introduction of the *Higher Education Support Act 2003*, government-funded semester and accumulated student loan debts were provable but not extinguished in bankruptcy. With the introduction of the *Higher Education Support Act 2003,* these loans were classified as non-provable. Bills Digest No. 159, regarding the *Higher Education Funding Amendment Bill 2001*, states that since the Commonwealth retains the prospect of repayment, because these loans are not extinguished in bankruptcy, it should not be able to claim a share of the sale of the bankrupt's assets, thus reducing the amount available to other creditors who have no future hope of repayment.[60] Accordingly, subsequent reforms to the *Bankruptcy Act 1966* that reference the *Higher Education Support Act 2003* exempt semester and accumulated student debts completely from the operation of bankruptcy. The treatment of assessment debts remains unchanged; they are provable and extinguished in bankruptcy.

Similarly, in the U.K., one rationale advanced by the House of Commons Standing Committee on March 9, 2004, in support of the treatment of government-funded student loans under the *Higher Education Funding Act 2004*, was that classifying student loans as non-provable would leave more money available to other creditors.[61]

C. Perceived Abuses of the Bankruptcy System

In all of the countries under review, the most influential rationale for the introduction of more restrictive discharge provisions regarding student loans was the claim that the bankruptcy process was susceptible to abuse by students who were eager to rid themselves of their loans prior to embarking on lucrative careers. A further trend is that these allegations of abuse were rarely substantiated.

In the U.K. Margaret Hodge, the former Minister of Lifelong Learning and Higher Education, initiated and supported legislative reforms that effectively eliminated bankruptcy as an option for debt relief for outstanding government-funded student loans based on concerns about potential abuse. She was concerned that students viewed bankruptcy as an easy route to avoid repaying student loans.[62] On March 9, 2004, the House of Commons

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[56] *Budget Implementation Act,* 1998, S.C. 1998 c.21, s. 103, amending the *BIA*.
[57] S. Ben-Ishai, "One Paradox of the Bankruptcy Fresh Start: Government Student Loans" (Forthcoming in (2005) Annual Insolvency Review).
[58] *Higher Education Act 2004* (U.K.), 2004, c. 8, s. 42 [hereinafter *HEA*].
[59] *Ibid.*
[60] *Higher Education Funding Amendment Bill 2001* (Cth.), Bill Digest No. 159 (2001).
[61] U.K., H.C., *Standing Committee Debates* col. 578 (9 March 2004) (Mr. Willis).
[62] *Ibid.*, col. 572.

Standing Committee acknowledged that the number of students claiming bankruptcy had increased dramatically from eight in 1992 to 899 in 2003.[63] However, the Committee further acknowledged that the number of students claiming bankruptcy was less than one per cent of the total number of students with government-funded loans.[64] These statistics did not support the contention that the bankruptcy process was in jeopardy of being abused. Nevertheless, the House of Commons Standing Committee advanced this rationale in support of the recent legislative reforms.

Similarly, in 1976, the U.S. Congress enacted a nondischargeability provision to "ensure the viability of student loan programs by preventing students with fraudulent intentions from deliberately abusing the bankruptcy system by incurring massive loan obligations, obtaining a free education, then filing a petition to have all their debts wiped out."[65] Opponents of the nondischargeability provision for government student loans noted that there was little empirical evidence of abuse. The cases of fraudulent abuse were rare, but were sensationalized by the media.[66] A study by the General Accounting Office, conducted prior to the implementation of 523 (a) (8), revealed that only a fraction of one per cent of matured student loans had been discharged in bankruptcy.[67]

In Canada, similar concerns about abuse prompted the introduction of the two-year nondischargeability provision for student loans. For example, Mr. Tobin, during Proceedings of the Standing Senate Committee on Banking, Trade and Commerce, stated, "We are trying to avoid situations where someone declares bankruptcy simply to get rid of their student loan and then finds a job."[68] No empirical data has been put forward to justify this contention. Rather, empirical data has demonstrated that this is not the case.[69]

With the introduction of the Higher Education Loan Programme (HELP) in Australia, a greater number of students had access to student loans. There was a fear that as more students acquired loans the instances of abuse would increase.[70] Therefore, one rationale for exempting semester and accumulated student debts from the bankruptcy process was to mitigate these potential instances of abuse.[71] Again, no empirical data was put forward to justify this concern.

In New Zealand, the Student Loan Scheme was enacted to support the government's social and economic goals for higher education. Since 1990, education policy has required students to contribute more to the costs of their education. The shift toward greater student contribution is based on the increased demand for higher education, increased costs incurred to meet this demand and pressure to reduce government spending. An argument is also advanced that the student, who accrues the benefits from higher education, should be required to pay more for those benefits.[72] However, based on the punitive aspects that remain in the New Zealand bankruptcy process - the inability to obtain funding under the Student Loan Scheme, the requirement of consent from the Official Assignee or the court before leaving New Zealand, restrictions on employment in certain positions and restrictions on obtaining credit over $100 - and the lack of empirical evidence to suggest that students

[63] *Ibid.*, col. 571.
[64] *Ibid.*, col. 577.
[65] Frattini, *supra* note 49 at 541.
[66] Hennessy, *supra* note 43 at 74.
[67] *Ibid.*
[68] Canada, Senate, Proceedings of the Standing Senate Committee on Banking, Trade and Commerce Issue 13 – Evidence (4 November 1996) (Mr. Tobin).
[69] Schwartz, *supra* note 33.
[70] Interview of B. Cruickshanks (31 May 2005) from Insolvency and Trustee Services Australia.
[71] *Ibid.*
[72] N.Z., "Student Loans and Funding for Tertiary Education", November 5, 1999, Parliamentary Library.

are currently abusing the bankruptcy process, no attempts have been made to introduce an exception to discharge for student loans under the Student Loan Scheme.

In the context of the proposed "no-asset procedure," because there is less stigma, a shorter term and fewer restrictions than bankruptcy, there is a fear that students will resort to the process only to discharge their student debt. The government predicts that by preventing the discharge of student loan debt under the Student Loan Scheme in a "no-asset procedure," 250 debtors will be affected.[73] All other provable debts (apart from debts which are non-dischargeable in bankruptcy, such as child maintenance orders) will be dischargeable through the "no-asset procedure."[74]

D. Increasing Number and Value of Student Loans

In all of the countries under review, claims surrounding abuse of the bankruptcy process by students proliferated with an increase in the number and the value of government-funded student loans. Using this rationale, with the exception of New Zealand, nondischargeability provisions were enacted as a response when the number and the value of student loans, and associated defaults, were anticipated to rise.

As noted above, leading up to the enactment of the nondischargeability provision in the U.K. in 2004, the number of students claiming bankruptcy had dramatically increased from eight in 1992 to 899 in 2003.[75] There were also proposals to increase tuition fees and abolish upfront fees, which would necessitate the need for greater student loan support.[76] In anticipation of this increased demand, the U.K. opted to exempt student loans from bankruptcy.

In Canada, prior to the introduction of the nondischargeability provision in 1997, the number of student loan defaults increased from only nine per cent in 1980 to 17 per cent in 1990.[77] In 1997 when the nondischargeability provision was introduced, the government had reportedly lost $70 million in 1996-97 on Government Student Loans in bankruptcy up from $30 million in 1990 – 1991.[78] In 1990-1991, 223,505 full-time students received federal Government Student Loans with an average value of $2863.[79] In comparison, in 1996 -1997, 343,224[80] full-time students received federal Government Student Loans with

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[73] See New Zealand Ministry of Education, "A Guide to the Student Support Changes" (May 2004) online: A Guide to the Student Support Changes <http://www.minedu.govt.nz/web/downloadable/dl9643_v1/9643-student-support-guide.pdf> (date accessed: 4 August 2005).

[74] See Ministry of Economic Development, Draft Insolvency Law Reform Bill: Discussion Document (April 2004), online: Draft Insolvency Law Reform Bill: Discussion Document <http://www.med.govt.nz/ri/insolvency/review/draft-bill/discussion/index.html> (date accessed: 4 August 2005).

[75] *Supra* note 61, col. 571.

[76] L. Dearden et al., "Higher Education Funding Policy: Who Wins and Who Loses? A Comprehensive Guide to the Current Debate" (London: The Institute for Fiscal Studies, 2005) at 1.

[77] Schwartz, *supra* note 33 at 317.

[78] *Ibid.* at 318.

[79] Human Resources and Skills Development Canada, "Evaluation of the Canada Student Loans Program" (1997), online: 2.0 Profile of Canada Student Loan Program < http://www.hrsdc.gc.ca/asp/gateway.asp?hr=/en/cs/sp/edd/reports/1997-000340/page06.shtml&hs=cxp> (date accessed: 4 August 2005) [hereinafter HRSDC].

[80] Human Resources and Skills Development Canada, "Number of Canada Student Loans Borrowers for 1996-1997 (Full-Time Students Only)", online: Canada Student Loans Program Statistics <http://www.hrsdc.gc.ca/asp/gateway.asp?hr=/en/hip/cslp/statistics/03_st_Borrowers1996.shtml&hs=cxp> (date accessed: 4 August 2005).

an average value of $4615.[81] This represented an increase of 53.6 per cent in the number of borrowers and a 61.2 per cent increase in the average value of the loans received in that period.

In the U.S., student loans were first exempt from discharge under the *Bankruptcy Reform Act of 1978*. One goal of the *Bankruptcy Reform Act of 1978* was to rescue "the student loan program from fiscal destruction."[82] From 1978 to 1981, the percentage of students with student loans increased from 15 per cent to 33 per cent.[83] Federal outlays for the program went from $500 million in 1978 to $2.3 billion in 1981.[84] The increase in student loans was a result of legislative amendments,[85] which promoted increased accessibility to higher education and increased tuition fees charged by colleges.[86]

Although New Zealand still permits government-funded student loans to be discharged in bankruptcy, the government is currently experiencing an increase in the number of student loans that are written off each year. In 2002, total student debt owing to the government was over $5 billion, and only one in ten students was debt free.[87] The New Zealand University Students' Association estimates that by 2020 total student debt in New Zealand will rise to almost $20 billion, an amount the country's Auditor General believes could be "potentially a major source of risk" to New Zealand's national government.[88] In June 2004, $8.5 million in student loans was written off for 542 borrowers compared to $3.5 million for 326 borrowers in June 2003.[89]

E. Protecting the Public Interest: Recipient of Benefit Should Pay

The legislative debates and government reports coming out of the countries under review reveal a consensus that students, as the primary beneficiaries of higher education, should be required to contribute to the cost of their education through tuition fees. This line of reasoning has been used in the bankruptcy context to claim that students should not be able to skirt these contributions by using bankruptcy to discharge loans incurred to cover these costs. Insisting that students contribute to their education and prohibiting the discharge of student loans in bankruptcy are often justified by policies that are based on the need to protect the public interest, namely taxpayer dollars that are used to finance student loan programs.

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[81] Human Resources and Skills Development Canada, "Average Dollar Amount of Negotiated Canada Student Loans (CSL) Full-Time Students Only", online: Canada Student Loans Program Statistics <http://www.hrsdc.gc.ca/asp/gateway.asp?hr=/en/hip/cslp/statistics/10_st_DollarAmount.shtml&hs=cxp> (date accessed: 4 August 2005).

[82] R. Roots, "The Student Loan Debt Crisis: A Lesson in Unintended Consequences" (2000) 29 Sw. U.L. Rev. 501 at 512.

[83] *Ibid.* at 506.

[84] *Ibid.*

[85] *Ibid.* at 505. See for example, the *Higher Education Act 1965* and the *Middle Income Student Assistance Act*, which extended student loan benefits to Americans regardless of household income. Prior to that only households with an income of less than $25,000 were eligible for loans under the *Higher Education Act*. *Ibid.* at n. 19.

[86] *Ibid.*

[87] New Zealand University Students' Association, "The Student Loan Scheme: Inequities and Emerging Issues" (Wellington, 2002).

[88] *Ibid.*

[89] N.Z., "Annual Report Student Loan Scheme"(October 2004), online: Annual Report Student Loan Scheme 2004 <http://www.studylink.govt.nz/pdf/2004/sls-annual-2004.pdf> (date accessed: 5 August 2005) at 34 [hereinafter Annual Report N.Z.].

