# Human Capital Contracts and Bankruptcy: Balancing the Equities Between Exception to Discharge and the Opportunity to Prove Undue Hardship

*"[T]here's a new hot concept in the land of personal finance: personal corporatehood, the notion that people can act like corporations. . . . [I]t's easy to see something suspect about the idea of young people in a downtrodden economy pledging away part of their livelihood to the investor class. . . . [I]n the future . . . we could wind up with a society where vast numbers of people are traded like stocks, where every life is assigned a monetary value, and where Wall Street bankers bundle the income streams of a bunch of 22-year-olds into exotic financial instruments."*[1]

## I. INTRODUCTION

In times of economic downturn, educational prestige is directly correlated to financial resiliency.[2] Indoctrinated with the belief that virtually all highly-coveted jobs require postsecondary education, many ambitious yet financially disadvantaged young people in the twenty-first century face no alternative than to rely on student loans to fund educational pursuits.[3] While traditional federal and private loans may offer students the opportunity to enter the middle class, the debt incurred from these loans will likely follow them throughout the better part of their lives.[4]

1. Kevin Roose, *The IPO of You and Me: How Normal People Are Becoming Corporations*, N.Y. MAG. (Nov. 19, 2013), http://nymag.com/daily/intelligencer/2013/11/ipo-of-you-and-me.html# [https://perma.cc/B26T-23MX] (foreshadowing human capital contracts' (HCC) potential financial shortcomings).

2. *See* Nicole Hurd, *Defining Higher Education Success*, U.S. NEWS & WORLD REP. (Sept. 13, 2011), http://www.usnews.com/education/articles/2011/09/13/defining-higher-education-success [https://perma.cc/ K7S7-AJ8R] (emphasizing high educational achievement and financial security interconnectedness in economic decline).

3. *See id*. (describing higher education's necessity in job market). Specifically, "[ninety] percent of the fastest-growing jobs in the future will require some postsecondary education or training." *Id*.; *see also* Stephen W. Sather, *Dischargeability of Student Loans in Bankruptcy*, LEXIS NEXIS LEGAL NEWSROOM (May 6, 2014), https://www.lexisnexis.com/legalnewsroom/bankruptcy/b/bankruptcy-law-blog/archive/2014/05/06/dischargeability-of-student-loans-in-bankruptcy.aspx [https://perma.cc/6QCF-LAWZ] (proclaiming students owe over one trillion dollars in student loan debt).

4. *See* Sather, *supra* note 3 (explaining student loan debt attaches to individuals throughout life); *see also* Caroline Ratcliffe & Signe-Mary McKernan, *Forever in Your Debt: Who Has Student Loan Debt, and Who's Worried?*, URB. INST. (June 2013), https://www.urban.org/sites/default/files/alfresco/publication-pdfs/412849-Forever-in-Your-Debt-Who-Has-Student-Loan-Debt-and-Who-s-Worried-.PDF [https://perma.cc/X955-WH32] (highlighting student loan debt follows one out of five Americans over nineteen years old).

An innovative, less-restrictive financing option has gained popularity in recent years: HCCs allow investors to fund young investees' educational and entrepreneurial endeavors in exchange for a percentage of the investee's future income.[5] HCCs uniquely allow these investees to treat themselves as independent, corporate entities.[6] Touted as human "equity-like" investments, HCCs offer an effective alternative for many students skeptical of traditional public and private loans.[7] HCC proponents consider this financing option more financially sound than traditional loan models.[8] Specifically, repayments to investors are contingent upon the investee's actual income rather than traditional loans' fixed interest rates.[9] Furthermore, while mounting federal loan debt has sparked widespread criticism, increasingly progressive online accessibility to wealthy investors suggests HCC and similar lending practices are not likely to dwindle in the immediate future.[10]

5. *See* MIGUEL PALACIOS LLERAS, INVESTING IN HUMAN CAPITAL: A CAPITAL MARKETS APPROACH TO STUDENT FUNDING 41 (2004) [hereinafter PALACIOS, INVESTING IN HUMAN CAPITAL] (describing HCCs' alternative means for financing education). Palacios defines HCCs as "contracts in which students commit part of their future income for a predetermined period of time in exchange for capital for financing education." *Id*. Aside from attaining higher education, investees also use HCCs to fund athletic and entrepreneurial aspirations. *See* Jeff Schwartz, *The Corporatization of Personhood*, 2015 U. ILL. L. REV. 1119, 1122, 1129-30 (2015).

6. *See* Schwartz, *supra* note 5, at 1120-21 (describing human-equity investments in terms of human corporatization); Roose, *supra* note 1 (recounting how "normal people" create corporate identities through HCCs).

7. *See* Miguel Palacios, *Human Capital Contracts: "Equity-like" Instruments for Financing Higher Education*, POL'Y ANALYSIS No. 462 1, Dec. 16, 2002, http://object.cato.org/sites/cato.org/files/pubs/pdf/pa462.pdf [https://perma.cc/8XUA-8R9E] (labeling HCCs, "equity-like" investments). HCCs are "equity-like" because, unlike traditional loans, investors' returns derive from investees' actual earnings as opposed to an established rate. *See id*.; *see also* Ritika Kapadia, Note, *A Solution to the Student Loan Crisis: Human Capital Contracts*, 9 BROOK. J. CORP. FIN. & COM. L. 591, 599-600 (2015) (describing HCCs' equity-like structure because of risk shifting from student to investor).

8. *See* Susan Dynarski & Daniel Kreisman, *Loans for Educational Opportunity: Making Borrowing Work for Today's Students* 13, 30 (Hamilton Project, Discussion Paper No. 2013-05, 2013), http://www.hamiltonproject.org/assets/legacy/files/downloads_and_links/THP_DynarskiDiscPaper_Final.pdf [https://perma.cc/88DE-L625] (arguing income-based repayment models should replace traditional loans). *See* Kapadia, *supra* note 7, at 601 (suggesting HCCs constitute solution to educational loan crisis).

9. *See* James Surowiecki, *The New Futurism*, NEW YORKER (Nov. 4, 2013), https://www.newyorker.com/magazine/2013/11/04/the-new-futurism [https://perma.cc/3RLH-WAT8] (emphasizing HCCs' repayment flexibility compared to traditional loans). Because HCC repayments are structured based on income, the less money an investee earns, the less money he or she owes the investor under the HCC terms. *See id*.

10. *See* Shu-Yi Oei & Diane M. Ring, *The New "Human Equity" Transactions*, 5 CAL. L. REV. CIR. 266, 267 (2014) (predicting technology "magnifies the potential impact" of human equity investments); Andrew Josuweit, *Student Debt Is Already a Hallmark Issue for 2016*, HUFFINGTON POST (Nov. 4, 2015), http://www.huffingtonpost.com/andrew-josuweit/student-debt-is-already-a_b_8392530.html [https://perma.cc/GX24-765D] (forecasting student loan debt would present major issue in 2016 presidential election); Surowiecki, *supra* note 9 (hypothesizing HCCs will "likely become more common"). *But see* Max Vogel, Note, *Crowdfunding Human Capital Contracts*, 36 CARDOZO L. REV. 1577, 1579-80, 1580 n.19 (2015) (addressing Upstart and Pave's HCC discontinuation). Although Upstart and Pave are no longer HCC-financing platforms, HCC regulation remains a pertinent issue given the number of recent scholarly analyses dedicated to its regulation. *See generally* Groshoff et al., *Crowdfunding 6.0: Does the SEC's Fintech Law Failure Reveal the Agency's True Mission to Protect—Solely Accredited—Investors?*, 9 OHIO ST. ENTREPRENEURIAL BUS. L.J. 277, 307 (2015) (describing how HCC-funding platforms currently gain "traction and media attention" for postgraduate educational

Unlike student loan debt, however, the bankruptcy treatment of HCCs remains unanswered.[11] Some scholars suggest resolving HCC bankruptcy treatment similarly to discharging student loans.[12] Student loan debt is considered an "exception" to conventional bankruptcy discharge, and students seeking to discharge traditional student loan obligations are permitted to do so only under limited circumstances.[13]

Although a lofty threshold, if outstanding student-loan debt would present the debtor with undue hardship after filing for bankruptcy, a bankruptcy court may discharge the debt.[14] Despite failed legislative attempts, HCC investees do not yet enjoy the same limited recourse in bankruptcy.[15] The result is that even under circumstances of the most "undue hardship," students choosing to finance their educations by treating themselves as corporate entities must repay these debts to their investors, notwithstanding filing for bankruptcy.[16]

financing); Benjamin M. Leff & Heather Hughes, *Student Loan Derivatives: Improving on Income-Based Approaches to Financing Law School*, 61 VILL. L. REV. 99 (2016) (proposing law school repayment method, Income-Based Repayment Swap (IBR Swap), based on HCCs' appealing structure); Shu-Yi Oei & Diane Ring, *Human Equity? Regulating the New Income Share Agreements*, 68 VAND. L. REV. 681 (2015) [hereinafter Oei & Ring 2015] (proposing HCC regulation); Schwartz, *supra* note 5 (analyzing legal challenges surrounding HCCs); Vogel, *supra* (discussing and analyzing HCC crowdfunding).

11. *See* Schwartz, *supra* note 5, at 1145 n.181 (stating: "The bankruptcy treatment of human equity has not yet been decided"); Vogel, *supra* note 10, at 1608 n.231 (acknowledging traditional student loan bankruptcy dischargeability, while HCC bankruptcy treatment remains unknown). Schwartz suggests HCC bankruptcy treatment should mirror recent dischargeability for student loan debt. *See* Schwartz, *supra* note 5, at 1145 n.181. The current absence of HCC bankruptcy regulation contributes to uncertainty surrounding these instruments. *See* Leff & Hughes, *supra* note 10, at 137 (emphasizing HCCs' unknown bankruptcy treatment sparks regulation concerns); *see also* Colleen Baker, *The Fate of Human Capital Contracts in Bankruptcy*, *in* AN EXECUTIVE BRIEFING ON FINANCING HUMAN CAPITAL 80, 83 (Elizabeth F. O'Halloran et al. eds., 2004) (drawing connections between student loans and HCCs in bankruptcy); Palacios, *supra* note 7, at 8 (asserting need for bankruptcy protection to remove "legal uncertainties" for HCCs).

