



INTERNATIONAL ASSOCIATION OF INSOLVENCY
REGULATORS

REPORT ON
TREATMENT OF
STUDENT LOANS IN
BANKRUPTCY

Introduction.....	4
Background.....	4
Key points to note.....	5
Country reports.....	6
Australia.....	6
British Virgin Islands.....	7
Canada.....	8
Finland.....	13
Hungary.....	14
Ireland.....	15
Jersey.....	16
Latvia.....	17
Malaysia.....	17
Mexico.....	19
New Zealand.....	19
Northern Ireland.....	22
Singapore.....	23
Thailand.....	24
United Kingdom.....	24
United States of America.....	26
Appendix A.....	29

Introduction

1. The International Association of Insolvency Regulators (IAIR) agreed at its 2005 annual meeting in Helsinki, Finland to commission a report on the treatment of student loans in bankruptcy.
2. This report is based on information provided by 17 countries which are either members of IAIR or have participated as observers. This information was obtained using a questionnaire (see Appendix A). The following countries responded to the survey:

Australia
British Virgin Islands
Canada
Finland
Hungary
Ireland
Jersey
Latvia
Malaysia
Mexico
New Zealand
Northern Ireland
Singapore
South Africa
Thailand
United Kingdom
USA

3. A number of countries do not operate personal insolvency systems and would not have responded on the basis that student loans are only an issue in personal insolvency.

Background

4. Many countries have in place a system providing for loans to students to allow them to undertake university education. These loans may be provided by the Government or by a private sector lender. The student usually becomes liable to repay the loan once they are employed. In some cases, the repayments commence only after the student is earning above a minimum threshold income.
5. If the student becomes bankrupt and has not paid off the student loan, how is that debt treated in the bankruptcy? This is becoming a significant issue for some countries as the amount of debt owed by former students has increased substantially. If the debt is completely or automatically discharged in bankruptcy, this increases the cost of providing student loans, particularly in countries with high numbers of consumer bankruptcies.

6. This report seeks to bring together information on the following broad topics related to the treatment of student loans in bankruptcy:
 - the student loan systems operating in different jurisdictions;
 - rules applying to student loans in bankruptcy;
 - issues arising from these rules; and
 - areas of particular concern in individual jurisdictions.

Key points to note

7. The key observations to note about the way in which student loans are treated in bankruptcy across the jurisdictions which contributed to this report are:
 - in most countries, there have not been significant concerns about the way in which student loans are treated in bankruptcy;
 - there are student loans operating in many countries with a wide range of systems operating encompassing both Government and private funding;
 - student loans generally are of some public interest in many countries and this interest appears to have increased in recent years;
 - there are more likely to be concerns about how these loans are treated in bankruptcy where they are largely funded by the Government; and
 - the most common way of ensuring that former students cannot use bankruptcy as means of avoiding repayment of student loans is to provide that the debts are not provable (and hence not discharged) in bankruptcy.

Country reports

Australia

Student loan system

8. The Australian Government provides financial assistance to students under various schemes such as the HECS-HELP scheme for undergraduate students. Under this scheme, the Commonwealth makes a contribution to the student's tuition costs and effectively provides a loan to the student for the balance of the costs. The amount which the student must repay is linked to the type of course undertaken (for example, studies in medicine and law attract higher charges than arts courses). These 'student loans' cover only tuition costs and do not extend to living and other expenses. Further assistance for living expenses is available to students through the social security system – that assistance is means tested and is not repayable by the student.
9. There are similar schemes available for postgraduate students and for students who are offered a non-Commonwealth supported place (whereby the Government effectively loans an amount to the student to cover tuition costs).
10. The student accumulates a debt for each year of study. The amount of this accumulated debt is increased by indexation each year until it is repaid.
11. Students obtain a discount for making up-front payments of the HECS debt or for making lump sum payments after the debt begins to accumulate.
12. The student must commence repaying the accumulated debt upon earning income above a statutory threshold. The amount to be repaid is calculated each when the student lodges an income tax return and the payments are made to the Australian Taxation Office. The repayment threshold has been reduced significantly in recent years in response to concerns about the total amount owing to the Commonwealth under this scheme.
13. Some banks and other financial institutions also offer loans to students (often at a discounted interest rate) to assist them in meeting the costs of their studies.

Rules applying to student loans in bankruptcy

14. Since 1 January 2005, the accumulated debts owing by students under the HECS-HELP and similar schemes have not been provable in bankruptcy. As a result, they are not discharged by bankruptcy.
15. However, that part of the debt which has been assessed after the student lodges a tax return and has become payable is a provable debt. This assessed debt is treated in the same way as other unsecured debts and will be discharged.

16. Prior to 1 January 2005, the accumulated debt had the unusual status of being provable in the bankruptcy but not discharged. This meant the Commonwealth could prove in the bankruptcy and receive a dividend along with other unsecured creditors but then continue to assess and collect the debt following discharge from bankruptcy. The law was amended to remove this advantage to the Commonwealth.
17. The rules are the same in voluntary arrangements (debt agreements and personal insolvency agreements).
18. Loans advanced to students by private financial institutions are treated in the same way as other unsecured debts and will be discharged by bankruptcy.

Issues arising from current rules

19. There have occasionally been concerns that students may use bankruptcy to avoid repaying these loans. These concerns have not been widespread and come up in the context of the significant amount of these debts which remain unpaid. However, this would only ever have been the case in relation to that part of the debt which had become repayable because the former student lodged a tax return disclosing income above the threshold. The accumulated debt has never been discharged by bankruptcy. Since the 2005 amendments, students have little to gain from declaring bankruptcy as they are unlikely to avoid repaying most of the debt.
20. Generally, the level of Commonwealth funding for higher education is regularly debated, particularly by the major political parties.