In the U.K., the rationale for the Labour Party's proposal to increase tuition fees is that students, who derive substantial benefits from their education, should be required to contribute to the cost of their education.[90] The Labour Party is also recommending a variable fee rate that reflects the different economic benefits derived from various courses of study.[91] Furthermore, in support of the *Higher Education Act 2004*, which effectively removed student loans from bankruptcy, the House of Commons Standing Committee expressed concerns about protecting the public interest, specifically tax payer dollars that are used to fund the student loan program.[92]

In Australia, prior to 1989, students did not pay any tuition fees. John Dawkins, the Labour Minister of Education at the time, believed that this policy constituted an unfair subsidy to the rich by the poor.[93] Therefore, the Australian government enacted a system of deferred contributions, which required students who stood to benefit from the education to pay a portion of the cost.[94] Directly linked to this system was the creation of a partial exception to discharge for outstanding student contributions.

In the U.S. and Canada, similar rhetoric to the U.K. and Australia surrounding the private benefit of an education can be observed in the legislative debates. In addition, in these two countries, courts have often applied this rhetoric to deny relief in the context of judicial applications for relief. In the U.S., courts often consider whether the student benefited from their education when determining whether the debtor has satisfied the undue hardship test.[95] If a debtor has secured employment in her chosen field, it is less likely that the court will grant a discharge of the debtor's student loans.

In Canada, Hon. Bob Rae stated "While there is unquestionably a significant social benefit to higher education that should be recognized by a stronger commitment to public funding, there is also an important private benefit to the student and the graduate. It is only reasonable for students to pay part of the cost. Otherwise we would be asking taxpayers who don't go [to university or college] to subsidize those who do."[96] In the bankruptcy context, in some instances Canadian courts have translated this idea into a consideration of whether a debtor has derived an economic benefit from her education when determining if an application for relief from the exception to discharge should be granted. For example, in *Allen (Re)*, the applicant was denied a discharge because she had secured employment in her chosen field and thus had derived an economic benefit.[97] However, in *Swann (Re)*, the applicant was not successful at obtaining employment in her chosen field and therefore was granted a discharge.[98] The application of this principle has, however, been inconsistent and has often resulted in the court overlooking other life circumstances that impact on financial hardship. For example, in *Allen (Re)*, the court focused on the fact that that the applicant secured employment in her chosen field, and downplayed the fact that she suffered from a disability that prevented her from working full-time hours.[99]

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[90] U.K., Secretary of State for Education and Skills, "The Future of Higher Education" Secretary (By Command of Her Majesty, 2003) at 83.
[91] *Ibid.*
[92] *Supra* note 61, col. 578.
[93] A. Usher, *Much Ado About a Very Small Idea: Straight Talk on Income Contingent Loans* (Toronto: Educational Policy Institute, 2005) at 3.
[94] *Ibid.*
[95] Frattini, *supra* note 49 at 553, 566.
[96] Rae Review, *supra* note 27 at 23-24.
[97] *Allen (Re)*, 2000 CarswellOnt 4167 (Gen. Div.) at para. 6 [*Allen*].
[98] *Swann (Re)*, 2001 CarswellBC 1959 (Master) a para. 12.
[99] *Allen, supra* note 111 at para. 3.

F. Development of Securitization Markets

In both the U.S. and the U.K. the ability to access public capital markets to fund government-funded and guaranteed student loans through securitization has played a role in shaping an increasingly more restrictive exception to discharge for student loans. In the U.S., the existence of a securitization market likely played a role in extending the exception to private student loans and in the U.K. in introducing an exception for government-funded student loans. The American asset-backed securities market is the world's largest. Around the world the asset-backed securities market has been growing rapidly. Australia, New Zealand, Canada and the U.K. have all seen the introduction of asset-backed securities. However, currently only the U.S. and the U.K. appear to have developed markets for the securitization of student loans. Canada appears to be moving in the direction of developing a securitization market for student loans.

Securitization of student loans refers to the process where an entity pulls together student loans and then sells the rights to those receivables to investors in the form of securities.[100] The way that this process generally takes place is that a trust, referred to as a special purpose vehicle, is established to acquire the student loans from the originators of the student loans.[101] The trust issues debt securities or other interests to investors.[102] The debt securities or other interests issued by the trust are secured by the student loan notes acquired, related government guarantees and/or subsidies of the student loans. The cash that the trust receives from investors is used to pay the originator of the loans for the loans purchased.[103] The trust collects the cash generated by loans and distributes it to security holders over time. [104]

Securitization is beneficial to transferors because they can obtain funds at a more favourable interest rate that does not take into account the bankruptcy risk of the originator of the loans.[105] Rather than considering the credit rating of the originator of the loans, investors need only look to the cash flow from the loans themselves in evaluating the risk for the investment.[106] An equally important reason for originators of loans to engage in securitization is the favourable accounting treatment of such transactions.[107] Off-balance-sheet financing rules allow the transferor to increase liquidity and lower their debt-to-equity ratio as a result of the transaction.[108]

In the U.S., securitization of government guaranteed student loans was a $34 billion business in 2004.[109] Capital markets do not play a direct role in directly financed government student loans in the U.S.[110] A number of secondary market institutions are involved in purchasing and packaging for sale student loans from originators of government guaranteed student loans who choose not to keep the loans on their books.[111] The Student

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[100] J. L. Debruin, "Corporate Law: Recent Developments in and Legal Implications of Accounting for Securitizations"(1999) Ann. Surv. Am. L. 367 at 368.
[101] *Ibid.* at 369.
[102] *Ibid.*
[103] Dominion Bond Rating Service, online: US Student Loan ABS http://www.dbrs.com/web/sentry?COMP=2900&DocId=147792 (date accessed: 15 July 2005)[hereinafter DBRS].
[104] *Ibid.*
[105] Debruin, *supra* note 100 at 370.
[106] *Ibid.*
[107] *Ibid.* at 371.
[108] *Ibid.*
[109] DBRS, *supra* note 103.
[110] *Ibid.* at 2.
[111] *Ibid.*

Loan Marketing Association (Sallie Mae) is both the largest issuer of student loan asset backed securities and the largest private source of funding, delivery and servicing for student loans in the U.S.[112] Sallie Mae issues student loan asset backed securities backed by both government guaranteed and private student loans.[113] In 2004, Sallie Mae issued 12 deals totaling approximately $26 billion.[114] Nelnet Education Loan Funding Inc., which recently purchased Edulinx, the entity contracted to service federal and some provincial Government Student Loans in Canada, was next in line with four deals totaling over $5 billion.[115]

Initially when tuition fees were introduced in the U.K., the U.K. government offered students mortgage-style loans. In five years it had built up a debt portfolio of £3 billion. The U.K. government faced a similar challenge to the one that Canadian governments will face if there is a move from our current mortgage-style government-funded student loan system to an income-contingent model: What should be done with the existing loans? In 1998 and 1999, the U.K. government addressed this question by selling £2 billion of the U.K. government's student loan portfolio to the private sector. Each transaction involved the sale of approximately £1 billion in student loans owing to the government.[116] In both instances, the Student Loan Company Limited, a non-profit company, wholly owned by U.K. government, was contracted to administer the portfolios. One of the contracts to service the student loans sold to the private sector was renewed and the other was discontinued in 2004.[117] The 1998 transaction involved the securitization of student loans. In that transaction 300,000 student loans granted to those who entered post-secondary education before September 1, 1998 were transferred to Honours Student Loans, a special purpose vehicle set up by Honours Trustee Limited, a company formed jointly by Deutsche Bank and the Nationwide Building Society.[118] Honours Trustee Limited paid £1 billion to the U.K. government for these loans.[119] Given that the Student Loan Company Limited operates as a business and must account to the Department of Education and Skills for its performance, the accounting treatment resulting from the sale of the student loans, was likely a key motivating factor in the sale of the student loans.

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[112] Nomura, "Student Loan ABS 101" (26 January 2005), online: <http://www.securitization.net/pdf/Nomura/StudentLoan_26Jan05.pdf> (date accessed: 8 August 2005) at 8.
[113] *Ibid.* at 9.
[114] *Ibid.*
[115] *Ibid.*
[116] Student Loan Company, "Annual Report and Accounts 2003-2004, Delivery in the Future", online: Annual Report 2003-2004 <http://www.slc.co.uk/pdf/annualreport2004.pdf> (date accessed: 4 August 2005) at 3.
[117] *Ibid.*
[118] J. Cumbo, "Former Students Confused by Loan Switch" *Financial Times* (5 November 2004), online: FT.com <http://news.ft.com/cms/s/e4f2c072-2f4a-11d9-984e-00000e2511c8.html> (date accessed: 4 August 2005).
[119] *Ibid.*

2. Recommendations and Issues for Further Consideration

Following our review of the experiences of the bankruptcy system's treatment of government-funded or guaranteed student loans in Canada and four other countries, this section outlines our recommendations and suggestions on issues that merit further consideration. At the outset of this discussion it is important to note that Canada appears to be the only jurisdiction that is taking seriously proposals to make the exception to discharge in bankruptcy for student loans less restrictive. For this reason, the other countries under review are paying close attention to the Canadian proposals and developments. Accordingly, the implications of Canada's own choices are more far-reaching and significant than the national context.

The proposals that are currently on the table for reforming the treatment of student loans in bankruptcy in Canada merely attempt to tweak the waiting period attached to the exception and the ability to make an application for relief. Missing from these proposals is a consideration of the substantive features of the exception and an evaluation of the justifications for these features. In particular, current proposals do not address the soundness of the key justifications for the current exception: (a) student abuse of the bankruptcy process; and (b) the need to protect the public interest. Our findings suggest that these justifications are unfounded in the current context.

As a short-term measure, the reduction in the waiting period for the inapplicability of the exception and for obtaining relief from the exception proposed in Bill C-55 and the earlier government reports may resolve some of the tensions in the existing system. However, such a measure is not recommended. Rather, we put forward the following recommendations and issues for further consideration concerning the justifications for the exception, the reform process and the substance of reforms to the current exception.

A. Recommendations

i. Public Interest and Abuse Justifications for Exception are Unsubstantiated

A common theme in each of the jurisdictions considered, except New Zealand, is that the exception to discharge for government-funded or guaranteed student loans has been created or made more restrictive as a means to make figures documenting the increasing costs of a post-secondary education more palatable in the political process. Ironically, these figures are the direct result of the goal of democratizing post-secondary education. Policy making in the bankruptcy context has operated in opposition to this goal by discounting the social gains of an education and constructing education as a private benefit. The move to impose an increasingly restrictive discharge has followed from anecdotal stories documenting abuse offered by politicians and those representing certain private interests, even in the face of the availability of empirical data that challenges these stories. Saul Schwartz's study provides a good empirical platform in the Canadian context to challenge these stories.[120] Similarly, a review of all the reported applications for relief from the exception to discharge provides an alternative source of narratives that also challenges the dominant accounts of student abuse in the bankruptcy process.[121]

Directly linked to accounts of student abuse to justify the current exception are claims that because the government is the creditor at issue, it is in the public's interest for the government to be given special treatment for these debts. This public interest justification

[120] Schwartz, *supra* note 33.
[121] S. Ben-Ishai, "One Paradox of the Bankruptcy Fresh Start: Government Student Loans" (Forthcoming in (2005) Annual Insolvency Review).

has been rejected in numerous jurisdictions that have recently dispensed with the Crown's priority status in bankruptcy. While historically Crown priority for payment of debts was rooted in the theory that the "King could do no wrong" this principle is being abandoned globally.[122] In this context, claims centered on the protection of the public purse have been discounted on the grounds that if a debtor cannot obtain a fresh start (or in the corporate context – reorganize) the debtor will not be able to pay future debts to federal, provincial and local governments and will become a burden on them. There is a growing recognition that the quality of neighbourhoods, communities, the environment and retirement may be at stake in decisions as to whether to protect the public purse by abolishing or granting Crown priority.

Importantly, in the current context, as is discussed in the section on securitization above (Part 2(E)), any special treatment based on the public interest flowing from the government's identity as the creditor needs to be carefully evaluated. In the American context, the identity of the government as the creditor was used to justify an exception for student loans that has just been expanded to private lenders outright. On this basis, the National Bankruptcy Conference opposes the amendment to the nondischargeability provision. Specifically, the Conference has stated:

"The justification typically provided for excepting government insured loans from discharge does not apply to private loans made by for profit-institutions. For-profit institutions extend credit at market rates and on the same basis as every other lender."[123]

Originally, one justification for the current nondischargeability provision was to provide protection to non-profit and governmental entities, so that they could issue student loans and not harm the public purse.[124] When the amendment to expand the exception to "for profit" lenders was first proposed, the American Bankers Association and Consumer Bankers Association Task Forces on Bankruptcy asserted, "this proposed change simply suggests that if sufficient political pressure can be generated, a special interest group can obtain special treatment under the bankruptcy law."[125]

Similarly, in the U.K., the sale of directly funded government student loans to the private sector likely played a role in introducing the exception to discharge for these loans. The exception makes securities backed by government-funded student loans safer and more attractive to investors looking for low risk investments.