12. *See* Groshoff et al., *supra* note 10, at 318 (opining like student loans, HCCs constitute nondischargeable obligations in bankruptcy); Leff & Hughes, *supra* note 10, at 138 (hypothesizing if treated like student loans, HCCs would constitute nondischargeable debts absent undue hardship); *The Global Viability of Human Capital Contracts*, ROOSEVELT INST., YALE U. (Dec. 2015), http://static1.squarespace.com/static/549b9425e4b07bee0353cf88/t/56aad58c0ab37725a38581c3/1454036366091/HumanCapitalContractsFinal.pdf [https://perma.cc/P9FV-82A8] (encouraging future research to focus on similar student-loan bankruptcy protection for HCCs). *But see* Dynarski & Kreisman, *supra* note 8, at 30 (asserting private loans "should not survive bankruptcy," suggesting their dischargeability).

13. *See* MARGARET HOWARD, BANKRUPTCY: CASES AND MATERIALS 711 (5th ed. 2012) (reiterating student loan debt remains generally nondischargeable).

14. *See* Sather, *supra* note 3 (recounting student loan dischargeability in bankruptcy because of undue hardship). Discharge in the face of undue hardship affords the debtor a "fresh start" from cumbersome student loan debt. *See* Michael Lux, *Student Loans and Bankruptcy: What the Law Actually Says*, STUDENT LOAN SHERPA (May 20, 2013), http://studentloansherpa.com/student-loans-bankruptcy-law/ [https://perma.cc/RXZ8-5XJH].

15. *See* Schwartz, *supra* note 5, at 1145 n.181, 1174 n.327 (stating human equity investment bankruptcy treatment remains undecided, and describing failed Rubio bill).

16. *See* Investing in Student Success Act of 2014, H.R. 4436, 113th Cong. (2014) (proposing nondischargeability for human-equity-like financing in bankruptcy proceedings). Although this "Rubio-Petri Bill" failed, it is "an example of a unified approach and provides a benchmark for likely reform proposals." Oei & Ring 2015, *supra* note 10, at 686 n.13; *see also* Groshoff et al., *supra* note 10, at 307 (emphasizing

This Note argues that HCC investees' financial obligations to their investors should be dischargeable in bankruptcy similar to student loan debt dischargeability; however, HCC bankruptcy treatment should also protect investors by subjecting dischargeability to an undue hardship threshold.[17] This Note begins by discussing HCCs' history and current trends in the United States.[18] Next, this Note reviews bankruptcy law's goal to provide debtors with a "fresh start" by discharging prebankruptcy student-loan debts if the debtor can prove undue hardship.[19] The analysis argues that similar to student loan debts, HCC payments should be categorized as claims in bankruptcy to protect investors and encourage widespread HCC implementation.[20] Likewise, although there should be a per se exception to discharge, HCCs should be afforded similar, limited bankruptcy discharge.[21] This Note's conclusion reiterates the commonalities between HCCs and student loans, emphasizing their proposed similar bankruptcy dischargeability under limited circumstances.[22]

## II. HISTORY

### *A. Human Capital Contracts*

#### *1. History and Modern Structure*

HCCs permit individuals to acquire immediate financial backing in exchange for a fixed percentage of their income over a set period of time.[23] HCCs operate similarly to income share agreements (ISAs).[24] While HCCs have gained widespread attention in recent years, Nobel Prize winner Milton Friedman proposed an HCC-like financing option as a solution for funding

Investing in Student Success Act's importance in providing students with affordable financing).

17. *See* STAN DAVIS & CHRISTOPHER MEYER, FUTURE WEALTH 139, 163 (2000) (proffering individuals should control human capital risks and government should manage risk through bankruptcy legislation); Dynarski & Kreisman, *supra* note 8, at 7 (proposing greater bankruptcy protection for borrowers for HCC-like financing instruments); *infra* note 148 and accompanying text (demonstrating need to protect HCC investors to encourage HCC proliferation and regulation).

18. *See infra* Part II.A.

19. *See infra* Part II.B.

20. *See infra* Part III.

21. *See id.*

22. *See infra* Part IV.

23. *See* Nicholas Barr, *Foreword* to PALACIOS, INVESTING IN HUMAN CAPITAL, at xix (2004) (outlining basic HCC financial structure).

24. *See* MIGUEL PALACIOS, TONI DESORRENTO, & ANDREW P. KELLY, AM. ENTER. INST., INVESTING IN VALUE, SHARING RISK: FINANCING HIGHER EDUCATION THROUGH INCOME SHARE AGREEMENTS 3 n.6 (2014), https://www.aei.org/wp-content/uploads/2014/02/-investing-in-value-sharing-in-risk-financing-higher-education-through-inome-share-agreements_083548906610.pdf [https://perma.cc/MRA6-ALBW] [hereinafter PALACIOS ET AL., INVESTING IN VALUE] (noting authors use terms "ISAs" and "HCCs" synonymously); *see also* Leff & Hughes, *supra* note 10, at 100 n.9 (using ISA to describe both HCCs and IBR Swaps); *infra* notes 48-52 (discussing ISAs and HCCs interchangeably).

higher education in 1955.[25] Friedman argued that although attaining higher education yields positive "neighborhood effects" for general society, financing higher education is ultimately a private venture because higher compensation more directly benefits the individual student than it does society.[26] Thus, Friedman suggested that the private market rather than the federal government should assist in financing higher education.[27] Identical to many modern HCC structures, Friedman's original proposal contemplated private investors funding professional education through buying shares in students' future incomes.[28] This funding concept became the basis for income-contingent loans (ICLs).[29]

Over thirty-five years after HCCs' original contemplation, Human Capital Resources (HCR) became the first company to actively consider utilizing HCCs.[30] Ultimately, HCR chose not to implement HCCs because of the many legal uncertainties investors would face.[31] In 2001, however, the company MyRichUncle officially utilized HCCs for the first time in history, solidifying Friedman's vision.[32] MyRichUncle's initial success with HCCs was short-lived, however: the company filed for bankruptcy following the 2009 financial crisis.[33]

25. *See* Milton Friedman, *The Role of Government in Education*, *in* ECONOMICS AND THE PUBLIC INTEREST 123, 127-28 (Robert A. Solo ed., 1955) (introducing human equity investment structure by highlighting government's interest in educating children); Schwartz, *supra* note 5, at 1124 (documenting Friedman's early contributions to human equity investment scholarship in 1955); David Bornstein, *A Way to Pay for College, With Dividends*, N.Y. TIMES (June 2, 2011), http://opinionator.blogs.nytimes.com/2011/06/02/a-way-to-pay-for-college-with-dividends/?_r=0 [https://perma.cc/A79X-WZ6Z] (acknowledging HCCs "are not a new idea"). Friedman first introduced the HCC concept in a footnote, suggesting, "at first blush [HCCs] may seem fantastic." *See* PALACIOS, INVESTING IN HUMAN CAPITAL, *supra* note 5, at 41 (citation omitted) (describing HCCs' naissance deriving from Friedman's early proposals).

26. *See* Friedman, *supra* note 25, at 124 (balancing higher education's general societal and private investment benefits); Schwartz, *supra* note 5, at 1124 (detailing Friedman's private categorization for higher education investing).

27. *See* Friedman, *supra* note 25, at 144 (concluding private market rather than government should source educational financing due to students' direct benefits); Schwartz, *supra* note 5, at 1124 (reiterating higher education's privately-funded nature based on Friedman's categorization).

28. *See* PALACIOS, INVESTING IN HUMAN CAPITAL, *supra* note 5, at 41.

29. *See* Surowiecki, *supra* note 9 (describing interconnectedness between HCCs and ICLs). Like HCCs, ICLs are financing instruments where lenders share in an individual's income. *See id.*

30. *See* Palacios, *supra* note 7, at 8 (discussing HCR's original HCC implementation stemming from desire for new educational financing option).

31. *See id*. HCR lobbied for Congress to modify existing laws to minimize these legal apprehensions. *See id.* at 8 n.14. HCR specifically proposed: "(1) validation of [HCCs], (2) *modification of bankruptcy laws*, (3) clarification of tax treatment of [HCCs], and (4) definition of [HCCs] as securities so that investment institutions can hold them." *Id*. (emphasis added).

32. *See* PALACIOS, INVESTING IN HUMAN CAPITAL, *supra* note 5, at 49 (considering MyRichUncle "the first entrepreneur[] to make Friedman's idea a reality").

33. *See Human Capital Contracts Could Revolutionize the Way We Borrow Money*, VICE (Oct. 13, 2014), https://www.vice.com/read/rumpelstiltskin-loans-0000466-v21n10 [https://perma.cc/8KDA-W7RK] [hereinafter VICE] (discussing MyRichUncle's short-lived financial platform resulting from "founders being ahead of their time"); *My Rich Uncle . . . Not Feeling So Flush; "Pauses" Private Lending (Update)*, STUDENT LENDING ANALYTICS BLOG (Sept. 5, 2008), https://studentlendinganalytics.typepad.com/student_lending_analytics/2008/09/my-rich-unclenot-so-rich-after-all-suspends-private-lending.html [https://perma.cc/SNF5-

In 2012, two new companies—Pave and Upstart—began offering HCC financing for educational and professional pursuits.[34] Using Upstart's platform, Security and Exchange Commission (SEC) "accredited investors" could loan money to recent college graduates for any educational or entrepreneurial venture in exchange for up to two to six percent of the borrower's income for as long as five years.[35] Pave also began offering HCCs in 2012; "Backers" offered "Talents," or borrowers, funding in exchange for up to ten percent of the borrower's income for a maximum of ten years.[36]

Both Upstart and Pave made profits funding exchanges between borrowers and investors.[37] The companies treated borrower default differently, however; Upstart's deferral policy provided that deferred payments would increase the borrower's contract term by one year if his or her income dropped below a certain amount.[38] Pave did not have an extending period if a Talent's income fell below 150% of the poverty line, but if the Talent was enrolled in school, the repayment period would be extended.[39] Currently, both Upstart and Pave offer more traditional loan programs in lieu of HCCs.[40]

KE5V] (tracking MyRichUncle's prebankruptcy economic downfall).

34. *See* Oei & Ring 2015, *supra* note 10, at 690-93 (documenting Pave and Upstart comprehensively over time); Kapadia, *supra* note 7, at 606-07 (explaining how Pave and Upstart constitute solutions to student loan dilemma); *see also* Alison Griswold, *A Group of Investors Is Buying a Stake in the Next Generation of Geniuses*, BUS. INSIDER (Feb. 22, 2014), https://www.businessinsider.com/upstart-and-pave-investing-in-human-capital-2014-2 [https://perma.cc/K99M-DHZV] (noting Upstart founder, Dave Girouard's, original mission in starting Upstart). According to Girouard, Upstart was primarily founded to help facilitate individuals' goals, whatever they may be. *See* Griswold, *supra*.

