

The Ethics of Seeking Student Loan Discharges under DOJ Guidance

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“You can’t discharge student loans in bankruptcy.” As bankruptcy professionals, we have all heard and repeated this refrain for years. Technically, of course, this was never exactly true. Section 523(a)(8) of the Bankruptcy Code has long provided for the discharge of student loans if the debtor could demonstrate “undue hardship.” Practically, however, discharging student loans proved nearly impossible, with fewer than 0.1% achieving discharge.¹ As such, advising debtors that their student loans were not dischargeable was sound and accurate advice consistent with a bankruptcy attorney’s ethical obligations.

On Nov. 17, 2022, the Department of Justice (“DOJ”) and Department of Education (“DOE”) announced new guidance (“Guidance”) for discharging federal student loans in bankruptcy. The Guidance provides a streamlined and objective approach. Instead of guessing what “undue hardship” means and how to prove it, the Guidance clearly outlines how the standard will be reviewed and applied. Instead of spending countless hours and dollars in discovery and litigation, the Guidance offers an attestation form that the DOJ and DOE use to evaluate if a debtor meets the standard.

Industry experts estimate that up to 75% of cases seeking discharge under the Guidance succeed.²



The Guidance has completely shifted the landscape. What once was rare and hopeless is now proving to be attainable and life-changing for many debtors. This raises the question: What impact does the Guidance have on the debtor attorney's ethical obligations to review and represent the debtor on the dischargeability of their student loans?

At the core of this discussion are two sub-issues: (1) what a debtor attorney must tell their client and (2) what the debtor attorney must do in the course of their representation.

The Model Rules of Professional Conduct ("Rules") make it clear that the basic role of a lawyer is to provide clients "with an informed understanding of [their] legal rights and obligations and [explain] their practical implications."³ In doing so, attorneys must provide "competent representation" (Rule 1.1), "act with diligence and promptness" (Rule 1.3) and consult with and keep the client properly informed (Rule 1.4).

At a minimum, attorneys now have an obligation to notify their clients—past and present—that they may now have a realistic path to discharging their federal student loans. After all, student debt is the second largest consumer debt and has a tremendous impact on the financial well-being of a debtor. Numerous studies show that student debt significantly influences debtors' life decisions.⁴ It is our informed assessment, based on the Guidance, that attorneys now have an obligation to at least alert their clients to the possibility that these loans may now be dischargeable under the Guidance.

That said, Rule 1.2(c) clearly allows attorneys to "limit the scope of the representation if the limitation is reasonable under the circumstances and the client gives informed consent." Given that the Guidance requires the filing of an adversary proceeding, a process with which attorneys may not be familiar or comfortable, and which is beyond the scope of most standard representation arrangements, attorneys should not be obligated to prosecute the adversary proceeding on behalf of the client

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in the ordinary course of their bankruptcy representation. But, as Rule 1.2(c) also makes clear, the client must give "informed consent". Rule 1.0 explains that "informed consent denotes the agreement by a person to a proposed course of conduct *after the lawyer has communicated adequate information and explanation* about the material risks of and reasonably available alternatives to the proposed course of conduct." (emphasis added). Thus, even if the attorney does not elect to represent the client in the discharge adversary proceeding, the ethics rules make clear that attorneys must communicate to the debtor that they have the option of doing so.

The DOJ Guidance on discharging student loans is groundbreaking, making what was once nearly impossible now very realistic. With the Guidance in place, attorneys can no longer simply tell clients that "student loans are not dischargeable in bankruptcy." While lawyers are not required to file an adversary proceeding to seek the discharge, they should advise their clients that discharge is now possible and explain the process. If their clients wish to proceed, attorneys should be prepared to handle the matter, co-counsel or refer it to another attorney for prosecution. ■

FOOTNOTES

1. Jason Iuliano, *The Student Loan Bankruptcy Gap*, 70 Duke L.J. 497-543 (2020)
Available at: <https://scholarship.law.duke.edu/dlj/vol70/iss3/>
2. NACBA 2024 Conference.
3. Model Rules of Professional Conduct: Preamble & Scope
4. <https://www.nyc.gov/site/dca/news/046-21/student-loans-negatively-affect-life-decisions-half-new-york-city-borrowers#:~:text=Effect%20on%20Major%20Life%20Choices&text=About%2033%20percent%20indicated%20they,prevented%20from%20starting%20a%20business>

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What do you think of the ethical requirement? Email Igor Roitburg at Igor.Roitburg@stretto.com with your comments.

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