Given the involvement of Nelnet Education Loan Funding Inc. with the federal government student loan program and a number of provincial student loan programs in Canada, it appears that the development of a securitization market for these loans is imminent. Careful consideration needs to be given to the benefits of accessing public markets in this way. In particular, it will be necessary to evaluate whether such a market may be created without an exception to discharge for Government Student Loans. The U.K. model suggests that this is possible. The securitization of government-funded student loans in the U.K. took place prior to the introduction of an exception to discharge for government-funded student loans.

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[122] For a broader discussion of these reforms and the current status of the government in bankruptcy in Canada see S. Ben-Ishai, "Technically the King Can Do Wrong in Reorganizing Insolvent Corporations: Evidence form Canada" (2004) 13 Intl. Insolv. Rev. 1.

[123] Report of National Bankruptcy Conference on Titles I-III of the Bankruptcy Legislation, 2001 WL 770326, 96 (Nat'l Bankr. Confr. 2001) as cited in Hennessy, *supra* note 43.

[124] Hennessy, *ibid.*

[125] H.R. Rep. No. 95-595, at 150 (1977), reprinted in 1978 U.S.C.C.A.N. 5963, 6111 as cited in Hennessy, *ibid.* at 92.

At the same time, it is likely that once the securitization market was created, the private entities involved in this market played a significant role in shaping the policy that led to the enactment of the exception to discharge for government-funded student loans. In the U.S., which has the most developed securitization market, the private entities involved in this market played a significant role in shaping the exception to discharge that now includes private student loans.

In the Canadian context, it will be important to consider the role that players in the securitization market will have in shaping bankruptcy policy. An argument can be made that investment in student loans through the securitization market serves the public interest in increasing liquidity in the student loan market and increasing the total funding available to make student loans. However, there are a number of criticisms that can be levelled against the securitization of student loans. Importantly, we do not want to find ourselves in a situation where the driving force in making bankruptcy policy is the issue of how best to facilitate the securitization market at the expense of taking into account the implications for other stakeholders impacted by these policies. For example, in the U.S. claims such as this have been put forward to advance the interests of institutions involved in the securitization of government guaranteed student loans: "Is it sound policy to make a high priority federal program on which nearly 5.0 million students depend annually, an asset of only marginal appeal to lenders?"[126] Along the same line, student groups in Canada have argued that the 1998 amendment to the Canadian exception to discharge can be attributed to the banks' participation in the federal student loan program during this period and the government's desire to appease them.[127]

ii. Abolish the Exception

In light of our findings that the two key justifications for the exception to discharge for Government Student Loans are unsubstantiated, the exception to discharge should be abolished. The onus should be placed upon the government to oppose discharges where financial hardship would not result from continued payment of Government Student Loans and/or where bad faith can be demonstrated. In this way, the nine-month bankruptcy period could be extended where appropriate and a model more akin to the model in place in Australia and in New Zealand may be implemented. A key benefit of this approach is that bankruptcy registrars would be relieved of their role in making decisions surrounding student hardship that they currently must make in applications for relief from the exception.

The Canadian model attempts to accomplish what the Australia and New Zealand system accomplish through a longer bankruptcy process and the possibility for administrative hearings related to student hardship through the tax system. However, it fails for two reasons. First, with the 10-year waiting period, the exception introduces an inconsistency in the duration of the bankruptcy process for debtors with student loans and debtors without student loans. In Australia and New Zealand, because bankruptcy is a three-year period, the same concerns surrounding quick downloading of student loans through bankruptcy do not exist. The 10-year waiting period before students can apply for relief from the exception to discharge attempts to address this concern in the Canadian context. However, unlike the approach taken in New Zealand and Australia, this is inconsistent with the decision on the length of the bankruptcy process.

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[126] J. E. Gray, "Impact of Current Law on Profitability and Availability of FFEL Loans" (5 March 1998), online: Statement of Jonathan E. Gray <http://edworkforce.house.gov/hearings/105th/pet/loan3598/gray.htm> (date accessed: 8 August 2005).
[127] Membership Advisory, *supra* note 10 at 2.

A second problem with the exception is that it places the burden of making decisions about student hardship on bankruptcy registrars, without giving them any guidance on how to make these decisions. Unlike the situation in jurisdictions such as Australia, where such decisions are administrative decisions under the taxation scheme, bankruptcy registrars do not have experience to draw on from other similar situations or a large body of precedent for student loan decisions. No other exception to the bankruptcy discharge in Canada provides for an exception to its application on good faith and financial hardship grounds. For these reasons and because of the procedural and substantive obstacles to bringing an application for relief, the current role played by bankruptcy registrars is ineffective. Given both the American and the Canadian experience with applications for relief from the exception, where decisions are inconsistent and limited relief is provided, a better approach would be to place the onus on the government to oppose a former student's discharge in appropriate cases.

The approach we propose is essentially a return to the Canadian model that was in place between 1992 and 1997. In 1992, the government's preferred status in bankruptcy was removed, consistent with a broader trend in other jurisdictions to limit the priority status of the Crown.[128] When the preference was taken away from the government, the government argued that there was little to be gained from objecting to a bankrupt's discharge, since it had to share any recovery with the bankrupt's other unsecured creditors. The government claimed that it was experiencing significant losses as a result of its general unsecured position and the increasing number of students who were going bankrupt with unpaid Government Student Loans. As has already been discussed (Part 3(A)(i)), the empirical data demonstrates that while default on student loans and bankruptcies may increase with an increasing number and value of student loans, there is no empirical evidence of abuse of the bankruptcy process. Accordingly, the solution is not to deal with the costs associated with democratizing post-secondary education by closing the door to bankruptcy. Further, unlike the situation prior to 1997, mandatory surplus income payments are now required for high-income debtors during the 9-month bankruptcy period[129] and Bill C-55, would extend that period.[130] Accordingly, while the government would have to share any recovery with other unsecured creditors there is a possibility for greater recovery through income contributions during the bankruptcy period, which for high-income debtors looks similar to lengthier bankruptcy periods in Australia and New Zealand. Further, while this approach may result in increased monitoring and litigation costs in relation to student loans, these costs would presumably outweigh the costs of distress suffered by existing students who cannot discharge their Government Student Loans.

As there were few cases between 1992 and 1997 where the government opposed a bankrupt's discharge on account of unpaid Government Students Loans, it is difficult to evaluate the role that bankruptcy registrar's played in that period in relation to student loans. In order to avoid an unpredictable and inconsistent system, if the exception is abolished it would be important for the government to issue a bulletin as to its policy and criteria for opposing discharges on the ground of outstanding Government Student Loans.

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[128] For a broader discussion of this reform and the current status of the government in bankruptcy see Ben-Ishai, *supra* note 122.

[129] See *An Act to Amend the Bankruptcy and Insolvency Act, the Companies Creditors' Arrangement Act and the Income Tax Act:* S.C. 1997, c.12 and Office of the Superintendent of Bankruptcy Canada, *Directive No. 11: Surplus Income* (Issued 30 October 2000 and revised 26 January 2005), online: Office of the Superintendent of Bankruptcy <http://strategis.ic.gc.ca/epic/internet/inbsf- osb.nsf/en/br01055e.html> (date accessed: 14 June 2005).

[130] Bill C-55, *supra* note 40, s. 58.

B. Issues for Further Consideration

i. The Provability of Government Student Loans

An issue that has not arisen in the Canadian context concerns the provability of Government Student Loans. It is unclear from a review of both primary and secondary sources why this issue has not arisen in the Canadian context. One possibility is that where Government Student Loans are in a bankrupt's portfolio of debts, the distribution from the bankrupt's estate to unsecured creditors is so low that the issue does not have much economic significance. This possibility needs to be further investigated in the current context. The rationale behind the approach in Australia and in the U.K. suggests that if the exception for Government Student Loans is retained in Canada, they should not be provable in bankruptcy. That is, since the government retains the prospect of repayment because student loans are not extinguished in bankruptcy, it should not be able to claim a share of the sale of the bankrupt's assets, thereby reducing the amount available to other creditors who have no future hope of repayment.

ii. The Treatment of Government Student Loans in a No-Asset Procedure

It may be argued that the summary administration process, currently in place under the *BIA*, is Canada's version of a no-asset bankruptcy procedure. However, this process still includes a number of features that distinguish it from the proposed no-asset processes in New Zealand and the U.K. One of the most significant of these features is the cost of going bankrupt in Canada. To the extent that our second recommendation is adopted and the exception to discharge for Government Student Loans is abolished, if a no-asset procedure, similar to the U.K. or New Zealand model, is implemented in Canada, further consideration will need to be given as to whether an exception to discharge for Government Student Loans should be in place for this process.

4. New Zealand

A. Overview of the Government Student Loan Program

New Zealand's government-funded Student Loan Scheme was established in 1992. The Student Loan Scheme is governed by the *Student Loans Scheme Act 1992*.[131] Under this program the government of New Zealand directly finances the loans.[132] In order to be eligible to apply for a loan, a student must be a New Zealand citizen, permanent resident or refugee and enrolled in an approved tertiary course. Loans under the Student Loan Scheme are not awarded on the basis of financial need.[133] Currently, undischarged bankrupts are not eligible to obtain a loan under the Student Loan Scheme.[134]

Debt repayment of loans under the Student Loan Scheme is income-contingent. Repayment is not compulsory until the student's income surpasses the repayment threshold (currently $16,588 a year before tax).[135] The amount of repayment required in any income year is determined by the amount of income earned over the threshold. The minimum rate of repayment in 2004 was 10 cents per dollar earned over the repayment threshold.[136] Voluntary repayments can be made at any time. Once the student has reached the income threshold, Inland Revenue calculates the minimum weekly payment that must be made towards the loan. Inland Revenue recovers the weekly payments in the same way it collects taxes (for employees through employer deductions and for business and investment income through instalment payments).

The amount borrowed under the Student Loan Scheme is subject to interest from the first date the loan is used. The current interest rate is seven per cent per year.[137] On the basis of their income, students may qualify for an interest write-off pursuant to the *Student Loans Scheme Act 1992*.[138] For full-time, full year students interest write-offs are calculated in April. For part time or part year students, interest write-offs are calculated when Inland Revenue issues the student a personal tax summary in July or when the student files their tax return. There are three forms of interest write-off: Full Interest Write-Off[139], Base Interest Write-Off[140] and a Base Interest Reduction.[141]

In 2006, to qualify for a Full Interest Write-Off the borrower must be a full-time, full-year student or a part-time or part-year student earning less than $26,799 a year before tax (between 1 April 2005 and 31 March 2006), and a New Zealand tax resident.[142] Students who do not qualify for a Full Interest Write-off may still be able to qualify for a Base

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[131] *Student Loans Scheme Act 1992* (N.Z.), 1992/141, online: Statutes of New Zealand < http://www.legislation.govt.nz/browse_vw.asp?content-set=pal_statutes> (date accessed: 4 August 2005).
[132] *Ibid.*, s. 2.
[133] See Usher, *supra* note 93.
[134] Study Link, "Help for Students, How We Can Help With Your Costs While You're Studying", online: Study Link <http://www.studylink.govt.nz/pdf/help-for-students.pdf> (date accessed: 4 August 2005) at 19.
[135] *Student Loan Scheme (Repayment Threshold) Regulations 2004* (N.Z.), 2004/462, s. 3.
[136] Annual Report N.Z., *supra* note 89 at 11.
[137] *Student Loan Scheme (Interest Rates) Regulations 2005* (N.Z.), 2005/22, ss. 3-4.
[138] *Supra* note 131, ss. 38A-41.
[139] *Ibid.*, ss. 38A-38D.
[140] *Ibid.*, s. 39.
[141] *Ibid.*, s. 40.
[142] *Ibid.*, s. 38A-38D. See also, StudyLink, online: About Interest Write-Off < http://www.studylink.govt.nz/financial-assistance/student-loan/about-interest/about-interest-write-off.html> (date accessed: 4 August 2005) [hereinafter Interest Write Off].

Interest Write-Off provided the student's income is $16,588 a year or less before tax (between 1 April 2005 and 31 March 2006) and they are a New Zealand tax resident.[143] Students who do not qualify for either a Full-Interest Write-Off or Base Interest Write-Off may still qualify for a Base Interest Reduction provided that the student's income is more than $16,588 a year before tax (between 1 April 2005 and 31 March 2006) and the base interest charged is more than 50 per cent of the student's repayment obligation for the year.[144] The amount of interest written off is equal to the student's base interest charged minus 50 per cent of the student's annual repayment obligation.