35. *See* Oei & Ring 2015, *supra* note 10, at 690 & n.28 (describing Upstart's investment structure); Rachel Louise Ensign, *'Crowdfunding' College Costs*, WALL STREET J. (Oct. 19, 2012), http://www.wsj.com /articles/SB10000872396390444657804578048461063769132 (describing limitless purposes for use of funds raised on Upstart); Griswold, *supra* note 34 (noting "accredited investors" have either net worth of $1,000,000 or salary of $200,000 for both Upstart and Pave).

36. *See* Oei & Ring 2015, *supra* note 10, at 691-92 (outlining and comparing Pave's structure to Upstart's, including terminology). While Pave is less transparent about its contractual terms than Upstart, like Upstart, Pave investors also must be SEC accredited. *See* Griswold, *supra* note 34.

37. *See* Griswold, *supra* note 34 (discussing Pave and Upstart's profit-making structures through funding human capital exchanges). Both Upstart and Pave collected 3% of what students initially raised, but Upstart charged an annual 0.5% on repayments to lenders while Pave charged 1.5%. *See id*.

38. *See* Oei & Ring 2015, *supra* note 10, at 691 (outlining Upstart's deferral provisions and parameters).

39. *See id.* at 692-93 (highlighting differences between Upstart and Pave's contractual provisions). Additionally, Pave's Talents could opt to terminate the HCC earlier than the agreed time period by paying their Backers five times their original funding amount. *See id*. at 693; *Upstart Income Share Agreement*, UPSTART, https://www.upstart.com/funding_terms (last visited Nov. 21, 2016) [https://perma.cc/9C9C-9YX9] (establishing contractual provision regarding HCC-deferral consequences in sections 2(b)-(c)).

40. *See* Oei & Ring 2015, *supra* note 10, at 691, 693 (discussing Upstart and Pave's decision to offer traditional loan financing structures); Vogel, *supra* note 10, at 1580 n.19 (noting Upstart and Pave's current HCC discontinuation). Upstart, however, "continues to distinguish their loans from more traditional loan products on the grounds that their model incorporates factors such as educational institution attended, academic area of study, academic performance, and employment history in determining the applicable interest rate." Oei & Ring 2015, *supra* note 10, at 691. Pave similarly employs a multi-faceted approach to lending by considering a borrower's multiple attributes.

### *2. Human Capital Contracts Versus Traditional Loans*

HCCs and ICLs offer borrowers a number of financial advantages over traditional loans.[41] For instance, HCCs provide students of many diverse backgrounds access to financing "without requiring a government guarantee or subsidy," and incentivize investors to support their investee students through mentoring.[42] Additionally, a student whose income drops below a certain threshold is not required to make immediate repayments, although the repayment term may be extended for up to fifteen years.[43] Nevertheless, borrowers who are financially able to repay their loans but fail to do so may face delinquency consequences that are similar to traditional loans, including credit report filings, collection agency involvement, and interest rates of up to fifteen percent.[44] In short, borrowers who are financially capable of repaying investors will be held to their HCCs.[45] Conversely, students who anticipate earning a significant income may limit the amount they repay by electing a "human capital option" (HCO) that contractually prevents a borrower from overpaying if they earn above a certain amount.[46]

### *3. Implementation Challenges*

Despite HCCs' allure for many students, their implementation is fraught with regulatory, constitutional, and ethical challenges.[47] The greatest challenge

41. *See* PALACIOS ET AL., INVESTING IN VALUE, *supra* note 24, at 1-2 (advocating for ISAs to replace traditional loans).

42. *See id*. (describing ISA benefits over traditional loans through mentoring and preferable loan selection structure).

43. *See* Paul Sullivan, *A Financial Backer When a Parent's Wallet Isn't an Option*, N.Y. TIMES (June 7, 2013), https://www.nytimes.com/2013/06/08/your-money/upstart-matches-young-people-with-investors.html (detailing Upstart's payment extension period for low-earning students).

44. *See* Tara Siegel Bernard, *Program Links Loans to Future Earnings*, N.Y. TIMES (July 19, 2013), https://www.nytimes.com/2013/07/20/your-money/unusual-student-loan-programs-link-to-future-earnings.html?_r=0 (linking HCC delinquent payment treatment to traditional loans when borrower possesses repayment capability); Sullivan, *supra* note 43 (highlighting "staggering" fifteen percent interest rate if HCCs face conversion to traditional loans through default). Given the significant risk that many students will default on their student loan payments, traditional loan interest rates are higher than most students could ever feasibly afford. *See* Eric C. Hallstrom, Note, *Here We Go Again—The Conversion of Qualified Scholarship Funding Corporations from Nonprofit to For-Profit Status: What We Can Learn from the Health Care Conversion Bonanza*, 25 J. CORP. L. 659, 664 (2000) (demonstrating student loans' exorbitant interest rates); *see also Can I Defer Payment?*, PAVE, http://support.pave.com/knowledge_base/topics/can-i-defer-payment (last visited Mar. 22, 2016) [https://perma.cc/Y68M-YRVJ] (illustrating Pave's significant delinquency consequences for non-HCC loans).

45. *See* Sullivan, *supra* note 43 (explaining investors hold financially capable borrowers responsible for failure to repay HCCs).

46. *See* PALACIOS, INVESTING IN HUMAN CAPITAL, *supra* note 5, at 85 (considering HCOs "puts or calls" in managing borrower risk); Barr, *supra* note 23, at xix (noting HCOs constitute separate contracts to thwart borrower overpayment). Therefore, HCCs are preferable to traditional loans because they offer financial protection to both parties in the case of either nonpayment or overpayment. *See* PALACIOS, INVESTING IN HUMAN CAPITAL, *supra* note 5, at 85.

47. *See* Palacios, *supra* note 7, at 7-10 (reviewing challenges facing HCCs).

to widespread HCC use is the lack of federal regulation.[48] In particular, the lack of bankruptcy regulation surrounding HCCs severely impedes implementation because HCC investors are currently entirely unprotected if an investee files for bankruptcy.[49] Investors' vulnerability is especially concerning when investees intentionally file for bankruptcy to avoid these very financial obligations.[50] Indeed, HCC implementation critically depends on protecting investors principally through amending bankruptcy laws.[51]

HCC utilization faces additional regulatory and constitutional challenges: Although both Democrats and Republicans have introduced legislation for HCCs, these bills have failed to gain substantial traction.[52] HCCs have also faced Thirteenth Amendment challenges because contractual investments in future income is somewhat reminiscent of human ownership: HCC proponents consider this argument weak, however, given that investees retain full freedom of choice in HCCs.[53]

In addition to regulatory and constitutional challenges, accessibility to HCCs is not always evenly distributed across genders and socio-economic classes.[54] When deciding whether and to what extent to invest in a particular student,

48. *See* PALACIOS ET AL., INVESTING IN VALUE, *supra* note 24, at 12.

49. *See* Palacios, *supra* note 7, at 8 n.14 (regarding "modification of bankruptcy laws" among "most crucial" for successful implementation).

50. *See* Groshoff et al., *supra* note 10, at 304-05 (describing making student loans nondischargeable stems from fear of students "tak[ing] advantage of bankruptcy"); Kapadia, *supra* note 7, at 610 (framing need for HCC investor protection against intentional bankruptcy filing).

51. *See* Palacios, *supra* note 7, at 8 n.14 (highlighting bankruptcy regulation's crucial role for HCC implementation).

52. *See* Investing in Student Success Act of 2014, H.R. 4436, 113th Cong. (2014). Although the bill died at the 113th Congress's close, in April 2014, Senator Marco Rubio and former Representative Tom Petri introduced the "Investing in Student Success Act"—a bill "seeking to clarify the legality of ISAs and their treatment under securities, tax, bankruptcy, and usury laws." Oei & Ring 2015, *supra* note 10, at 686 & n.13. Such proposals demonstrate desire for needed HCC regulation. *See* Groshoff et al., *supra* note 10, at 307 (praising Investing in Student Success Act); Oei & Ring 2015, *supra* note 10, at 686 & n.13. However, reflecting on the lack of HCC federal regulation, others dismally describe previously proposed bills as "descend[ing] into committee, a legislative morass from which they may never emerge." VICE, *supra* note 33.

53. *See* PALACIOS, INVESTING IN HUMAN CAPITAL, *supra* note 5, at 105-09 (arguing HCCs do not constitute partial slavery because no suppression of individual free will); Barr, *supra* note 23, at xix (considering whether HCCs create form of slavery, concluding they do not). Professor Barr supports the argument that HCCs are not a form of slavery because a well-informed student commits a "fraction of her future *income* not her future *activities*, and thus retains full freedom over her future course of action." Barr, *supra* note 23, at xix (emphasis original).

54. *See* PALACIOS, INVESTING IN HUMAN CAPITAL, *supra* note 5, at 110-11 (describing HCCs' potentially unethical discrimination between genders and socio-economic statuses); Mary L. Heen, *From Coverture to Contract: Engendering Insurance on Lives*, 23 YALE J.L. & FEMINISM 335, 335 (2011) (describing general contractual inequalities between genders); Leff & Hughes, *supra* note 10, at 101 (asserting objections to HCCs based on fear investors believe male, privileged students constitute best investments); PALACIOS ET AL., INVESTING IN VALUE, *supra* note 24, at 10 (questioning whether ISAs discriminate against women and minorities more than traditional loans). Ultimately, Palacios argues that HCCs do not employ arbitrary discrimination between individuals because they reflect systematic financial expectations rather than subjective prejudices. *See* PALACIOS, INVESTING IN HUMAN CAPITAL, *supra* note 5, at 110.

investors consider numerous personal factors, including a student's academic institution, socio-economic status, and academic focus.[55] Students whose future careers promise the greatest financial return often raise the most funds and owe the lowest income percentages to investors; financially desperate students, on the other hand, are the least likely to gain any funding, and those who do generally pay investors a significant portion of their future earnings.[56] This imbalanced distribution undermines HCCs' cornerstone goal of ensuring a fair and mutually beneficial investment structure for both the investee and investor.[57] To balance financially disadvantaged students' economic needs against investors' desires to maximize profits, some HCC platforms promote a mentor-mentee relationship between the parties.[58] Notwithstanding these attempts to level the playing field, "inertia" likely contributes to many students' disinclinations to pursue HCCs over traditional student loans.[59]

### *B. Bankruptcy Law Overview: Claims, Discharge, and the "Fresh Start"*

When a debtor files for bankruptcy, his or her creditors may have either a claim against or an interest in the debtor's nonexempt property.[60] Equity interests are residual property interests and typically refer to corporate shares.[61]

55. *See* Kapadia, *supra* note 7, at 612 (describing various considerations HCC investors use evaluating investee potential). Analysts consider these many factors to ascertain an HCC's contractual value. *See id*.