A student may also seek relief from their repayment obligation pursuant to section 54 of the *Student Loans Scheme Act 1992*.[145] Upon receipt of a written application, the Commissioner of Inland Revenue may refrain from collecting payment of any repayment obligation, for a period of time, where the Commissioner is satisfied that payment has caused or would cause serious hardship to the borrower or considers that there are other special reasons that make it fair and reasonable. The amount of payment that the Commissioner refrains from collecting is subject to interest at the total interest rate on the daily amount outstanding. Inland Revenue indicates that there are no available statistics or access to case decisions. Each case is handled on a case-by-case basis.[146]

B. Treatment of Student Loans in Bankruptcy

Bankruptcy in New Zealand is governed by the *Insolvency Act 1967*.[147] A debtor may file a petition for bankruptcy at the High Court. There is a $40.00 fee for filing this petition.[148] A creditor may also file a petition with the High Court to initiate bankruptcy proceedings against a debtor. After a debtor is adjudicated bankrupt an Official Assignee, who is a civil servant, is appointed.[149] An Official Assignee acts as an officer of the court and is responsible for administering the debtor's affairs.[150] The Official Assignee will sell all appropriate assets and ensure that the proceeds are fairly and equitably distributed amongst the debtor's creditors.[151] Having regard to the financial circumstances and conduct of the bankrupt, the Official Assignee may require that the bankrupt make regular contributions to the bankruptcy estate for the benefit of her creditors during the bankruptcy period.[152] In most cases, discharge will occur automatically on the third anniversary of the date of the bankruptcy order.[153] Debtors can seek an early discharge at any time during bankruptcy.[154] Discharge may be delayed if an objection to automatic discharge is filed with the High Court.[155] Student loans under the Student Loan Scheme are provable and dischargeable in bankruptcy.[156]

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[143] *Ibid.*, s. 39. See also Interest Write Off, *ibid.*
[144] *Ibid.*, s. 40. See also Interest Write Off, *ibid.*
[145] *Ibid.*, s. 54.
[146] Interview of Jay (last name undisclosed), Inland Revenue Call Center agent (13 June 2005) Inland Revenue.
[147] *Insolvency Act 1967* (N.Z.), 1967/54, online: Statutes of New Zealand < http://www.legislation.govt.nz/browse_vw.asp?content-set=pal_statutes> (date accessed: 4 August 2005 2005) [hereinafter *Insolvency Act 1967*].
[148] *Insolvency Regulations 1970* (N.Z.), 1970/260, s. 5(1).
[149] *Insolvency Act 1967, supra* note 147, s. 15.
[150] *Ibid.*
[151] *Ibid.*, s. 72.
[152] *Ibid.*, s. 45.
[153] *Ibid.*, s. 107 (1).
[154] *Ibid.*, s. 108.
[155] *Ibid.*, s. 107 (3).
[156] *Ibid.*, s.87 and 114.

C. Treatment of Student Loans in Alternative to Bankruptcy Processes

In New Zealand there are currently two formal alternatives to bankruptcy: proposals and summary instalment orders. In addition, a third alternative has been recently proposed for no-asset bankruptcies. Under all three alternatives, loans under the Student Loan Scheme are not dischargeable.

A person who is not bankrupt, but who is for any reason unable to meet her debts that would be provable in bankruptcy as they become due, can make a proposal to her creditors with regard to the payment or satisfaction of her debts. The provisions relating to proposals are outlined in Part 15 of the *Insolvency Act 1967*.[157] A proposal may include any other conditions for the benefit of the creditors and may be accompanied by a security or guarantee.[158] Debts that are provable in bankruptcy are also provable in proposals.[159] Therefore, student loans under the Student Loan Scheme may be included in a proposal. However, they cannot be discharged.[160]

In addition to a proposal, a debtor or creditor, with consent of the debtor, can apply to the District Court for a summary instalment order, when the total unsecured debts that would be provable in bankruptcy is not more than $12,000.[161] Currently, there is a recommendation by Cabinet of Economic Development that the debt cap for summary instalment orders be raised to $40,000.[162] Provisions relating to summary instalment orders are outlined in Part 16 of the *Insolvency Act 1967*.[163] The District Court, upon hearing any creditors or debtors who seek to be heard, may make an order providing for the payment of the debts "by instalments or otherwise and either in full or to such extent as that Court considers practicable in the circumstances of the case."[164] In most cases, the District Court will appoint a supervisor who is responsible for ensuring that the debtor complies with the terms of the order.[165] No summary instalment order can be made under which the payment of instalments if kept up without default would extend over a period of more than three years from the date of the order.[166] Those debts, which would be provable in bankruptcy, such as student loans under the Student Loan Scheme, can be included in a summary instalment order.[167] However, under the Student Loan Scheme, student loans cannot be discharged under a summary instalment order unless they are paid in full.[168]

The Cabinet of Economic Development has proposed a "no asset procedure" as a third alternative to bankruptcy for those debtors with no assets who cannot repay their debts while still maintaining a minimum standard of living. This alternative would only apply to debts under $40,000.[169] The Insolvency Law Reform Bill, which is expected to be enacted in 2005 or 2006, will introduce the "no asset procedure."[170] The rationale for the "no-asset procedure" is to facilitate swifter recovery from financial failure, provide incentives for

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[157] *Insolvency Act 1967, supra* note 137, ss. 139-145.
[158] *Ibid.*, s. 140(3).
[159] *Ibid.*, s. 139.
[160] Interview of J. Ruane, Investigating Accountant (7 June 2005) (Ministry of Economic Development).
[161] *Insolvency Act 1967, supra* note 147, s. 146.
[162] N.Z., "Bankruptcy Administration: No Asset Procedure and Insolvency Act Changes", December 2003, (Lianne Dalziel, Chair) at para. 10.
[163] *Insolvency Act 1967, supra* note 147, s. 146 – 152.
[164] *Ibid.*, s. 146 (4).
[165] *Ibid.*, s. 146 (5).
[166] *Ibid.*, s. 146 (12).
[167] *Ibid.*, s. 146.
[168] *Supra* note 160.
[169] *Supra* note 162 at para. 16.
[170] Annual Report, *supra* note 89 at 12.

individuals to become productive members of society and to reduce the social stigma associated with bankruptcy.[171] The Committee proposing this procedure is concerned that since this procedure aims at reducing the punitive aspects of bankruptcy, it may be susceptible to abuse. A number of safeguards have been built into the procedure in order to reduce the incentives for abusing the system. In particular, the Committee has recommended that student loans under the Student Loan Scheme, which are dischargeable in bankruptcy, should not be dischargeable through the "no asset procedure."[172] The purpose of this provision is to reduce any incentive for students to enter into a "no asset procedure" simply to avoid paying back their loans.[173] However, debtors, under the "no asset procedure," would be eligible to receive student loans under the Student Loan Scheme unlike undischarged bankrupts.[174]

D. Consumer Debts Not Extinguished by Bankruptcy

Section 87 of the *Insolvency Act 1967*[175] identifies a small number of debts, which are not provable and thus not extinguished on discharge from bankruptcy. Debts that are not provable include:

> Any fine or penalty imposed or order for payment of money made pursuant to any conviction under section 42 of the Criminal Justice Act 1954 or section 19 of the Criminal Justice Act 1985 or section 106 of the Sentencing Act 2002 shall not be provable in bankruptcy, but the provisions of any other Act as to recovery of any such sum of money shall not be otherwise affected.

Since the current alternative to bankruptcy processes, proposals and summary instalment orders and the proposed "no-asset procedure," only pertain to provable debts, these processes cannot be used to extinguish the above debts.

Section 114 of the *Insolvency Act 1967* also includes a number of debts which are provable but where the bankrupt is not released from liability upon discharge. These include:

a) Any debt or liability incurred by means of any fraud or fraudulent breach of trust to which he was a party;
b) Any debt or liability whereof he has obtained forbearance by any fraud to which he was a party;
c) Any judgment debt or any amount payable under any order for which he is liable under section 45 or section 110 of this Act;
d) Any amount payable under a maintenance order under the Family Proceedings Act 1980;
e) Any amount payable under the Child Support Act 1991

These debts may be included in a proposal or summary instalment order, but the debt would have to be paid in full in order to be discharged.[176] In a "no-asset procedure" these debts would not be discharged.

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[171] *Supra* note 162 at para. 3.
[172] *Ibid.* at para. 50.5.
[173] Annual Report, *supra* note 89 at 12 - 13.
[174] *Supra* note 162 at para. 50.6.
[175] *Insolvency Act 1967, supra* note 147, s. 87.
[176] *Supra* note 153.

5. Australia

A. Overview of the Government Student Loan Program

On January 1, 2005, the Australian government introduced the Higher Education Loan Programme (HELP), which significantly altered the existing student loan program under the Higher Education Contribution Scheme (HECS). The changes to the HECS were enacted under the *Higher Education Support Act 2003*.[177] The HECS program is a system of deferred contributions that dates back to 1989. Prior to the HECS program, Australian students paid no tuition fees.

HELP loans are provided by the government and remain with the Australian Tax Office against a student's tax file number. HELP loans are not means tested.[178] Under the HELP there are three types of loans available to students: HECS-HELP,[179] FEE-HELP[180] and OS-HELP. [181]

OS-HELP is available to assist eligible undergraduate Commonwealth supported students undertake some of their course of study overseas.[182] This report will not focus on OS-HELP loans.

HECS-HELP loans are available to eligible Commonwealth supported students to cover all or part of their student contribution. The Australian government allocates Commonwealth supported places to eligible higher education providers each year. Acceptance into a Commonwealth supported place is based on merit as determined by the higher education provider. Students who receive a Commonwealth supported place are only required to make a contribution towards the cost of their education (known as a student contribution) while the Australian Government contributes the majority of the cost. The amount that the Australian Government contributes depends on the course of study: in 2005, the government contributed from $1472 for law to $15996 for agriculture.[183] No loan fee applies to HECS-HELP loans. HECS-HELP loans are paid directly to the student's education provider. HECS-HELP loan repayment discounts of 20 per cent are also available for students who pay all,[184] or at least $500, of their student contribution upfront.[185]

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[177] *Higher Education Support Act 2003* (Cth.).
[178] *Ibid.* at 6.
[179] *Ibid.*, Pt. 3-2. See also Australian Government, Department of Education, Science and Training, Going to Uni, online: Loans Overview <http://www.goingtouni.gov.au/Main/FeesLoansAndScholarships/Undergraduate/Loans/Default.htm> (date accessed: 4 August 2005).
[180] *Ibid.*, Pt. 3-3.
[181] *Ibid.*, Pt. 3-4.
[182] *Ibid.*, Pt. 3-4, s. 115 (1). See also, Australian Government, Department of Education, Science and Training, Going to Uni, online: OS-HELP. <http://www.goingtouni.gov.au/Main/Quickfind/StudyOverseas/OSHELP.htm> (date accessed: 4 August 2005).
[183] Australian Government, Department of Education, Science and Training, Going to Uni, online: How Much Does the Australian Government Contribute? <http://www.goingtouni.gov.au/Main/Resources/ICSS/PayingForAUnitOfStudy/HowMuchDoesTheAustralianGovernmentContribute.htm> (date accessed: 4 August 2005).
[184] *Supra* note 177, s. 96-10.
[185] *Ibid.*, ss. 96-5.

FEE-HELP is a loan given to eligible fee-paying students to help pay for all or part of their tuition fees up to a maximum of $50,000 over the student's lifetime.[186] Fee paying (non-Commonwealth supported) students must pay full tuition fees. The Australian government does not contribute towards the cost of a student's education in such cases. A loan fee of 20 per cent applies to FEE-HELP loans for undergraduate courses of study.[187] This fee is not included in the $50,000 FEE-HELP limit. The Commonwealth pays the amount of the loan directly to the student's education provider.

There is no real interest charged on HELP debts, but accumulated HELP debt is indexed annually on June 1st to reflect changes in the Consumer Price Index.[188] Debt repayment under all HELP loans is income-contingent. The repayment threshold is indexed in line with the Consumer Price Index. For 2005-2006, the repayment threshold will be $36, 184.[189] For 2004 – 2005 the rates ranged from four per cent to eight per cent of one's total HELP repayment income.[190] The Australian Tax Office recovers the payments in the same way that it collects taxes (employer deductions and instalments for business and investment income). Students receive a 10 per cent bonus for all voluntary repayments of $500 or more.[191] Voluntary repayments are made directly to the Australian Tax Office.

A debtor can seek to have her compulsory repayments on their HELP debts deferred or amended. Under section 154-45 of the *Higher Education Support Act 2003* a former student who believes that compulsory repayments deducted from her salary in a financial year would subsequently cause her considerable hardship, may apply to the Commissioner of Taxation for a deferment of her taxable income assessment.[192] The application must specify the income year for which the deferral is being sought; and the reasons for seeking the deferral. The income year specified in the application must be within two years of the year in which the application is made.[193] The Commissioner may defer an assessment if the Commissioner is of the opinion that:

(a) if the assessment were made, payment of the assessed amount would cause serious hardship to the person; or
(b) there are other special reasons that make it fair and reasonable to defer making the assessment.[194]

Citing privacy legislation, the Australian Taxation Office was unable to disclose specific cases where the Commissioner had granted deferment of compulsory repayments.[195] However, the following are broad interpretations of serious hardship and other special

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[186] *Ibid.*, s. 104-20.
[187] *Ibid.*, s. 137-10(2)(a).
[188] *Ibid.*, s. 140-1(2)(a). Australian Government Department of Education, Science and Training, Going to Uni, online: Interest and Indexation < http://www.goingtouni.gov.au/Main/FeesLoansAndScholarships/LoanRepayments/Interest-Indexation.htm> (date accessed: 6 June 2005).
[189] *Ibid.*, s. 154-10(a).
[190] *Ibid.*, s. 154-20. See also Australian Government Department of Education, Science and Training, Going to Uni, online: Compulsory and Voluntary < http://www.goingtouni.gov.au/Main/FeesLoansAndScholarships/LoanRepayments/Compulsory-Voluntary.htm> (date accessed: 6 June 2005).
[191] *Ibid.*, s. 151-5. See also Australian Government Department of Education, Science and Training, Going to Uni, online: Compulsory and Voluntary < http://www.goingtouni.gov.au/Main/FeesLoansAndScholarships/LoanRepayments/Compulsory-Voluntary.htm> (date accessed: 6 June 2005).
[192] *Ibid.*, s. 154-45.
[193] *Ibid.*, s. 154-45 (2), (3).
[194] *Ibid.*, s. 154-45(4)
[195] Interview of A. Sutherland, Australian Taxation Officer (10 June 2005) Australian Taxation Office.

reasons. Serious hardship exists when a person is unable to provide food, accommodation, clothing, medical treatment, education or other necessities for herself, or her family or other people for whom she is responsible.[196] Other special reasons cover any unusual or unique situations that do not qualify as serious hardship but make it fair and reasonable for a person not to make their compulsory repayment.

In 2003-2004 there were 353,000 compulsory HELP debt repayments raised totalling $640.43 million. There were also 1393 HELP debt repayments deferred, totalling $2.38 million.[197]

B. Treatment of Student Loans in Bankruptcy

Bankruptcy in Australia is governed by the *Bankruptcy Act 1966*.[198] The Australian bankruptcy process is similar to the process in New Zealand. A debtor may become bankrupt voluntarily by filing with the Official Receiver a debtor petition and a statement of affairs.[199] A creditor, who is owed at least $2000, may file a petition with the Federal Court or the Federal Magistrates Court for the bankruptcy of the debtor.[200] In this case a hearing will be held to determine whether the debtor should be made bankrupt. It costs nothing to file a consumer bankruptcy petition and the Official Trustee (employees of an executive agency of the Attorney General's department) handles the majority of bankruptcies.[201] In a similar fashion to the Canadian system, bankrupts who earn relatively high incomes are required to make contributions to their bankrupt estate from their income.[202] The level of contributions depends on the net income after allowing for tax and any child support being paid and the bankrupt's number of dependants. During the bankruptcy period, a bankrupt's ability to obtain credit is reduced[203], she is not able to manage a corporation[204] and she requires written approval to travel oversees.[205] There is an automatic discharge from bankruptcy three years,[206] after the statement of affairs is filed with the Official Receiver, subject to an objection to discharge filed by the trustee, which can extend the bankruptcy to either five or eight years.[207]

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[196] *Ibid.*
[197] *Ibid.*
[198] *Bankruptcy Act 1966* (Cth.) [hereinafter *Bankruptcy Act 1966*].
[199] *Ibid.*, s, 55 (1). See also J. Ziegel, *Comparative Consumer Insolvency Regimes – A Canadian Perspective* (Portland: Hart, 2003) at 97 [hereinafter Ziegel].
[200] *Ibid.*, s. 44 (1) (a). See also R. Mason and J. Duns, "Developments in Consumer Bankruptcy in Australia" in J. Niemi-Kiesilainen, I. Ramsay & W. Whitford, eds., *Consumer Bankruptcy in Global Perspective* (Portland: Hart, 2003) at 233.
[201] See ITSA's prescribed information on Bankruptcy and Alternatives under reg. 4.11 dated November 2001, online: ITSA <http://www.itsa.gov.au/aghome/commafff/itsa/frame_bankruptcy.html> as cited in R. Mason & J. Duns, "Developments in Consumer Bankruptcy in Australia" in J. Niemi-Kiesilainen, I. Ramsay & W. Whitford, eds., *ibid.* at 232.
[202] *Bankruptcy Act 1966, supra* note 198, Pt. VI. See also, Ziegel, *supra* note 202 at 100.
[203] *Ibid.*, s. 269. See also, Australian Government, Insolvency and Trustee Services Australia, online: Obligations of Bankrupt <http://www.itsa.gov.au/dir228/itsaweb.nsf/docindex/bankruptcy->bankruptcy+-+long+version?opendocument#Obligations> (date accessed: 8 August 2005).
[204] See Australian Government, Insolvency and Trustee Services Australia, online: Obligations of Bankrupt <http://www.itsa.gov.au/dir228/itsaweb.nsf/docindex/bankruptcy->bankruptcy+-+long+version?opendocument#Obligations> (date accessed: 8 August 2005).
[205] *Bankruptcy Act 1966, supra* note 198, s. 272 (1)(c). See also, Australian Government, Insolvency and Trustee Services Australia, online: Obligations of Bankrupt <http://www.itsa.gov.au/dir228/itsaweb.nsf/docindex/bankruptcy->bankruptcy+-+long+version?opendocument#Obligations> (date accessed: 8 August 2005).
[206] *Ibid.*, s. 149. See also Ziegel, *supra* note 199 at 102.
[207] *Ibid.*, s. 149A. See also Ziegel, *ibid.*

HECS-HELP, FEE-HELP and OS-HELP semester and accumulated debts, are not provable and thus not extinguished in bankruptcy.[208] This provision came into effect on January 1, 2004 despite the fact that no HELP debts could be incurred until January 1, 2005.[209] Prior to this amendment, semester and accumulated debts were provable but not extinguished in bankruptcy.[210] Semester debts are incurred when the Commonwealth makes a loan to cover a student's contribution in respect of a course of study in a semester.[211] Accumulated HECS debts are calculated yearly on June 1 and are adjusted to reflect indexation, any new semester debts incurred and any repayments made during the year.[212] Assessment debts refer to the amount that is due to be paid in respect of an accumulated HEC debt and is included in a notice of an assessment issued by the Australian Taxation Office.[213] HELP assessment debts are provable and are discharged in bankruptcy.[214]

C. Treatment of Student Loans in Alternative to Bankruptcy Processes

In Australia, there are two alternatives to bankruptcy: debt agreements and personal insolvency agreements. Only those debts, that are provable in bankruptcy, can be included in a debt agreement or personal insolvency agreement.[215] Since assessment HELP debts are provable they can be included in a debt agreement or personal insolvency agreement. Accumulated and semester HELP debts are not provable and cannot be included in these alternatives to bankruptcy.

A debt agreement allows a debtor and creditor to enter into a legally binding agreement as an alternative to bankruptcy. This process provides additional protections and consequences that may be absent in private arrangements. The provisions relating to debt agreements are outlined in Part IX of the *Bankruptcy Act 1966*.[216]

A personal insolvency agreement allows debtors to make a proposal to their creditors, which they then consider and vote upon at a formal meeting. If the proposal is accepted it is binding on the debtor and all creditors in respect of their unsecured provable debts. Provisions relating to personal insolvency agreements are outlined in Part X of the *Bankruptcy Act 1966*.[217]

D. Consumer Debts Not Extinguished by Bankruptcy

In addition to HELP student loans there are a number of other consumer debts, which are not provable and thus not extinguished by bankruptcy or alternatives to bankruptcy.[218]

Debts which are not provable include the following: demands in the nature of unliquidated damages arising otherwise than be reason of a contract, promise or breach of trust; penalties or fines imposed by a court in respect of an offence against a law, whether a law of the Commonwealth or not; an amount payable under an order made under section 1317G of the

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[208] *Bankruptcy Act 1966, supra* note 198, s. 82 (3AB).
[209] Insolvency and Trustee Services Australia, online: Examples – Provable Debts < http://www.itsa.gov.au/dir228/itsaweb.nsf/docindex/Creditors->Provable%20Debts->Examples%20-%20Provable%20Debts?OpenDocument#HELD> (date accessed: 4 August 2005).
[210] *Ibid.* See also *Higher Education Funding Act 1988* (Cth.), s. 106YA [hereinafter HEFA].
[211] HEFA, *ibid.*, s. 106J.
[212] *Ibid.*, s. 106N.
[213] *Ibid.*, s. 34.
[214] *Supra* note 209.
[215] *Bankruptcy Act 1966, supra* note 198, s. 185, 187.
[216] *Ibid.*, Pt IX.
[217] *Ibid.*, Pt. X.
[218] *Bankruptcy Act 1966, supra* note 198, s. 82.

Corporations Act 2001; an amount payable under an order made under a proceeds of crime law; a debt is not provable in bankruptcy in so far as the debt consists of interest accruing, in respect of a period commencing on or after the date of bankruptcy, on debt that is provable in bankruptcy; any debt or liability which the value cannot be fairly estimated; debts incurred after a person becomes bankrupt; council rates as they attach to the property for which the rates are due (i.e. secured debts); creditor's legal costs unless the are allowed by judgment prior to bankruptcy or were allowed as part of the contractual obligation incurred prior to bankruptcy; costs of abortive writs or collection agents' expenses unless the debtor is liable under the terms of the contract or there are specific provisions in statute allowing such; and a debt not enforceable at law owing to a prohibition contained in a statute (e.g. debt due to minor, an unlicensed bookmaker or a debt related to illegal purchases).[219]

There are also a number of debts listed in Section 153 of the *Bankruptcy Act 1966*, which are provable, but where the bankrupt is not released from liability upon discharge from bankruptcy. These debts can be included in debt agreements and personal insolvency agreements, but the debtor cannot be released. Alternative to bankruptcy processes cannot be used to override provisions pertaining to bankruptcy.[220]

Section 153 of the *Bankruptcy Act 1966* states:

(1) Subject to this section, where a bankrupt is discharged from a bankruptcy, the discharge operates to release him or her from all debts (including secured debts) provable in the bankruptcy, whether or not, in the case of a secured debt, the secured creditor has surrendered his or her security for the benefit of creditors generally.

Note: The operation of this section in relation to accumulated HEC debts and semester debts under the *Higher Education Funding Act 1988* is affected by section 106YA of that Act.

(2) The discharge of a bankrupt from a bankruptcy does not:

(a) release the bankrupt from:

(i) a debt on a recognizance; or

(ii) a debt with which the bankrupt is chargeable at the suit of the sheriff or other public officer on a bail bond entered into for the appearance of a person prosecuted for an offence against a law of the Commonwealth or of a State or Territory of the Commonwealth; or

(aa) release the bankrupt from liability to pay an amount to the trustee under subsection 139ZG(1); or

(b) release the bankrupt from a debt incurred by means of fraud or a fraudulent breach of trust to which he or she was a party or a debt of which he or she has obtained forbearance by fraud; or

(c) subject to any order of the Court made under subsection (2A), release the bankrupt from any liability under a maintenance agreement or maintenance order;

Note: A discharged bankrupt remains liable under any pecuniary penalty order because such liabilities are not provable in bankruptcy, see subsection 82(3A).

(2A) The Court may order that the discharge of a bankrupt from bankruptcy shall operate to release the bankrupt, to such extent and subject to such conditions as the Court thinks fit, from liability to pay arrears due under a maintenance agreement or maintenance order.

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[219] *Ibid.*

[220] *Supra* note 70.

(3) The discharge of a bankrupt from a bankruptcy does not affect the right of a secured creditor, or any person claiming through or under him or her, to realize or otherwise deal with his or her security:

(a) if the secured creditor has not proved in the bankruptcy for any part of the secured debt—for the purpose of obtaining payment of the secured debt; or

(b) if the secured creditor has proved in the bankruptcy for part of the secured debt—for the purpose of obtaining payment of the part of the secured debt for which he or she has not proved in the bankruptcy;

and, for the purposes of enabling the secured creditor or a person claiming through or under him or her so to realize or deal with his or her security, but not otherwise, the secured debt, or the part of the secured debt, as the case may be, shall be deemed not to have been released by the discharge of the bankrupt.