56. *See* Vogel, *supra* note 10, at 1588-89 (recognizing investors may only make HCCs available to students who pursue lucrative careers); Siegel Bernard, *supra* note 44 (suggesting those with high earning potential can raise greater funds for lower repayment amounts). Given that HCCs are priced based on students' anticipated algorithmic future earnings, students may be encouraged to lie about the information they provide about themselves. *See* Bornstein, *supra* note 25 (questioning students' future career truthfulness because of HCC disparate treatment). Because students with more lucrative future careers will be asked to pay lower interest rates, "what is to stop a student who secretly wants to become a teacher from pretending that he wants to become a banker?" *See id*.

57. *See* Vogel, *supra* note 10, at 1589 (highlighting discrepancy between HCC fairness objectives and fund distribution trends).

58. *See id*. (discussing mentor-mentee relationship goals); Siegel Bernard, *supra* note 44 (noting investor mentor relationships constitute HCC "perk"). Through the mentor-mentee relationships, the mentor "groom[s] and mold[s] the [mentee] they invest in to ensure . . . that the [mentee] pursue[s] a lucrative field upon graduation." Vogel, *supra* note 10, at 1589. Some investors also have altruistic motives for investing in HCCs, including simply wanting to help young people and supporting conscientious individuals. *See id*. at 1591-92; Dwyer Gunn, *Investing in Human Capital, One Person at a Time*, FREAKNOMICS (Feb. 1, 2013), https://freakonomics.com/2013/02/01/investing-in-human-capital-one-person-at-a-time/ [https://perma.cc/DQK9-EXAD] (recounting investor's desire to support "hard workers who believe in who they are"); Sullivan, *supra* note 43 (describing HCC investor's motive in terms of "want[ing] to help young people").

59. *See* Vogel, *supra* note 10, at 1602 & n.191 (acknowledging HCC-implementation obstacle of consumer unwillingness to choose unfamiliar financing means). Indeed, Siegel Bernard predicts HCCs are "unlikely to put even a tiny dent in the vast market for federal and private student loans." Siegel Bernard, *supra* note 44.

60. *See* BAKER, *supra* note 11, at 82-83 (describing difference between claims and interests).

61. *See id*. at 83-84 (explaining term "interests" remains undefined in the Bankruptcy Code (the Code)). Equity securities are generally understood and discussed as "corporate shares, partnership interests, or related nonconvertible warrants or rights." *Id*.; *see also* 11 U.S.C. § 101(16)(A)-(C) (2012) (defining equity security in Code in primarily corporate context).

A claim is defined as a "right to payment" and entitles creditors to payments on debts.[62]

Creditors' claims may be either unsecured or secured by a lien on the debtor's property.[63] Student loan debts, for example, are categorized as unsecured claims because creditors do not have a security interest in the debtor's property to secure repayment.[64] Whether a claim is secured or unsecured is significant because secured creditors are paid out of the bankruptcy estate before unsecured creditors.[65] Most debtors file for bankruptcy relief under chapter 7 of the Code, which allows them to liquidate nonexempt assets to repay creditors vis-a-vis their claims' secured statuses.[66] HCCs have yet to be defined as equity interests or claims in chapter 7 bankruptcies.[67]

Bankruptcy law's major goal is to offer a fresh start to "honest but unfortunate debtors."[68] Honoring debtors' opportunities to accomplish this fresh start necessarily involves balancing discharge considerations and creditors' bona fide rights to repayment.[69] Debtors are generally entitled to discharge all prepetition financial obligations under the Code to effectuate the

62. *See* § 101(5) (defining claim in terms of "right to payment" or equitable remedy under Code); § 101(12) (defining debt in terms of "liability on a claim").

63. *See* 11 U.S.C. § 506(a)(1) (2012) (describing secured and unsecured claims). Secured claims are secured by liens on the debtor's property to the financial extent of the value of the creditor's interest. *See id*. Unsecured claims are claims that are not secured by the value of any lien. *See id.*; *see also* Bank of Am. v. Caulkett, 135 S. Ct. 1995, 1998-99 (2015) (defining secured and unsecured claims via statutory construction).

64. *See In re* Chambers, 348 F.3d 650, 652 (7th Cir. 2003) (noting unsecured nature of debtor's student loan debt); *supra* note 63 (describing difference between secured and unsecured claims).

65. *See* Catherine E. Vance & Paige Barr, *The Facts & Fiction of Bankruptcy Reform*, 1 DEPAUL BUS. & COM. L.J. 361, 374-75 (2003) (emphasizing "supremacy" of secured claims over unsecured claims). Secured claims' collateral value will determine if and to what extent holders of unsecured claims will be paid. *See id*. at 374; *see also* Leff & Hughes, *supra* note 10 at 137 (noting low priority bankruptcy debts often subjected to discharge). Leff and Hughes suggest that HCCs would fall into a low priority bankruptcy classification, and thus be subject to discharge. *See* Leff & Hughes, *supra* note 10, at 137.

66. *See Chapter 7—Bankruptcy Basics*, U.S. CTS., http://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-7-bankruptcy-basics (last visited Nov. 22, 2016) [https://perma.cc/7Q9R-4GND] [hereinafter *Bankruptcy Basics*] (describing significant chapter 7 purpose of liquidating nonexempt property to repay creditors); *Chapter 13 vs. Chapter 7 Bankruptcy*, FINDLAW, http://bankruptcy.findlaw.com/chapter-13/chapter-13-vs-chapter-7-bankruptcy.html (last visited Nov. 22, 2016) [https://perma.cc/YPK9-P52J] (suggesting most debtors file under chapter 7 for ease and unsecured debt elimination).

67. *See* Baker, *supra* note 11, at 83-84 (outlining arguments on whether HCCs should constitute claims or equity interests).

68. *See, e.g.*, Marrama v. Citizens Bank of Mass., 549 U.S. 365, 366 (2007) (discussing Congress's goal in enacting Code); Grogan v. Garner, 498 U.S. 279, 287 (1991) (reiterating Code's purpose to provide fresh start to "honest but unfortunate debtor[s]"); Stellwagen v. Clum, 245 U.S. 605, 617 (1918) (emphasizing Code's purpose of providing unfortunate debtors with fresh starts following bankruptcy); *see also* Daniel J. Bussel, *Textualism's Failures: A Study of Overruled Bankruptcy Decisions*, 53 VAND. L. REV. 887, 900 (2000) (praising Code's comprehensive structure based on "100 years of extensive prior federal experience").

69. *See* Thomas H. Jackson, *The Fresh-Start Policy in Bankruptcy Law*, 98 HARV. L. REV. 1393, 1395 (1985) (describing need to strike balance between promoting discharge and honoring creditors' claims).

fresh start after asset liquidation.[70]

Although a broad entitlement, discharge is not absolute.[71] For instance, liens constitute secured claims that survive chapter 7 bankruptcies and cannot usually be discharged.[72] Some debts, like fraudulently transferred property, are statutorily denied discharge under § 727.[73] The Code also provides outright exceptions to discharge under § 523 for some debts, including, for example, those resulting from taxes, domestic support obligations, and student loans.[74]

HCC bankruptcy treatment remains unresolved.[75] Challenges in evaluating a debtor's payment obligations under HCCs, as well as enforcing nonfinancial terms postpetition, exacerbate creditors' already scant chances of financial repayment.[76] Despite ambiguous bankruptcy treatment, since the 1898 Bankruptcy Act, courts have generally protected debtors from paying future income to creditors.[77] For instance, in *Local Loan Co. v. Hunt*,[78] the Supreme Court permitted discharging a debtor's prepetition assignments of future income to repay loans.[79]

70. *See* Baker, *supra* note 11, at 86 (describing bankruptcy generally discharges all prepetition debts). *See generally* 11 U.S.C. § 524 (2012) (proscribing bankruptcy discharge's effect).

71. *See Bankruptcy Basics*, *supra* note 66 (considering general bankruptcy discharge power "not absolute").

72. *See* 11 U.S.C. § 101(37) (2012) (considering liens "interest[s] in property to secure [debt] payment . . . or performance of an obligation"); Bank of Am. v. Caulkett, 135 S. Ct. 1995, 1995 (2015) (holding debtor cannot strip away underwater junior mortgage lien through bankruptcy); Stephen Elias, *What Happens to Liens in Chapter 7 Bankruptcy?*, https://www.nolo.com/legal-encyclopedia/what-happens-liens-chapter-7-bankruptcy.html (last visited Nov. 22, 2016) [https://perma.cc/SR6D-ACTZ] (noting liens generally survive chapter 7 bankruptcies).

73. *See generally* 11 U.S.C. § 727 (2012) (listing nondischargeable debts).

74. *See* 11 U.S.C. § 523(a) (2012); *see also* Roy Chapman, *Legislative Requirements for Human Capital Contracts*, *in* AN EXECUTIVE BRIEFING ON FINANCING HUMAN CAPITAL 96, 100 (Elizabeth F. O'Halloran et al. eds., 2004) (observing "there are really only two" discharge exceptions: student loans and luxury purchases facing bankruptcy).

75. *See* Baker, *supra* note 11, at 85, 87 (noting while bankruptcy generally discharges claims, ambiguity surrounds whether HCCs constitute exceptions to discharge); Leff & Hughes, *supra* note 10, at 137 (stressing ambiguity surrounding HCC bankruptcy regulation).

76. *See* Baker, *supra* note 11, at 85 (presenting challenges with valuating HCC payment obligations). Where valuation is already a "contentious and heavily litigated issue," courts will likely face difficulties liquidating HCCs. *See id*. Professor Baker suggests courts may allow claims solely for debtor's prepetition earnings because students cannot be compelled to work pursuant to the HCCs. *See id*.; *see also* George Triantis, *A Different Perspective on Bankruptcy*, *in* AN EXECUTIVE BRIEFING ON FINANCING HUMAN CAPITAL 94 (Elizabeth F. O'Halloran et al. eds., 2004) (agreeing courts would divide prepetition and postpetition claims requiring challenging valuation for nonfinancial term). Courts may, however, treat HCCs as executory contracts, providing the debtor with the option to reject the HCC, which would discharge *future* obligations under the HCC. *See* Triantis, *supra*, at 94-95.