(4) The discharge of a bankrupt from a bankruptcy does not release from any liability a person who, at the date on which the bankrupt became a bankrupt:

(a) was a partner or a co-trustee with the bankrupt or was jointly bound or had made a joint contract with the bankrupt; or

(b) was surety or in the nature of a surety for the bankrupt.

(5) Where a bankrupt has been discharged from a bankruptcy, all proceedings taken in or in respect of the bankruptcy shall be deemed to have been validly taken.[221]

[221] *Bankruptcy Act 1966, supra* note 198, s. 153.

6. The United Kingdom

A. Overview of the Government Student Loan Program

The current U.K. government-funded student loan program was established in 1998. The student loan program is governed by the *Teaching and Higher Education Act 1998*[222] and for England and Wales the *Education (Student Loans) (Repayment) Regulations 2000*[223] as amended and the *Education (Student Support) (No.2) Regulations 2002*.[224] All students can receive up to 75 per cent of the student loan, while 25 per cent is means-tested.[225] The Student Loan Company Limited, a non-departmental publicly funded company, which is wholly owned by the Secretary of State for Education and Skills and the Secretary of State for Scotland, is responsible for paying out and administering the government-funded student loan program.[226]

The government subsidizes the "actual" cost of interest on government-funded student loans. However, to make sure that all borrowers pay back the same amount that they borrowed, students are responsible for paying a rate of interest equal to inflation. This interest is charged from the moment the loan is paid to the borrower, until the borrower repays the loan in full. Interest is charged on a daily basis and is compounded.[227]

Prior to 1998, the U.K. had a fixed-term, mortgage-style government-funded student loan program.[228] However, debt repayment is now income-contingent. Students do not have to start making repayments until April of the year after they finish or leave a post-secondary education program. After that time, payments are only required if the student's income surpasses the repayment threshold (currently £15,000 or £1250/month or £288 a week).[229] Students may also make voluntary partial or total loan repayments at any time.[230]

For borrowers who are employees, repayments are calculated as a percentage of income above £1250 a month or £288 a week, not as a percentage of total income. The current percentage is nine per cent.[231] If a former student is an employee, the employer deducts repayments from her pay cheque, in the same way as tax and National Insurance contributions are deducted.[232] If a borrower is self-employed she must send Inland Revenue a tax return each year under the self-assessment system. For self-employed

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[222] *Teaching and Higher Education Act 1998* (U.K.), 1998, c. 30 [hereinafter *THEA*].
[223] *Education (Student Loans) (Repayment) Regulations 2000,* S.I. 2000/944.[hereinafter *Repayment Regulations*].
[224] *Education (Student Support) (No.2) Regulations 2002* S.I. 2002/3200.
[225] Department for Education and Skills, online: Student Loans and the Question of Debt < http://www.dfes.gov.uk/hegateway/uploads/Debt%20-%20FINAL.pdf http://www.dfes.gov.uk/hegateway/uploads/Debt%20-%20FINAL.pdf > (date accessed: 4 August 2005) at 5.
[226] *Supra* note 116 at 2.
[227] THEA, *supra* note 222, s. 22 (3)(a), 4 (a)(i). See also, Department of Education and Skills, "Student Loans: A Guide to Terms and Conditions", online: Guide to Terms and Conditions <http://www.dfes.gov.uk/studentsupport/uploads/ACF2FEE.pdf> (date accessed: 4 August 2005) at 10 [hereinafter Guide to Terms and Conditions].
[228] *Supra* note 116 at 3.
[229] *Repayment Regulations, supra* note 223, reg. 29. See also Guide to Terms and Conditions, *supra* note 227 at 10.
[230] *Ibid.*, reg. 11(1). See also, Guide to Terms and Conditions, *ibid.* at 9.
[231] *Ibid.*, reg. 29(1). See also, Guide to Terms and Conditions, *ibid.* at 7.
[232] *Ibid.*, reg. 28. See also, Guide to Terms and Conditions, *ibid.* at 12.

former students, loan repayment is based on gross income over £15,000, including all unearned income if it is more than £2000 pounds.[233]

Under the *Higher Education Act 2004*, if a borrower's income falls below £15,000 gross per annum their repayments will cease automatically. However, borrowers cannot apply to defer repayments if their income is over the threshold.[234]

As long as a former student has made all repayments based on income to that date the Student Loan Company will cancel a loan plus any interest when a person: a) reaches age 65; b) dies before the loans is repaid; or c) becomes permanently disabled and is unfit for work.[235] For students entering higher education after September 1, 2006 loans will also be written off 25 years after the April that the borrower first became liable to repay the loan, except for any arrears due.[236] Arrears due, refers to repayments that are due based on the borrower's prior income, which are still outstanding. These payments would still be required to be paid, but any remaining balance would be written off.[237] Generally, only overseas borrowers have arrears due, because they do not make repayments automatically through the tax system.

B. Treatment of Student Loans in Bankruptcy

Bankruptcy in the UK is governed by the *Insolvency Act 1986*[238] and the *Enterprise Act 2002*.[239] Either a debtor or a creditor, who is owed at least £750 that is unsecured, may present a bankruptcy petition to the High Court in London or at a County Court.[240] Similar to Canada, it is expensive to go bankrupt in the UK (approximately £370).[241] When the court makes a bankruptcy order, an Official Receiver is appointed by the Secretary of State. The Official Receiver is a civil servant in the Insolvency Service and an officer of the court.[242] The Official Receiver is responsible for administering a debtor's bankruptcy. The Official Receiver also acts as a trustee of the debtor's bankruptcy estate unless a private insolvency practitioner is appointed.[243] Because of a number of legislative obstacles, private practitioners have little to gain financially from taking on consumer bankruptcy work and are rarely involved in this process.[244]

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[233] *Ibid.*, reg. 15(5)(a), (c). See also Guide to Terms and Conditions, *ibid.* at 12.
[234] See Student Loan Company, online: FAQS online: < http://www.slc.co.uk/noframe/faqs/sssmaint.html > (date accessed: 4 August 2005).
[235] *Repayment Regulations, supra* note 223, reg. 12. See also Guide to Terms and Conditions, *supra* note 230 at 11.
[236] Guide to Terms and Conditions, *ibid.* at 11.
[237] *Ibid.* at 11.
[238] *Insolvency Act 1986* (U.K.) 1986, c. 45 [hereinafter *Insolvency Act 1986*].
[239] *Enterprise Act 2002* (U.K.) 2002, c. 40.
[240] *Insolvency Act 1986, supra* note 238, s. 267. See also Insolvency Service, online: Guide for Creditors <http://www.insolvency.gov.uk/guidanceleaflets/guideforcreditors/guideforcreditors.htm> (date accessed: 4 August 2005.
[241] I. Ramsay, "Bankruptcy in Transition: The Case of England and Wales – The Neo-Liberal Cuckoo in the European Bankruptcy Nests?" in J. Niemi-Kiesilainen, I. Ramsay & W. Whitford, eds., *supra* note 203 at 209.
[242] Insolvency Service, online: Dealing with Debt: How to Petition for Your Own Bankruptcy < http://www.insolvency.gov.uk/guidanceleaflets/dealingwithdebt/howtopetition.htm> (date accessed: 8 August 2005).
[243] *Supra* note 241 at 208.
[244] Ziegel, *supra* note 199 at 112.

Effective April 1, 2004 debtors are generally automatically discharged from bankruptcy after a maximum of 12 months (previously it was 2 to 3 years).[245] This period may be reduced if the Official Receiver concludes his enquiries regarding the debtor's affairs and files a notice in court.[246] Debtors are not entitled to an *automatic* discharge if: they had a previous bankruptcy within the last 15 years; the court has suspended the debtor's discharge; or the debtor is subject to a criminal bankruptcy order.[247] In addition, the Official Receiver may apply to the court for a Bankruptcy Restrictions Order, which means that a debtor will continue to be subject to some restrictions after discharge for a specified period of time.[248]

Prior to the enactment of section 42 of the *Higher Education Act 2004*[249] government-funded student loans were provable and could be extinguished in bankruptcy. However, effective September 1, 2004 for students in England and Wales and March 1, 2005 for students in Northern Ireland, government-funded student loans are no longer provable in bankruptcy and thus cannot be extinguished.[250] There are no exceptions to this provision.[251] Unsecured loans provided by private lenders to fund post-secondary education are treated as regular unsecured debts and are both provable and discharged in bankruptcy.[252]

C. Treatment of Student Loans in Alternative to Bankruptcy Processes

In the U.K., there are two formal alternatives to bankruptcy, which technically could include student loans funded by the government: administration orders and individual voluntary agreements. In addition, the Department of Constitutional Affairs proposed a third option in July 2004 – a "No Income No Assets" debt relief scheme – that is still being consulted on but is expected to be implemented in the next year. Government-funded student loans will not be able to be discharged under this option.[253]

A court can make an administration order when a creditor obtains a judgment in court against a debtor. An administration order is a court-based procedure whereby a debtor makes regular payments to the court towards debts owing to creditors. In order to quality for an administration order, a person's total debts must not be greater than £5000 and a person must have sufficient regular income to make weekly or monthly repayments.[254] Provisions relating to administration orders are set by County Courts. They are not included as a formal provision within the *Insolvency Act 1986*. Outstanding student loans

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[245] *Insolvency Act 1986, supra* note 238, s. 279(1). See also, The Insolvency Service, online: Frequently Asked Questions About the Enterprise Act - Individual < http://www.insolvency.gov.uk/faq/faqeacti.htm#01> (date accessed: 4 August 2005).
[246] *Insolvency Act 1986, ibid.*, s. 279(2).
[247] Insolvency Service, online: Changes to Bankruptcy Under the Enterprise Act 2002 http://www.insolvency.gov.uk/guidanceleaflets/changestobankruptcylaw/changestobankruptcylaw.htm (date accessed: 9 August 2005).
[248] *Insolvency Act 1986, supra* note 238, s. 281.
[249] *HEA, supra* note 58, s. 42.
[250] *Supra* note 224, reg. 39.
[251] Interview of M. Doughty, Central Line Enquiry Officer (30 May 2005) The Insolvency Service.
[252] Interview of L. Riches, Central Line Enquiry Officer (7 June 2005) The Insolvency Service.
[253] Department of Constitutional Affairs, "A Choice of Paths – Better Options to Manage Over-indebtedness and Multiple Debt" (2004), online: < http://www.dca.gov.uk/consult/debt/debt.pdf> (date accessed: 4 August 2005) [hereinafter "Choice of Paths"].
[254] The Insolvency Service, online: Guide to Bankruptcy <://www.insolvency.gov.uk/guidanceleaflets/guidetobankruptcy/guidetobankruptcy.htm> (date accessed: 4 August 2005) at para. 13(b).

are generally greater than £5000 and therefore are generally not subject to an administration order.[255]

An individual voluntary arrangement begins with a formal proposal to one's creditors to pay part or all of one's debts. A debtor must apply to the court and seek assistance from an insolvency practitioner. If at least 75 per cent of creditors vote to accept the proposal then the agreement is binding on all creditors that had notice of the proposal.[256] There are no restrictions with respect to minimum or maximum levels of debt or repayments. Provisions relating to individual voluntary arrangements are outlined in Part VIII of the *Insolvency Act 1986*.[257] Technically, student loans could be included in an individual voluntary arrangement, but it is unlikely that the government (where the creditor is the government -- see Part 2 on securitization) would accept a proposal to reduce the total amount owed. The creditor may consider a proposal to reduce the amount of individual repayments and extend the time period over which the student loan must be repaid.[258]

During July 2004 the Department of Constitutional Affairs issued a consultation document entitled "A Choice of Paths – Better Options to Manage Over-indebtedness and Multiple Debt,"[259] which suggested that the bankruptcy process and the available alternatives were inappropriate for the "can't pay" group of debtors who have little disposable income or assets and cannot make worthwhile repayments. The consultation paper suggested that a way to deal with "can't pay" debtors would be to offer a non-court based form of debt relief, and introduced the concept of a "No Income, No Assets" (NINA) debt relief scheme.[260] The cost of this scheme to the debtor is less than £100 and the intermediary in this process is a debt counsellor, who files the debtor's information online with the Official Receiver.[261] If the debtor meets the criteria for the scheme, a debt relief order is issued that will ultimately result in the debtor being discharged from her debts in one year's time.[262] In order to qualify for the scheme the debtor must have total liabilities of less than £15,000, including both secured and unsecured debt.[263] The same debts that are not extinguished in bankruptcy are not extinguished under NINA, including government-funded student loan debt. These debts do not count towards the £15,000 cap on liabilities for participation in the scheme.[264]

D. Consumer Debts Not Extinguished by Bankruptcy

In addition to government-funded student loans, there are only a few other consumer debts, which are not extinguished by bankruptcy or alternatives to bankruptcy in the U.K.[265] Discharge from bankruptcy releases a person from most debts owed on the date of the bankruptcy order except debts arising from fraud[266] and debts which are not provable.[267]

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[255] *Supra* note 251.
[256] Ziegel, *supra* note 202 at 121. See also Insolvency Service, online: Guide to Bankruptcy <http://www.insolvency.gov.uk/guidanceleaflets/guidetobankruptcy/guidetobankruptcy.htm > (date accessed: 4 August 2005) at para. 13(c).
[257] *Insolvency Act 1986, supra* note 238, Pt. VIII.
[258] *Supra* note 251.
[259] "Choice of Paths", *supra* note 253.
[260] *Ibid.* at para. 35.
[261] *Ibid.*
[262] *Ibid.* at para. 41.
[263] *Ibid.* at para. 35.
[264] *Ibid.*
[265] Ziegel, *supra* note 199 at 119.
[266] *Insolvency Act 1986, supra* note 238, s. 281 (3).
[267] *Ibid.*, s. 281 (6).

Debts which are not provable and thus not extinguished include court fines,[268] liability for personal injury claims,[269] and other obligations arising under an order made in family proceedings or under a maintenance assessment made under the *Child Support Act 1991*.[270] These debts could be included in an administration order, but this is unlikely given that these orders only apply to debts amounting to less than £5000. Technically, these debts could also be included in an individual voluntary agreement, but creditors are not obliged to accept the agreement.[271] These debts could not be extinguished under NINA.[272]

[268] *Ibid.*, s. 281 (4)
[269] *Ibid.*, s. 281 (5) (a)
[270] *Ibid.*, s. 281 (5)(b).
[271] *Supra* note 251.
[272] "Choice of Paths", *supra* note 253.

7. The United States

A. Overview of the Government Student Loan Program

The U.S. government offers two loan programs to students and their parents: direct and guaranteed loans.[273] The U.S. government directly funds direct loans. Guaranteed loans are known as FFEL loans and are funded by private lenders including banks and other eligible lending institutions. These loans are guaranteed by the federal government for close to 100 per cent of the principal and interest.[274] Whether students receive a direct or guaranteed loan depends on the program that their school participates in.[275] It is possible for a student to have both types of loans, but not for the same period of enrolment at the same school.[276] The majority of guaranteed loans are sold on the secondary market to investors through the securitization market.[277] For both direct and guaranteed loans a student can qualify for a subsidized or unsubsidized loan depending on financial need.[278]

There are three forms of direct loans: Federal Perkin Loans and subsidized and unsubsidized Direct Stafford Loans. Under the direct loan programs, the Department of Education provides each school participating in the program a certain amount of funds, which the school is responsible for distributing. The lender is the student's school.[279]

Undergraduate students, in receipt of Federal Perkins Loans, may be awarded up to $4000 a year (maximum $20,000 as an undergraduate).[280] Graduate students may be awarded up to $6000 a year (maximum $40,000 including undergraduate loans).[281] The amount students receive will depend on their financial need, the amount of other aid, and the availability of funds at their school.[282]

For subsidized Direct Stafford Loans students may be awarded $2625 to $8500 a year[283] and for unsubsidized loans from $2625 to $18,5000.[284] The amount students receive is based on their year of study and dependency status.[285] Financial need is only used to determine if a student qualifies for a subsidized loan.[286]

The current interest rate for direct and guaranteed subsidized loans is five per cent.[287] In most cases, interest begins to accrue nine months after a student graduates, withdraws or drops below half-time status. For students attending less than half-time, the interest begins to accrue nine months after from the date the loan is made.[288] Other than interest there are

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[273] DBRS, *supra* note 103 at 2.
[274] *Ibid.*
[275] Federal Student Aid, "The Student Guide: Financial Aid form the U.S. Department of Education 2005 – 2006", online: The Student Guide < http://studentaid.ed.gov/students/attachments/siteresources/Stud_guide.pdf> (date accessed: 4 August 2005) at 20 [hereinafter Guide].
[276] *Ibid.* at 19.
[277] DBRS, *supra* note 103 at 2.
[278] Guide, *supra* note 275 at 18.
[279] 28 U.S.C. tit. 20, §1087bb. See also Guide, *ibid.* at 19.
[280] *Ibid.*, § 1087dd 2(A)(i), B (ii). See also, Guide, *supra* note 279 at 2.
[281] *Ibid.*, § 1087dd 2(A)(ii), B (i).
[282] Guide, *supra* note 275 at 20.
[283] *Ibid.*
[284] *Ibid.*
[285] *Ibid.*
[286] *Ibid.*
[287] *Supra* note 279 § 1087dd (c)(1) (D). See also Guide, *ibid.* at 20.
[288] *Ibid.*, § 1087dd (c)(1)(A). See also Guide, *ibid.* at 24.

no additional fees.[289] For subsidized loans, students, provided they were attending school at least half time, do not have to begin repaying their loans until nine months after they graduate, leave school or drop below half-time status.[290] Payments are made directly to the school that provided them with the loan.[291]

In the case of unsubsidized direct and guaranteed loans the borrower is responsible for the interest on the loan from the time the loan is disbursed until it is paid in full.[292] For 2004-2005 the rate of interest for unsubsidized loans was 3.37 per cent.[293] In addition, students are charged a four per cent loan fee, which deducted from their loan disbursement.[294] Students can pay the interest as it is charged or allow it to accrue.[295] Students may be able to receive both a subsidized and unsubsidized loan for the same enrolment period as long as the combination does not exceed the annual loan limit. The annual loan limit for unsubsidized loans varies depending on the borrower's year of study, whether she is an undergraduate or graduate student and whether she is dependent or independent.[296]

For guaranteed loans, borrowers generally have between 10 and 25 years to repay their loan depending on the amount owed and the type of repayment plan selected.[297] For direct loans, borrowers generally have between 10 and 30 years to repay their loans depending on the amount owed and the repayment plan selected.[298]

For both direct and guaranteed loans there are four repayment options:

- A 10-year Standard Plan with a minimum monthly payment of $50;
- An Extended Plan that provides for repayment of the loan over a longer period;
- A Graduated Plan with a monthly payment that starts out low and then increases gradually during the repayment period; or
- A plan that bases the monthly payment amount on the borrower's income.[299]

For both direct and guaranteed loans, there are three options for borrowers who are having difficulty making repayments: consolidation, deferment and forbearance. Consolidation allows borrowers to simplify the repayment process, and hopefully reduce their monthly repayments, by combining their various federal education loans into one loan.[300] The loan holder pays off the existing loans and replaces them with a consolidation loan.[301] Subsidized consolidation loans are available, so a borrower will not lose the benefit of any interest subsidy they are entitled too.[302] Even if a borrower is in default she might be eligible for a consolidation loan if certain conditions are met.[303]

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[289] Guide, *ibid.* at 20.
[290] *Supra* note 282, §1087dd (c)(1)(A). See also Guide, *ibid.* at 24.
[291] *Ibid.*
[292] Guide, *ibid.* at 21.
[293] *Supra* note 279, § 1087e 9 (c). See also Guide, *ibid.* at 20.
[294] Guide, *ibid.* at 22.
[295] *Ibid.*
[296] *Ibid.* at 21.
[297] *Ibid.* at 20.
[298] *Ibid.* at 21.
[299] *Ibid.* at 25.
[300] Federal Student Aid, "Repaying Your Student Loans", online: Student Aid on the Web < http://studentaid.ed.gov/students/attachments/siteresources/RepayingYourStudentLoansEnglish2003_04.pdf> (date accessed: 4 August 2005) at 17.
[301] *Ibid.*
[302] *Ibid.*
[303] *Ibid.* at 18.

In very specific circumstances a borrower may be able to apply for a deferment, which will postpone any repayment obligations.[304] For subsidized loans a borrower will not have to pay interest or principal during the deferment period.[305] For unsubsidized loans the borrower will not have to pay principal, but will be responsible for paying interest.[306] A deferment cannot be sought for a loan that is in default.[307] Deferment may be granted (applies to loans received after July 1, 1993) to borrowers in the following situations: in at least half-time study at a postsecondary school; studying in an approved graduate fellowship program or in an approved rehabilitation training program for the disabled; unable to find full-time employment (deferment up to 3 years); or in economic hardship (deferment up to three years).[308]

Borrowers who are not eligible for a deferment may apply for forbearance. Unlike deferment, which borrowers are entitled to receive, a loan holder does not have to grant forbearance except in certain mandatory circumstances.[309] During forbearance a borrower's payments are temporarily postponed or reduced, but in all cases the borrower is still responsible for paying the interest on the loan.[310] If the borrower allows the interest to accrue it will be capitalized.[311] Forbearance may be granted where the borrower is unable to pay due to poor health or other unforeseen personal problems; serving in medical or dental internship or residency; serving in a position under the *National Community Service Trust Act* of 1993; or obligated to make payments on certain federal student loans that are equal to or greater than 20 per cent of the borrowers monthly gross income[312]

B. Treatment of Student Loans in Bankruptcy

The *Bankruptcy Code*[313] enacted in 1978 governs bankruptcy in the U.S. Chapter 7 of the *Bankruptcy Code* provides for a court-supervised process. A trustee collects the assets of the debtor's estate, converts them to cash, and distributes the proceeds to creditors, subject to the right of secured creditors and the debtors' right to retain certain exempt property.[314] A Chapter 7 proceeding begins with a debtor filing a petition with the bankruptcy court serving their area.[315] In some circumstances, a creditor may also initiate a Chapter 7 proceeding by filing a petition.[316] In addition to filing a petition, a debtor must file several schedules outlining the debtor's current financial affairs.

If a debtor wants to present a bankruptcy petition there are three fees, which must be paid:

- a $155 USD case filing fee; and
- a $39 USD miscellaneous administrative fee; and
- a $15 USD surcharge.[317]

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[304] *Ibid.* at 19.
[305] *Ibid.*
[306] *Ibid.*
[307] *Ibid.* at 21.
[308] 28 U.S.C. tit. 20 §1087e (f) (2005).
[309] *Supra* note 300 at 21.
[310] *Ibid.*
[311] *Ibid.*
[312] *Ibid.*
[313] U.S.C. tit. 11 (1978).
[314] Bankruptcy Judges Division, Administrative Office of the United States Courts, *Bankruptcy Basics* by Leonidas Ralph Mecham (2000) at 18 [hereinafter Bankruptcy Basics] at 3.
[315] *Supra* note 313 § 301.
[316] *Ibid.*,§ 303.
[317] 123 U.S.C. tit. 28 § 1930 (a).

In addition, the debtor will generally incur attorney fees for a Chapter 7 proceeding, which averaged $505 USD in 1998.[318]

Under Chapter 7, student loans are provable in bankruptcy, but not extinguished on discharge.[319] Section 523(8) of the *Bankruptcy Code*,[320] which applies to Chapter 7 proceedings, states:

> 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.[321]

C. Treatment of Student Loans in Alternative to Bankruptcy Processes

Chapter 13 Individual Debt Adjustment under the *Bankruptcy Code* is an alternative to bankruptcy, which a debtor could pursue. The *Bankruptcy Abuse Prevention Consumer Protection Act of 2005* provides that high-income debtors cannot file for straight bankruptcy under Chapter 7, but are required to reach an arrangement with their creditors under Chapter 13.[322] The purpose of Chapter 13 is "to enable financially distressed individual debtors, under court supervision and protection, to propose and carry out a repayment plan under which creditors are paid over an extended period of time."[323] Under this chapter a debtor is permitted to pay creditors, either in full or in part, in instalments over three years. In some circumstances, a plan that provides for instalments over a longer period of time may be approved, but in no case may a plan provide for payments over a period longer than five years. Relief under Chapter 13 is only available to an individual with regular income that owes, on the date of the filing of the petition, non-contingent, liquidated, unsecured debts of less than $307,675 and non-contingent, liquidated, secured debts of less than $922,975.[324] A Chapter 13 proceeding begins with the filing of a petition and a plan with the bankruptcy court. In order to initiate a Chapter 13 case the following fees must be paid:

- a $155 USD filing fee
- a $39 USD miscellaneous administrative fee[325]

In 1998, average attorney fees for a Chapter 13 proceeding amounted to $1000 USD.[326]

The debtor is entitled to discharge upon successful completion of all payments under the Chapter 13 plan.[327] In limited circumstances, even if a debtor has failed to complete the plan, a court may grant a "hardship discharge."[328]

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[318] "Consumer Bankruptcy Cost Economy 44 Billion in 1997" (1998) 7 Consumer Bankruptcy News.
[319] Interview of J. Wannamke, Attorney on Duty (8 June 2005) from Administration Office of the United States – Thurgood Marshall Federal Judiciary Building.
[320] *Supra* note 47.
[321] *Ibid.*
[322] *Ibid.*
[323] Bankruptcy Basics, *supra* note 314 at 18.
[324] 1 U.S.C. tit. 11 § 109 (e).
[325] Bankruptcy Basics, *supra* note 314 at 19.
[326] *Ibid.*
[327] 13 U.S.C. tit. 11 § 1328 (a).
[328] *Ibid.*, § 1328 (b).