77. *See* Chapman, *supra* note 74, at 100 (presenting courts' long-held policy of protecting debtors' future, unearned income); Jackson, *supra* note 69, at 1432 (reiterating human capital's traditional bankruptcy discharge protection).

78. 292 U.S. 234 (1934).

79. *See id*. at 245 (refusing to except debtor's future income assignment from bankruptcy discharge); *see also* Jackson, *supra* note 69, at 1432 (recounting bankruptcy law's traditional human capital protection). Emphasizing the importance of a fresh start for good-faith debtors, the Court stated: "The new opportunity in

### *C. Undue Hardship: The "Exception to the Exception" of Student Loan Bankruptcy Discharge*

#### *1. Requiring Undue Hardship for Discharge*

Student loan borrowers currently owe more than one trillion dollars in debt.[80] More staggering perhaps, is that seven million of these students are in default on their loan repayments.[81] From June 2015 to June 2016, 509,769 individuals voluntarily filed for bankruptcy relief under chapter 7.[82] Those with student loan debt face the highest risk of filing for bankruptcy.[83]

Before 1978, the Code freely permitted student loan discharge.[84] In 1978, Congress amended the Code to permit governmental or nonprofit organization loan discharge only if repayment imposed an undue hardship on the debtor.[85] In 2005, Congress extended the undue hardship requirement to private loans.[86] The increasing number of recent graduates filing for bankruptcy to discharge their loan obligations prompted the Code's statutory tightening.[87] Presently, neither public nor private student loans are dischargeable unless a court finds undue hardship.[88] Loans that fall into Code § 523(a)(8)(A)(ii)'s broad

life . . . which . . . is the purpose of the Bankruptcy Act . . . would be of little value to the wage-earner if he [had to] devot[e] the whole or a considerable portion of his earnings . . . in the future to the payment of indebtedness incurred prior to his bankruptcy." *Local Loan Co.*, 292 U.S. at 245.

80. *See* Susan Dynarski, *Why Students with Smallest Debts Have the Larger Problem*, N.Y. TIMES (Aug. 31, 2015), https://www.nytimes.com/2015/09/01/upshot/why-students-with-smallest-debts-need-the-greatest-help.html?_r=1 [https://perma.cc/RFZ6-LPMF?type=live] (citing student loan debt statistics based on Department of Education data).

81. *See id*.; *see also* Groshoff et al., *supra* note 10, at 302 (suggesting government responds to staggering student debt by seeking to increase students' bankruptcy protection).

82. *See* Admin. Office of U.S. Courts, Bankruptcy Filings (June 30, 2016), at tbl. F-2, http://www.uscourts.gov/statistics/table/f-2/bankruptcy-filings/2016/06/30 (click on "Download Data Table" link) (last visited Nov. 22, 2016) [https://perma.cc/5ZX3-MHQD] (compiling bankruptcy court filings by chapter across circuits for twelve-month period).

83. *See* Al Krulick, *Bankruptcy Statistics*, DEBT.ORG, https://www.debt.org/bankruptcy/statistics/ (last visited Nov. 22, 2016) [https://perma.cc/397W-DAUY] (relying on bankruptcy study to conclude student loan debt increases chances of bankruptcy filing).

84. *See* Mhyre v. U.S. Dep't. of Educ. (*In re* Mhyre), 503 B.R. 698, 703 (Bankr. W.D. Wis. 2013) (explaining absence of undue hardship requirement in Code prior to 1978). Chapman recollects that before the 1978 Code, "some students whose assets upon graduation . . . consisted of a white shirt, a tie, and a smile, declared bankruptcy and were released from their student loan obligations." Chapman, *supra* note 74, at 99-100.

85. *See Mhyre*, 503 B.R. at 703 (tracking Code's evolution in finding undue hardship sufficient to discharge student loan debt). Although the 1978 Code amendment limited discharge due to undue hardship for five years after governmental units or nonprofit organization loans became due, Public Law 105-244 eliminated this time restriction, allowing discharge in the face of undue hardship no matter how long the loan had been due. *See* Higher Education Amendments of 1998, Pub. L. No. 105–244, § 971(a), 112 Stat. 1837 (1998) (excluding loan time limitation for finding undue hardship). In 2005, Congress amended the Code to also include private student loans within discharge provisions. *See Mhyre*, 503 B.R. at 703.

86. *See Mhyre*, 503 B.R. at 703.

87. *See id*. (explaining rationale behind requiring undue hardship to discharge student loan debt).

88. *See* Monette Cope, *The 8th Circuit Opens the Door to Partial Discharge of Student Loans and*

"educational benefit" category are nondischargeable, although courts' interpretations of "educational benefit" vary in individual circumstances.[89]

Courts strictly construe undue hardship.[90] Undue hardship is a limited "exception to the exception" that student loan debt is generally nondischargeable.[91] Cases involving undue hardship have gained significant judicial attention in recent years.[92] Because the Code does not define undue hardship, courts apply either the Brunner test or the totality of the circumstances test (TCT) to determine whether undue hardship exists in a particular case.[93]

### *2. The Brunner Test*

In 1987, the Second Circuit first announced the Brunner test to examine

*Upends the Totality of the Circumstances Test*, WW&R BANKR. (Aug. 27, 2014), http://wwrbankruptcy.com /2014/08/27/the-8th-circuit-opens-the-door-to-partial-discharge-of-student-loans-and-upends-the-totality-of-the-circumstances-test/ [https://perma.cc/9Q3G-65WV] (noting bankruptcy does not discharge student loan debt unless court finds undue hardship); Patrick Lunsford, *Court Ruling May Pave Way for Some Student Loan Discharge in Bankruptcy*, INSIDEARM (Aug. 28, 2014), https://www.insidearm.com/ daily/featured-post/ court-ruling-may-pave-way-for-some-student-loan-discharge-in-bankruptcy/ [https://perma.cc/LY2W-V88C] (considering student loans "notoriously difficult to discharge in bankruptcy").

89. *See* Benson v. Corbin (*In re* Corbin), 506 B.R. 287, 287 (Bankr. W.D. Wash. 2014) (employing broad "educational benefit" interpretation in holding co-signing debtor's loan constituted educational benefit under Code). *But see* Decena v. Citizens Bank (*In re* Decena), 549 B.R. 11, 14 (Bankr. E.D.N.Y. 2016) (construing "educational benefit" more narrowly, refusing to consider private medical school loan educational benefit). The *Decena* court noted that § 523(a)(8)(A)(ii) is "not a 'catch-all' provision designed to encompass *any* educational claim arising out of *any* transaction that bestows an educational benefit on a debtor." *Id.* at 20 (emphases added). Although the court noted that Congress added the "educational benefit" language into the Code in order to expand nondischargeabilty to nontraditional loans, the court permitted the debtor to discharge her private loan because her medical school did not fit the Code's requirements for an "eligible educational institution." *See id.* at 20-21.

90. *See* Paul B. Porvaznik, *Is Discharging Student Loan Debt in Bankruptcy Getting Easier?*, 102 ILL. B.J. 540, 540-41 (2014) (expressing high threshold of proving undue hardship). Porvaznik notes that the "popular narrative on discharging student loans in bankruptcy . . . [is] dogmatic: 'Student loans can only be discharged in the most extreme situations—don't bother unless you meet the ultra-high burden. And you don't.'" *Id.*

91. *See* Betsy Mayotte, *Debunking the Student Loan Bankruptcy Myth*, U.S. NEWS & WORLD REP. (Aug. 13, 2014), http://www.usnews.com/education/blogs/student-loan-ranger/2014/08/13/debunking-the-student-loan-bankruptcy-myth [https://perma.cc/6DAG-BJT7] (considering discharging student loans "incredibly difficult—but not completely impossible" if undue hardship requirements met).

92. *See, e.g.*, United Student Aid Funds, Inc. v. Espinosa, 559 U.S. 260, 274 (2010) (noting Code's self-executing power to determine undue hardship); Grogan v. Garner, 498 U.S. 279, 287 (1991) (suggesting preponderance of evidence standard for warranting undue hardship discharge); Conway v. Nat'l Collegiate Trust (*In re* Conway), 559 Fed. App'x 610, 610 (8th Cir. 2014) (granting loan discharge after finding undue hardship); *see also* U.S. Dep't of Educ., Office of Postsecondary Educ., Opinion Letter on Undue Hardship Discharge of Title IV Loans in Bankruptcy Adversary Proceedings 14-15 (July 7, 2015), https://ifap.ed.gov/ dpcletters/attachments/GEN1513.pdf [https://perma.cc/HP2B-UARH] [hereinafter DOE Letter] (noting *Grogan v. Garner* preponderance of evidence standard extends to discharge for undue hardship).

93. *See* DOE Letter, *supra* note 92, at 3 (articulating courts use Brunner test and TCT to test hardship because Code leaves standard undefined).

undue hardship.[94] Nine circuits now apply the Brunner test to determine whether student loan debtors face undue hardship.[95] For a court to find undue hardship under the Brunner test, the debtor must show that: "(1) [they] cannot maintain, based on current income and expenses, a 'minimal' [living standard] for [themselves] and [their] dependents if forced to repay the loans; (2) . . . additional circumstances . . . indicat[e] . . . this [financial] state . . . is likely to persist for [most] of the repayment period . . . ; and (3) [they have] made good faith [repayment] efforts . . . ."[96]

Circumstances where courts have found an inability to maintain minimal living standards include frequently living below the poverty line and living with parents while unemployed or receiving only Social Security benefits.[97] Courts have found situations indicating the likely persistence of dismal financial affairs where debtors suffer serious medical conditions that complicate employment preservation, as well as extreme circumstantial changes precluding debtors from re-entering their previous careers.[98] Finally, courts have acknowledged good faith efforts to repay student loans where debtors maximize their endeavors to obtain employment.[99] Participating in Income-Contingent Repayment Programs (ICRPs) may also constitute a good faith effort to repay loans.[100] Although the Brunner test is widely adopted,

94. *See* Brunner v. N.Y. State Higher Educ. Servs. Corp., 831 F.2d 395, 396 (2d Cir. 1987) (articulating Brunner test for finding undue hardship); DOE Letter, *supra* note 92, at 16 (recounting Second Circuit first articulated Brunner test).

95. *See* Hedlund v. Educ. Res. Inst. Inc., 718 F.3d 848, 851 (9th Cir. 2013); Educ. Credit Mgmt. Corp. v. Frushour (*In re* Frushour), 433 F.3d 393, 400 (4th Cir. 2005); Oyler v. Educ. Credit Mgmt. Corp. (*In re Oyler*), 397 F.3d 382, 385 (6th Cir. 2005); Educ. Credit Mgmt. Corp. v. Polleys, 356 F.3d 1302, 1309 (10th Cir. 2004); U.S. Dep't of Educ. v. Gerhardt (*In re* Gerhardt), 348 F.3d 89, 91 (5th Cir. 2003); Hemar Ins. Corp. of Am. v. Cox (*In re* Cox), 338 F.3d 1238, 1241 (11th Cir. 2003); Pa. Higher Educ. Assistance Agency v. Faish (*In re* Faish), 72 F.3d 298, 306 (3d Cir. 1995); *In re* Roberson, 999 F.2d 1132, 1135 (7th Cir. 1993); *Brunner*, 831 F.2d at 396.

96. *Brunner*, 831 F.2d at 396 (listing Brunner test requirements).

97. *See* Traversa v. Educ. Credit Mgmt. Corp. (*In re* Traversa), 444 Fed. App'x. 472, 474 (2d Cir. 2011) (finding unemployed debtor receiving Social Security benefits living with parents satisfies first Brunner test prong); Educ. Credit Mgmt. Corp. v. Mosley (*In re* Mosley), 494 F.3d 1320, 1325 (11th Cir. 2007) (holding regularly living below poverty line satisfies first Brunner test prong); *see also* DOE Letter, *supra* note 92, at 17 (summarizing case law regarding first Brunner test prong). Although the first prong does not require outright poverty, it "requires more than a showing of tight finances" and not "merely [that] repayment . . . would require some major personal and financial sacrifices." *Faish*, 72 F.3d at 306.

98. *See Mosley*, 494 F.3d at 1326 (finding chronic depression and back issues satisfy second Brunner test prong); U.S. Dept. of Educ. v. Al-Riyami, 2014 WL 1584481, at *3 (M.D. Ala. Apr. 21, 2014) (opining forced overseas deployment away from children constitutes extreme life event, satisfying second test prong); *see also* DOE Letter, *supra* note 92, at 17 (summarizing case law regarding second Brunner test prong).

99. *See Mosley*, 494 F.3d at 1327 (concluding consistently seeking employment satisfies third Brunner test prong); *see also* DOE Letter, *supra* note 92, at 17-18 (summarizing case law on final Brunner test prong).

100. *See* Educ. Credit Mgmt. Corp. v. Mason (*In re* Mason), 464 F.3d 878, 884-85 (9th Cir. 2006) (showing ICRP participation constitutes good faith factor for third Brunner test prong); *cf.* Terrence L. Michael & Janie M. Phelps, *"Judges?!—We Don't Need No Stinking Judges!!!": The Discharge of Student Loans in Bankruptcy Cases and the Income Contingent Repayment Plan*, 38 TEX. TECH L. REV. 73, 89 (2005) (cautioning over-relying on ICRPs may lead to default "rule against dischargeability").

nonadopting circuits criticize the Brunner test for too strictly requiring debtors to satisfy all three prongs, which diminishes the Code's inherent discharge discretion.[101]

### *3. Totality of the Circumstances Test*

More recently, in 2003, the Eighth Circuit coined the TCT as a more flexible test for finding undue hardship.[102] Although the Eighth Circuit is the only circuit to rely on the TCT definitively, the First Circuit has employed the TCT in past cases concerning student loan debtors.[103] The TCT examines "(1) the debtor's past, present and . . . future financial resources; (2) [their] . . . reasonab[ly] necessary living expenses; and (3) any other relevant facts and circumstances."[104]

Under the TCT, courts consider debtors' lack of liquid assets and inability to maintain consistent employment.[105] Other relevant factors and circumstances include a debtor's mental and physical health, as well as dependents.[106] Courts have characterized the TCT as more flexible and equitable than the Brunner test because it considers all of a debtor's financial circumstances in unison rather than demanding debtors fulfill rigid prongs.[107]

### *4. Courts May Signal That Undue Hardship Is Becoming Easier to Establish*

Despite the traditional difficulty in proving undue hardship, debtors may have an easier time meeting this threshold in the future.[108] The very birth of the

101. *See* Long v. Educ. Credit Mgmt. Corp. (*In re* Long), 322 F.3d 549, 554 (8th Cir. 2003) (criticizing Brunner test for excessive strictness and adopting TCT); Kopf v. U.S. Dep't of Educ. (*In re* Kopf), 245 B.R. 731, 741 (Bankr. D. Me. 2000) (disagreeing with Brunner test for "test[ing] too much"); Michael & Phelps, *supra* note 100, at 91 (explaining critics find Brunner test too strict and overemphasize factors).

102. *See Long*, 322 F.3d at 554 (defining TCT).

103. *See* Bronsdon v. Educ. Credit Mgmt. Corp. (*In re* Bronsdon), 435 B.R. 791, 804 (1st Cir. 2010) (relying on TCT to determine undue hardship); *Kopf*, 245 B.R. at 741 (using TCT in undue hardship analysis). While the First Circuit has relied on the TCT in the past, it has refused to definitively adopt either the Brunner test or the TCT exclusively. *See* Nash v. Conn. Student Loan Found. (*In re* Nash), 446 F.3d 188, 190 (1st Cir. 2006) (declining to exclusively adopt either test).

104. *Long*, 322 F.3d at 554.

105. *See* Pollard v. Superior Cmty. Credit Union (*In re* Pollard), 306 B.R. 637, 649-50 (Bankr. D. Minn. 2004) (demonstrating court considered debtor's lack of liquid assets under TCT analysis); Strand v. Sallie Mae Servicing Corp. (*In re* Strand), 298 B.R. 367, 374 (Bankr. D. Minn. 2003) (adding courts consider debtors' inability to maintain employment under TCT); *see also* DOE Letter, *supra* note 92, at 19 (summarizing case law regarding courts' TCT considerations).

106. *See* Educ. Credit Mgmt. Corp. v. Jesperson, 571 F.3d 775, 780 (8th Cir. 2009) (considering debtor's young age and good physical health in TCT analysis); Reynolds v. Pa. Higher Educ. Assistance Agency (*In re* Reynolds), 425 F.3d 526, 533-34 (8th Cir. 2005) (suggesting courts consider debtors' mental health under TCT); *see also* DOE Letter, *supra* note 92, at 20 (summarizing case law regarding courts' TCT considerations).

107. *See* Long v. Educ. Credit Mgmt. Corp. (*In re* Long), 322 F.3d 549, 554 (8th Cir. 2003) (stressing importance of considering all relevant factors in finding undue hardship); DOE letter, *supra* note 92, at 19 (describing TCT's superior flexibility to Brunner test).

108. *See* Porvaznik, *supra* note 90, at 541, 544 (questioning whether debtor today can more easily

TCT demonstrates courts' willingness to employ more equitable and relaxed undue hardship analyses.[109] Additionally, a recent empirical assessment found that forty percent of unemployed debtors were able to discharge *all* loan debt.[110] Furthermore, some have interpreted the DOE Letter itself as giving students a ray of hope.[111]

## III. ANALYSIS

### *A. Human Capital Contracts Constitute Unsecured Bankruptcy Claims*

Like student loans, HCCs must fall within the Code's purview to facilitate widespread implementation.[112] Importantly, investors' contracts with investees should afford the investor the right to be paid on the HCC, which would call for enforcing HCCs' presumably valid contractual terms.[113] Honoring HCCs' validity is fundamental to protecting investors.[114] Indeed, courts may only construe HCCs as bona fide bankruptcy claims if the contracts are "enforceable outside of bankruptcy."[115]

HCCs should constitute claims in bankruptcy that entitle investors to a "right to payment" on a student's debt, which would be the the agreed-upon portion of the student's future income.[116] Professor Baker notes that HCCs fall within the Code's contemplation of a claim because an HCC "clearly represents an obligation by the student to an investor who presumably has a right to payment."[117] Professor Triantis definitively classifies HCCs as claims in bankruptcy, stating that "[t]he *claim* under [an HCC] on income already earned

discharge student debt than in past). Porvaznik discusses a trend toward partial discharge, which may define future bankruptcies. *See id*. at 544.

109. *See* Cope, *supra* note 88 (predicting other circuits may adopt TCT and "start to relax" undue hardship analyses).

110. *See* Jason Iuliano, *An Empirical Assessment of Student Loan Discharges and the Undue Hardship Standard*, 86 AM. BANKR. L.J. 495, 518 (2012) (finding forty percent of unemployed debtors received full student loan discharge); Mayotte, *supra* note 91 (relying on Iuliano's study to argue Code permits student loan dischargeability in some instances).

111. *See* Steve Rhode, *Department of Education Reaches Decision About Student Loans and Bankruptcy*, HUFFINGTON POST (July 9, 2015), http://www.huffingtonpost.com/steve-rhode/department-of-education-r_1_b_7753076.html [https://perma.cc/F5FF-FGK2] (interpreting DOE Letter to "give[] some hope" to student debtors).

112. *See supra* notes 11, 48-49 and accompanying text (urging need for HCC bankruptcy regulation to aid in HCC implementation).

113. *See* Baker, *supra* note 11, at 84 (noting courts will only enforce valid contracts); *see also supra* note 61 (describing typical differences between claims and equity interests); *infra* notes 120-121 (justifying HCC claim treatment to promote greater HCC utilization).

114. *See* Palacios, *supra* note 7, at 8-9 (emphasizing importance of HCC validity to investor protection).

115. *See* Baker, *supra* note 11, at 84.

116. *See* 11 U.S.C. § 101(5) (2012) (offering "claim" definitions); *see also supra* text accompanying notes 35-36 (describing various future income percentages students have pledged to investors in HCCs).