Prior to 1990, government-funded and guaranteed student loans could be discharged in bankruptcy under a Chapter 13 plan, regardless of whether the student would experience undue hardship in repaying them. In 1990, the *Student Loan Default Prevention Initiative Act*[329] was enacted, which rendered student loans undischargeable under Chapter 13.[330] Section 1328(a)(2),[331] references section 523(a)(8), which renders government student loans undischargeable in bankruptcy, unless undue hardship can be proven. However, government student loans may be included in a Chapter 13 plan and instalment payments can be made to reduce the total amount owed.[332]

D. Consumer Debts Not Extinguished by Bankruptcy

Under Chapter 5 § 523[333] the following long list of debts are not discharged in bankruptcy under a Chapter 7 proceeding or in an "undue hardship discharge" under Chapter 13. However, these debts are provable.[334]

523 Exception to Discharge
(a) 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--
(1) for a tax or a customs duty--
(A) of the kind and for the periods specified in section 507(a)(2) or 507(a)(8) of this title, whether or not a claim for such tax was filed or allowed;
(B) with respect to which a return, if required--
(i) was not filed; or
(ii) was filed after the date on which such return was last due, under applicable law or under any extension, and after two years before the date of the filing of the petition; or
(C) with respect to which the debtor made a fraudulent return or wilfully attempted in any manner to evade or defeat such tax;
(2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by--
(A) false pretences, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition;
(B) use of a statement in writing--
(i) that is materially false;
(ii) respecting the debtor's or an insider's financial condition;
(iii) on which the creditor to whom the debtor is liable for such money, property, services, or credit reasonably relied; and
(iv) that the debtor caused to be made or published with intent to deceive; or
(C) for purposes of subparagraph (A) of this paragraph, consumer debts owed to a single creditor and aggregating more than $1,225 for "luxury goods or services" incurred by an individual debtor on or within 60 days before the order for relief under this title, or cash advances aggregating more than $1,225 that are extensions of consumer credit under an open end credit plan obtained by an individual debtor on or within 60 days before the order for relief under this title, are presumed to be nondischargeable; "luxury goods or services" do not include goods or services reasonably acquired for the support or maintenance of the debtor or a dependent of the debtor; an extension of consumer credit under an open end

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[329] *The Student Loan Default Prevention Initiative Act*, Pub. L. No. 101-508, § 3001, 104 Stat. 1388 (1994), (codified at 20 U.S.C. § 1001 (1994)).
[330] P. Somers, "Student Loan Discharge Through Bankruptcy" (1996) 4 Am. Bankr. Inst. L. Rev. 457 at 461.
[331] *Supra* note 329, § 1328 (a) 2.
[332] *Supra* note 327.
[333] *Supra* note 48, § 523.
[334] *Supra* note 327.

credit plan is to be defined for purposes of this subparagraph as it is defined in the Consumer Credit Protection Act;
(3) neither listed nor scheduled under section 521(1) of this title, with the name, if known to the debtor, of the creditor to whom such debt is owed, in time to permit--
(A) if such debt is not of a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim, unless such creditor had notice or actual knowledge of the case in time for such timely filing; or
(B) if such debt is of a kind specified in paragraph (2), (4), or (6) of this subsection, timely filing of a proof of claim and timely request for a determination of dischargeability of such debt under one of such paragraphs, unless such creditor had notice or actual knowledge of the case in time for such timely filing and request;
(4) for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny;
(5) to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for, or support of such spouse or child, in connection with a separation agreement, divorce decree or other order of a court of record, determination made in accordance with State or territorial law by a governmental unit, or property settlement agreement, but not to the extent that--
(A) such debt is assigned to another entity, voluntarily, by operation of law, or otherwise (other than debts assigned pursuant to section 408(a)(3) of the Social Security Act, or any such debt which has been assigned to the Federal Government or to a State or any political subdivision of such State); or
(B) such debt includes a liability designated as alimony, maintenance, or support, unless such liability is actually in the nature of alimony, maintenance, or support;
(6) for wilful and malicious injury by the debtor to another entity or to the property of another entity;
(7) to the extent such debt is for a fine, penalty, or forfeiture payable to and for the benefit of a governmental unit, and is not compensation for actual pecuniary loss, other than a tax penalty--
(A) relating to a tax of a kind not specified in paragraph (1) of this subsection; or
(B) imposed with respect to a transaction or event that occurred before three years before the date of the filing of the petition;
(8) 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;
(9) for death or personal injury caused by the debtor's operation of a motor vehicle if such operation was unlawful because the debtor was intoxicated from using alcohol, a drug, or another substance;
(10) that was or could have been listed or scheduled by the debtor in a prior case concerning the debtor under this title or under the Bankruptcy Act in which the debtor waived discharge, or was denied a discharge under section 727(a)(2), (3), (4), (5), (6), or (7) of this title, or under section 14c(1), (2), (3), (4), (6), or (7) of such Act;
(11) provided in any final judgment, unreviewable order, or consent order or decree entered in any court of the United States or of any State, issued by a Federal depository institutions regulatory agency, or contained in any settlement agreement entered into by the debtor, arising from any act of fraud or defalcation while acting in a fiduciary capacity committed with respect to any depository institution or insured credit union;
(12) for malicious or reckless failure to fulfill any commitment by the debtor to a Federal depository institutions regulatory agency to maintain the capital of an insured depository institution, except that this paragraph shall not extend any such commitment which would otherwise be terminated due to any act of such agency; or
(13) for any payment of an order of restitution issued under title 18, United States Code;
(14) incurred to pay a tax to the United States that would be nondischargeable pursuant to paragraph (1);

(15) not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record, a determination made in accordance with State or territorial law by a governmental unit unless--
(A) the debtor does not have the ability to pay such debt from income or property of the debtor not reasonably necessary to be expended for the maintenance or support of the debtor or a dependent of the debtor and, if the debtor is engaged in a business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business; or
(B) discharging such debt would result in a benefit to the debtor that outweighs the detrimental consequences to a spouse, former spouse, or child of the debtor;
(16) for a fee or assessment that becomes due and payable after the order for relief to a membership association with respect to the debtor's interest in a dwelling unit that has condominium ownership or in a share of a cooperative housing corporation, but only if such fee or assessment is payable for a period during which--
(A) the debtor physically occupied a dwelling unit in the condominium or cooperative project; or
(B) the debtor rented the dwelling unit to a tenant and received payments from the tenant for such period,
but nothing in this paragraph shall except from discharge the debt of a debtor for a membership association fee or assessment for a period arising before entry of the order for relief in a pending or subsequent bankruptcy case;
(17) for a fee imposed by a court for the filing of a case, motion, complaint, or appeal, or for other costs and expenses assessed with respect to such filing, regardless of an assertion of poverty by the debtor under section 1915(b) or (f) of title 28, or the debtor's status as a prisoner, as defined in section 1915(h) of title 28;
(18) owed under State law to a State or municipality that is--
(A) in the nature of support, and
(B) enforceable under part D of title IV of the Social Security Act (42 U.S.C. 601 et seq.); or
(19) that--
(A) is for--
(i) the violation of any of the Federal securities laws (as that term is defined in section 3(a)(47) of the Securities Exchange Act of 1934), any of the State securities laws, or any regulation or order issued under such Federal or State securities laws; or
(ii) common law fraud, deceit, or manipulation in connection with the purchase or sale of any security; and
(B) results, before, on, or after the date on which the petition was filed, from--
(i) any judgment, order, consent order, or decree entered in any Federal or State judicial or administrative proceeding;
(ii) any settlement agreement entered into by the debtor; or
(iii) any court or administrative order for any damages, fine, penalty, citation, restitutionary payment, disgorgement payment, attorney fee, cost, or other payment owed by the debtor.

(b) Notwithstanding subsection (a) of this section, a debt that was excepted from discharge under subsection (a)(1), (a)(3), or (a)(8) of this section, under section 17a(1), 17a(3), or 17a(5) of the Bankruptcy Act, under section 439A of the Higher Education Act of 1965, or under section 733(g) of the Public Health Service Act in a prior case concerning the debtor under this title, or under the Bankruptcy Act, is dischargeable in a case under this title unless, by the terms of subsection (a) of this section, such debt is not dischargeable in the case under this title.

(c)(1) Except as provided in subsection (a)(3)(B) of this section, the debtor shall be

discharged from a debt of a kind specified in paragraph (2), (4), (6), or (15) of subsection (a) of this section, unless, on request of the creditor to whom such debt is owed, and after notice and a hearing, the court determines such debt to be excepted from discharge under paragraph (2), (4), (6), or (15), as the case may be, of subsection (a) of this section.

(2) Paragraph (1) shall not apply in the case of a Federal depository institutions regulatory agency seeking, in its capacity as conservator, receiver, or liquidating agent for an insured depository institution, to recover a debt described in subsection (a)(2), (a)(4), (a)(6), or (a)(11) owed to such institution by an institution-affiliated party unless the receiver, conservator, or liquidating agent was appointed in time to reasonably comply, or for a Federal depository institutions regulatory agency acting in its corporate capacity as a successor to such receiver, conservator, or liquidating agent to reasonably comply, with subsection (a)(3)(B) as a creditor of such institution-affiliated party with respect to such debt.

(d) If a creditor requests a determination of dischargeability of a consumer debt under subsection (a)(2) of this section, and such debt is discharged, the court shall grant judgment in favor of the debtor for the costs of, and a reasonable attorney's fee for, the proceeding if the court finds that the position of the creditor was not substantially justified, except that the court shall not award such costs and fees if special circumstances would make the award unjust.

(e) Any institution-affiliated party of an insured depository institution shall be considered to be acting in a fiduciary capacity with respect to the purposes of subsection (a)(4) or (11).

A broader discharge of debts is available to a debtor in a Chapter 13 proceeding than in Chapter 7 proceeding. The following debts are not discharged in a Chapter 7 proceeding, but can be included in a Chapter 13 plan.[335]

§ 1328. Discharge

(a) Subject to subsection (d), as soon as practicable after completion by the debtor of all payments under the plan, unless the court approves a written waiver of discharge executed by the debtor after the order for relief under this chapter [11 USCS §§ 1301 et seq.], the court shall grant the debtor a discharge of all debts provided for by the plan or disallowed under section 502 of this title [11 USCS § 502], except any debt--

(1) provided for under section 1322(b)(5) of this title [11 USCS § 1322(b)(5)];

(2) of the kind specified in paragraph (5), (8), or (9) of section 523(a) [or 523(a)(9)] of this title [11 USCS § 523(a)]; or

(3) for restitution, or a criminal fine, included in a sentence on the debtor's conviction of a crime.

(b) Subject to subsection (d), at any time after the confirmation of the plan and after notice and a hearing, the court may grant a discharge to a debtor that has not completed payments under the plan only if--

(1) the debtor's failure to complete such payments is due to circumstances for which the debtor should not justly be held accountable;

(2) the value, as of the effective date of the plan, of property actually distributed under the plan on account of each allowed unsecured claim is not less than the amount that would

[335] 13 U.S.C. tit. 11 § 1328.

have been paid on such claim if the estate of the debtor had been liquidated under chapter 7 of this title [11 USCS §§ 701 et seq.] on such date; and

(3) modification of the plan under section 1329 of this title [11 USCS § 1329] is not practicable.

(c) A discharge granted under subsection (b) of this section discharges the debtor from all unsecured debts provided for by the plan or disallowed under section 502 of this title [11 USCS § 502], except any debt--

(1) provided for under section 1322(b)(5) of this title [11 USCS § 1322(b)(5)]; or

(2) of a kind specified in section 523(a) of this title [11 USCS § 523(a)].

(d) Notwithstanding any other provision of this section, a discharge granted under this section does not discharge the debtor from any debt based on an allowed claim filed under section 1305(a)(2) of this title [11 USCS § 1305(a)(2)] if prior approval by the trustee of the debtor's incurring such debt was practicable and was not obtained.