117. *See* Baker, *supra* note 11, at 84 (proclaiming HCCs likely fall within 11 U.S.C. § 523 (a)(8)).

by the student is a simple debt and easily enforced by the courts."[118] An investor's right to payment should reflect the percentage the student pledged to repay over the contracted time period.[119]

Similar to student loan debts—unless an investor somehow secured a lien on a student's future income—HCC claims would likely constitute unsecured claims that would entitle investors to a higher payment priority status than if the Code considered HCCs equity interests.[120] The Code should not construe HCCs as equity interests because it is unlikely that Congress contemplated that creditors would be able to maintain equity interests in natural debtors.[121] Classifying HCCs as claims rather than equity interests in humans further bolsters the argument that HCCs do not represent a form of slavery over an individual.[122] Furthermore, assuming courts and the Code similarly categorize HCCs and student loans in bankruptcy, the student loan exception to discharge does not encompass equity interests.[123] Therefore, courts would likely consider HCCs claims under the Code, entitling creditors to payment on a debt rather than maintaining an equity interest in the debtor as a natural person.[124]

To receive priority on payment of their claims, an HCC investor would need to argue his or her HCC claim is secured by a prepetition lien.[125] Although establishing a security interest in a debtor's future income may be challenging because a creditor cannot easily "take possession of . . .collateral[,]" consensual liens have the capacity to cover both tangible and intangible personal property.[126] Baker notes that even if an investor holds a lien against a student's

118. Triantis, *supra* note 76, at 94 (emphasis added). While Professor Triantis classifies a student's prepetition earnings as bankruptcy claims, he notes that enforcing future contractual terms is a more difficult question. *See id.*; *see also supra* note 76 (presenting challenges to enforcing HCCs' nonfinancial terms like mandating work performance).

119. *See supra* note 23 and accompanying text (describing fundamental HCC contractual framework).

120. *See In re* Chambers, 348 F.3d 650, 652 (7th Cir. 2009) (construing student loan debt in terms of "unsecured claim[s]"); Baker, *supra* note 11, at 83 (delineating bankruptcy claimants' payment priority statuses, demonstrating equity holders paid last).

121. *See* Baker, *supra* note 11, at 84 (arguing Code does not suggest creditors possess equity interests in natural human debtors); *see also* Leff & Hughes, *supra* note 10, at 127 (suggesting derivative-like IBR Swaps do not constitute "equity investment[s] in . . . human being[s]"). Although Leff and Hughes assert IBR Swaps do not constitute equity interests, whether HCCs constitute equity interests remains unresolved. *See id.*

122. *See supra* note 53 and accompanying text (addressing, but rejecting, argument suggesting HCCs contravene Thirteenth Amendment).

123. *See* Baker, *supra* note 11, at 85 (arguing HCCs should constitute claims because student loan exception fails to cover equity interests).

124. *See id*. (predicting Code should consider HCC claims because Code does not contemplate interests in natural debtors).

125. *See id*. (discussing HCC creditors' projected higher payment status if they have secured claims); *see also* Leff & Hughes, *supra* note 10, at 137 (raising claim priority concerns in context of bankruptcy HCC debtors).

126. *See* HOWARD, *supra* note 13, at 5-6 (describing consensual liens and Uniform Commercial Code Article 9 remedy of "self-help repossession"); *see also* Baker, *supra* note 11, at 83, 85 (refusing to preclude possibility HCC investors have capacity to hold liens). Professor Baker argues, however, that any lien an investor holds against an HCC should be a secured claim, entitling the investor to a higher priority status in

future income, he or she should not expect that the lien would extend to income earned postbankruptcy.[127] Therefore, like student loan debt, courts would likely categorize the vast majority of HCCs as unsecured interests.[128]

### *B. Courts Must Except Human Capital Contracts from Discharge Under 11 U.S.C. § 523(a)(8)*

To protect HCC investors' unsecured bankruptcy claims and to foster HCC proliferation, HCCs should fall within § 523(a)(8)'s student loan exception to discharge.[129] Assuming HCCs constitute unsecured bankruptcy claims, they are likely dischargeable unless they qualify for a statutory exception.[130] Without establishing a secured claim, HCC investors may see little to no repayment in most consumer chapter 7 bankruptcies.[131] To foster investor protection, accredited investors advancing HCC funds "should receive at least the same [bankruptcy] protection that student loan lenders receive today."[132] Consequently, to protect investors' rights and encourage widespread HCC utilization, § 523(a)(8) must apply to HCCs.[133]

A plain reading of the Code supports the notion that HCCs fall within the student loan exception to discharge under § 523(a)(8).[134] Although courts frequently include governmental and nonprofit loans within § 523(a)(8)'s scope, the Code's limits will remain uncertain until the HCC and private student loan markets operate more frequently and expansively.[135] Notwithstanding the modest scale on which HCCs and other private loans operate, HCCs fall within § 523(a)(8)(A)(ii)'s plain language excepting from

bankruptcy. *See* Baker, *supra* note 11, at 83. *But cf*. *infra* note 128 and accompanying text (citing case precedent definitively construing student loan debts unsecured).

127. *See* Baker, *supra* note 11, at 86 (expressing practical difficultly of retaining liens on postbankruptcy income because of fresh start).

128. *See* Educ. Credit Mgmt. Corp. v. Mason (*In re* Mason), 464 F.3d 878, 881 (9th Cir. 2006) (considering student loan debts, "unsecured, nonpriority claims"); *In re* Chambers, 348 F.3d 650, 652 (7th Cir. 2003) (construing student loan debt in terms of "unsecured claim[s]").

129. *See* Baker, *supra* note 11, at 87 (addressing possibility HCCs could satisfy discharge exception to protect investors); Groshoff et al., *supra* note 10, at 318 (predicting debtors could not discharge HCCs in bankruptcy). *But see* Dynarski & Kreisman, *supra* note 8, at 30 (proclaiming "private student loans should not survive bankruptcy").

130. *See* Baker, *supra* note 11, at 87 (noting while bankruptcy generally discharges claims, ambiguity surrounds whether HCCs qualify for discharge exceptions).

131. *See id*. at 86 (predicting HCC investor creditors will not receive substantial payments).

132. *See* Palacios, *supra* note 7, at 9.

133. *See* Baker, *supra* note 11, at 87 (noting "one thin ray of hope for the investor" would entail exception to discharge); Leff & Hughes, *supra* note 10, at 138 (suggesting investors face heightened risks early in HCC agreements when investees may under-earn); Palacios, *supra* note 7, at 8-9 (urging bankruptcy reform to protect investors).

134. *See* Baker, *supra* note 11, at 87 (describing mechanism through which HCCs satisfy discharge exception); *supra* note 13 and accompanying text (describing Code's statutory student loan exemption construction).

135. *See* Baker, *supra* note 11, at 87 (acknowledging Code's limits remain unknown if "private market for educational financing" remains underutilized).

discharge "an[y] obligation to repay *funds received as an educational benefit*."[136] Because HCCs offer students substantial "educational benefits," including more flexible repayment schemes based on students' actual incomes, the Code's language plainly excepts HCCs from discharge.[137] Courts frequently interpret the Code according to its plain meaning.[138] Because HCCs establish "educational benefit[s]" under the Code, a plain reading demands their inclusion as an exception to discharge.[139]

Previous treatment of HCC default also supports the notion that they should fall within the student loan exception to discharge.[140] Specifically, although students are not required to repay investors if they are not earning any income, HCCs will be strictly enforced if a defaulting student possesses the financial means to repay his or her loans and fails to do so.[141] In such cases, the student may face interest rates of up to fifteen percent, similar to high student loan interest rates.[142] The analogous treatment between HCC and student loan default supports their related bankruptcy treatment.[143]

Judicial precedent further demonstrates that including HCCs within the student loan exception to discharge is necessary for investor protection.[144] Since Congress adopted the Bankruptcy Act of 1898, courts have generally protected human capital by discharging a debtor's obligation to pay future income to creditors.[145] To safeguard HCC investors and combat overprotecting

136. 11 U.S.C. § 523(a)(8)(A)(ii) (2012) (emphasis added); *see also* Baker, *supra* note 11, at 87 (suggesting HCCs fall within Code's plain language discharge exception); Groshoff et al., *supra* note 10, at 318 (presupposing HCCs exempted from discharge because they constitute "educational benefit" under Code); *supra* note 67 and accompanying text.

137. *See* Baker, *supra* note 11, at 87 (suggesting HCCs comport with Code's plain meaning); *supra* notes 9, 41-42 and accompanying text (describing HCC advantages over traditional loans). *Cf.* Decena v. Citizens Bank (*In re* Decena), 549 B.R. 11, 20 (Bankr. E.D.N.Y. 2016) (noting "educational benefit" discharge exception does not "catch-all" conceivable forms of such benefits).

138. *See* Baker, *supra* note 11, at 87 (arguing courts interpret HCCs' plain meaning in concert with Code); Bussel, *supra* note 68, at 909 (acknowledging Supreme Court's "insistence for a decade on 'plain meaning'" Code interpretation).

139. *See supra* note 137 and accompanying text (describing how HCCs constitute "educational benefits," comporting with Code). *Cf.* Baker, *supra* note 11, at 87 (questioning whether HCCs fit within student loan discharge exception). Professor Baker notes that although HCCs provide educational benefits, "it is not so obvious that a court would determine" HCCs immediately fall within the student loan exception to discharge. Baker, *supra* note 11, at 87.

140. *See supra* notes 44-45 and accompanying text (discussing similarities between HCC default and student loan default).

141. *See* Sullivan, *supra* note 43 (explaining HCC nonpayment ramifications); *supra* notes 44-45 and accompanying text (proscribing HCC delinquency consequences).

142. *See* Sullivan, *supra* note 43; *supra* note 44.

143. *See supra* notes 44-45 and accompanying text (concluding HCC and traditional loan delinquency parallels invite similar bankruptcy treatment).

144. *See* Chapman, *supra* note 74, at 100 (describing courts' long held policy "to protect a debtor's future income from creditors"); Jackson, *supra* note 69, at 1432-33 (noting bankruptcy law has traditionally protected human capital debt discharge, especially for younger debtors).

145. *See* Chapman, *supra* note 74, at 100 (tracking policy protecting debtor's future income); *see also* Local Loan Co. v. Hunt, 292 U.S. 234, 245 (1934) (discharging debtor's obligation to repay debt with future

a debtor's future income that he or she voluntarily contracted to pay, HCCs must fall within the student loan exception to discharge.[146] Subjecting HCCs to an exception to discharge is especially appropriate where "the individual incurred [the student loan debt] in order to acquire that human capital."[147]

### *C. If a Human Capital Contract Debtor Can Demonstrate "Undue Hardship" Based on the Totality of the Circumstances, Courts Should Discharge Future Repayment Obligations*

Although investor protection is critical to facilitating HCC utilization, courts must afford HCC student debtors the opportunity to discharge their HCC obligations if they can demonstrate that repaying investors would present an undue hardship.[148] HCC structure mandates that in exchange for financial backing, students pledge a percent of their incomes for a number of years.[149] If a student files for bankruptcy and ceases working, he or she would generate no income, and therefore, would not be required to pay any installments on his or her HCC.[150] When the student resumes working, however, the same contractual income percentage owed on the HCC would naturally revive, and at this time, a previously bankrupt debtor whose HCC was statutorily excepted from discharge should have the opportunity to demonstrate that repaying the percentage of his or her income imposes undue hardship.[151]

Similar to traditional student loan debtors, HCC debtors should have the chance to establish undue hardship given the Code's language and fresh start policy.[152] Assuming HCCs are included in the student loan exception to discharge because they constitute an "educational benefit," this debt categorization remains anchored to the Code's introductory prerequisite of being subject to undue hardship.[153] Therefore, the Code plainly instructs that if

income); *supra* note 79 and accompanying text (describing past HCC-like discharge).

146. *See* Chapman, *supra* note 74, at 100 (acknowledging student loan discharge exception contravenes general bankruptcy policy of protecting future income debts); Jackson, *supra* note 69, at 1432 (noting protecting human capital in bankruptcy remains "subject to" student loan debts).

147. Jackson, *supra* note 69, at 1432.

148. *See id*. at 1395 (describing need to balance creditors' rights to payment and debtors' rights to fresh start). Although protecting investors is crucial to implementing HCCs, courts must also consider protecting students' rights through private loans. *See* Dynarski & Kreisman, *supra* note 8, at 22.

149. *See supra* note 23 and accompanying text (outlining HCC financial structure).

150. *See* Sullivan, *supra* note 43 (alluding to how HCCs would not require payments if students' incomes dropped below certain threshold).

151. *See supra* note 91 and accompanying text (describing undue hardship in terms of limited exception to student loan nondischargeabilty).

152. *See supra* note 79 and accompanying text (describing policy underlying bankruptcy fresh start, especially for human capital debts).

153. *See* 11 U.S.C. § 523(a)(8)(A)(ii) (2012) (subjecting discharge to undue hardship language). The statute reads: "A discharge under . . . this title does not discharge an individual debtor from any debt . . . *unless* excepting such debt from discharge under this paragraph *would impose an undue hardship on the debtor and the debtor's dependents* . . . ." *Id.* (emphasis added).

courts construe HCCs as "educational benefits," they are necessarily excepted from discharge *unless* a debtor can prove undue hardship.[154]

Furthermore, while student loans are statutorily denied discharge, permitting student debtors to discharge HCCs when faced with undue hardship affords "honest but unfortunate debtor[s]" a fresh start.[155] Likewise, HCC debtors who resume employment following bankruptcy, thereby triggering repayment on their HCC, should have the opportunity to demonstrate undue hardship if repayment would impede achieving a fresh start.[156] For instance, Upstart's threshold earning amount to trigger borrowers' HCC repayment obligations was a mere $30,000.[157] Therefore, as soon as a borrower earned $30,000 annually, his or her contractual obligations—no matter how large—would begin again.[158] Conceivably, paying up to seven percent of $30,000 annually could present a significant undue hardship to the debtor.[159] Affording HCC debtors the opportunity to demonstrate undue hardship is also supported by the general contention that undue hardship may be getting easier for debtors to prove.[160]

The TCT is the standard courts should use to determine undue hardship for HCC debtors because of its flexibility and HCCs' multi-faceted nature.[161] While the Brunner test is more widely adopted, its restrictive form hampers courts' discretion to consider all the factual circumstances surrounding a debtor's bankruptcy.[162] Because HCCs are projected to become popular financing options, employing a strict and rigid undue hardship analysis under the Brunner test would impede the court's ability to interpret the Code at a time

154. *See id.* (demonstrating plain Code reading attaches "undue hardship" language to "educational benefit" language).

155. *See* Grogan v. Garner, 498 U.S. 279, 287 (1991) (demonstrating Code's long-standing commitment to fresh start for debtors); Lux, *supra* note 14 (explaining opportunity to prove undue hardship affords student loan debtors fresh starts).

156. *See supra* notes 2-3 and accompanying text (emphasizing young people's consciousness that higher education yields financial security). This awareness suggests HCC debtors will seek employment to combat financial challenges brought on by bankruptcy, which will trigger the HCCs' terms. *See* Sullivan, *supra* note 43 (describing general HCC structure of borrower committing percentage of future incomes to investors). If a borrower earns no income, he or she will not owe any payments, although they may face a loan extension period. *See id.*; *supra* note 44 and accompanying text (detailing HCC delinquency consequences). Likewise, when he or she does earn income over the minimum threshold amount, HCC obligations will resume. *See* Sullivan, *supra* note 43.

157. *See* Sullivan, *supra* note 43 (describing Upstart's minimum earning threshold to require HCC repayment for borrowers).

158. *See id.*

159. *See* Oei & Ring 2015, *supra* note 10, at 690-91 (providing maximum percentages Upstart investors could recover on HCC contracts).

160. *See supra* Part II.C.4.

161. *See supra* note 107 and accompanying text (discussing TCT advantages over Brunner test, emphasizing flexibility).

162. *See supra* note 101 and accompanying text (expressing dissatisfaction with Brunner test for excessively rigid nature).

when courts will need flexibility to solidify HCC bankruptcy treatment.[163] Additionally, as more and more courts relax their undue hardship analyses, the TCT could conceivably replace the Brunner test as the preferred undue hardship analysis.[164]

When employing the TCT to determine undue hardship, courts consider all "relevant facts and circumstances."[165] Because HCCs operate by considering students' numerous credentials before determining how much money he or she will receive and how much return capital will be paid, TCT analyses should afford debtors a similarly thorough consideration.[166] For instance, "[e]valuating the market price of an education . . . undoubtedly raise[s] sociopolitical and socioeconomic objections."[167] Therefore, courts should employ the TCT to consider such circumstances in undue hardship analyses.[168]

Key factors courts should consider in TCT analyses include an HCC debtor's age, pre-HCC socio-economic status, and dependents.[169] The debtor's age is an important circumstantial consideration because younger HCC debtors are more likely to regret financial decisions than older debtors.[170] Considering a debtor's pre-HCC financial state is warranted under the TCT because students with the lowest incomes pursuing nonlucrative degrees typically receive the lowest funding in exchange for the highest future income percentage over the greatest number of years.[171] Inequitable funding distribution for financially disadvantaged students may present considerable undue hardship if they were

163. *See* Long v. Educ. Credit Mgmt. Corp. (*In re* Long), 322 F.3d 549, 554 (8th Cir. 2003) (adopting TCT to retain statutory prerogative in finding undue hardship). The Eighth Circuit Court of Appeals adopted the TCT over the Brunner test because "requiring . . . bankruptcy courts to adhere to the strict parameters of a particular test [diminishes] . . . inherent discretion contained in § 523(a)(8)(B)." *Id.* Because HCCs are "likely [to] become more common" in the future, the Code must retain such inherent discretion in construing undue hardship. *See* Surowiecki, *supra* note 9 (predicting greater HCC implementation in future); *supra* note 10 and accompanying text (forecasting HCCs' future proliferation).

164. *See* Cope, *supra* note 88 (suggesting more circuits may adopt TCT, relaxing their undue hardship analyses); *supra* notes 108-111 and accompanying text.

165. *See Long*, 322 F.3d at 554 (setting forth TCT examination requirements); *supra* text accompanying note 104 (describing flexible TCT considerations).

166. *See supra* note 55 and accompanying text (outlining investors' various considerations when deciding to invest in particular investees).

167. Kapadia, *supra* note 7, at 611-12.

168. *See supra* note 55 and accompanying text (describing factors HCC investors contemplate in student investees).

169. *See* Educ. Credit Mgmt. Corp. v. Jesperson, 571 F.3d 775, 780 (8th Cir. 2009) (considering debtor's dependents in TCT undue hardship analysis); Jackson, *supra* note 69, at 1433 (suggesting bankruptcy discharge treats young human capital debtors more favorably than older debtors); DOE Letter, *supra* note 92, at 20 (describing number of dependents as TCT factor); *supra* note 56 and accompanying text (noting wealthy students may gain more funding than students with fewer financial means).

170. *See* Jackson, *supra* note 69, at 1433 (suggesting younger human capital debtors may make regrettable decisions, invoking greater discharge protection).

171. *See supra* note 56-57 and accompanying text (describing disparate HCC treatment amongst students who anticipate entering low-paying careers).

forced to repay a high percentage of future income postbankruptcy.[172] Finally, courts should continue considering the number of an HCC debtor's dependents under the TCT per the Code's plain statutory language.[173]

## IV. CONCLUSION

In an era where traditional student loans have buried hundreds of thousands of students in immense debt, HCCs' projected proliferation could not be more timely. Owning a share in another's future, and allowing borrowers to treat themselves like corporations, represents the next step in higher education financing. With this progression comes a significant need for investor protection. Ultimately, however, courts cannot turn a blind eye to the Code's commitment to a fresh start for bankrupt HCC borrowers.

Although pervasive HCC utilization has faced many challenges, the greatest by far remains the lack of federal regulation safeguarding investors. Including HCCs within the Code's protective purview by qualifying them as claims in bankruptcy will allow for greater investor protection. Like student loans, investors' HCC bankruptcy claims should be excepted from typical discharge for further security.

Absolute HCC discharge exception, however, should not define these contracts' bankruptcy treatment. Mirroring the statutory requirements for student loans, HCC borrowers should have the opportunity to demonstrate that repaying HCC obligations would present an undue hardship under § 523(a)(8). The TCT is the proper test courts should employ in determining undue hardship because a strict Brunner test analysis hampers courts flexibility to establish HCC bankruptcy treatment.

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172. *See id*. (demonstrating low-earning students' greater inability to achieve favorable HCC structures); *supra* note 79 (explaining how undue hardship impedes some HCC debtors' fresh starts).

173. *See* 11 U.S.C. § 523(a)(8) (2012). The statute states that debtors may discharge student loan debts if loan repayment would present "undue hardship on the debtor and the debtor's dependents." *Id*.; *see also Jesperson*, 571 F.3d at 780 (including debtor's dependents in TCT analysis for student loan discharge).