British Virgin Islands

Student loan system

21. There is no formal student loans system. However, student loans are provided by some commercial banks on commercial terms and at commercial rates. These are frequently guaranteed by parents.
22. The BVI Government also offers government scholarships to support the cost of tertiary education (usually overseas). Recipients of scholarships are expected to return to the BVI and work in the public service for a period of time on completion of their studies. Failing this, the scholarships are, in principle, repayable. These are not in the nature of student loans and are ignored for the purposes of this report.
23. The costs covered by the loan and the repayment arrangements depend on the terms of the loan, but will commonly cover tuition fees and living expenses.

Rules applying to student loans in bankruptcy

24. Student loan debts are provable in bankruptcy. They are discharged automatically along with other unsecured debts at the end of three years unless

certain exceptions apply. They have the same priority as other unsecured debts.

25. The way in which student loans are treated in a voluntary arrangement will depend upon the terms of that arrangement.

Issues arising from current rules

26. There is no evidence that former students are using bankruptcy to avoid repaying student loans. However, bankruptcy proceedings are very rare in the British Virgin Islands. There are no specific features of the bankruptcy which would either encourage or discourage former students to use bankruptcy.
27. Student loans are not seen as a problem area at all and, hence, there are no proposals for reform. The government scholarships referred to earlier are also not considered to be a problem area.

Canada

Student loan system

28. Since 1964, the Government of Canada, through the Canada Student Loans Program (the “CSLP”) has been assisting students to access post-secondary education by providing loans and grants to eligible full- and part-time students with demonstrated financial need. The Government of Canada jointly administers the CSLP and other forms of student assistance with nine participating provinces and the Yukon Territory. It also provides alternative payments to Quebec, the Northwest Territories and Nunavut, who operate their own student financial assistance programs.
29. The *Canada Student Loans Act* and its regulations govern Canada Student Loans issued prior to August 1, 1995. The *Canada Student Financial Assistance Act* and its regulations govern Canada Student Loans issued on or after August 1, 1995.
30. Between 1964 and 1995, student loans were financed through private financial institutions to post-secondary students who were approved to receive financial assistance. The private financial institutions also administered the loan repayment process. In return, the Government of Canada guaranteed each Canada Student Loan that was issued by reimbursing the private financial institution the full amount of loans that went into default.
31. In 1995, the Government of Canada developed a formalized risk-shared agreement with several financial institutions, whereby the institution would assume responsibility for the possible risk of defaulted loans in return for a fixed payment from the Government.
32. On July 31, 2000, the risk-shared arrangement between the Government of Canada and participating financial institutions came to an end. As of August 1, 2000, loans are funded by the Government of Canada and administered

through the National Student Loans Service centre (the “NSLSC”). Students no longer need to go to a financial institution to negotiate a Canada Student Loan. When it is time to repay the loan, the student makes payments directly to the NSLSC.

33. The Canada Student Loans Program provides 60% of a full-time student’s assessed need to a maximum of \$210 per week of study as of August 1, 2005. In addition to a federal student loan, a student may also be eligible for a full-time student loan up to the provincial maximum from the province or territory in which the student lives.
34. While the student is enrolled in school full-time, the Government of Canada will pay the interest on the Canada Student Loan. The Canada Student Loan remains interest-free as long as the student confirms that he or she is enrolled full-time for each period of study.
35. Loans made to part-time students are not eligible for interest-free status, and the student must make interest payments while in school. However, if the student’s income is below a certain level while in school, he or she may qualify for Interest Relief.
36. Student may choose to make payments on the Canada Student Loan while still in full-time studies but are under no obligation to do so. Any payments made during this time will be applied directly to the principal.
37. When full-time students cease their studies, they enter the loan repayment stage. Canada Student Loans received before August 1, 2000, are repaid to the financial institution holding the loans. Canada Student Loans received on or after August 1, 2000, are repaid to the Government of Canada through the NSLSC.
38. Full-time students are entitled to a six-month grace period after leaving school before they must start making payments on their loans. (Part-time students are required to make interest payments throughout.) Interest accrues on the loan during the grace period. Within these six months, full-time students must contact the financial institution and/or the NSLSC to consolidate all loans and set up a repayment schedule. They sign a consolidation agreement that sets out the interest rate, the full amount of the loan, when the first payment is due, the number and frequency of payments, and the amount of each payment.

Rules applying to student loans in bankruptcy

39. Student loan debts are provable in bankruptcy. Proofs of claim may be filed for them, and the creditor can receive a dividend on them.
40. By way of amendments in 1998 to paragraph 178(1)(g) of the *Bankruptcy and Insolvency Act*, an order of discharge does not release the bankrupt from any debt or obligation in respect of a loan made under the *Canada Student Loans Act*, the *Canada Student Financial Assistance Act*, or any enactment of a province that provides for loans or guarantees of loans to students where the

date of bankruptcy of the bankrupt occurred (i) before the date on which the bankrupt ceased to be a full- or part-time student, or (ii) within 10 years after the date on which the bankrupt ceased to be a full- or part-time student. The 10-year period runs from the date of the termination of the student's studies, not from the date of bankruptcy.

41. In situations where the bankrupt has acted in good faith regarding the student loan liabilities and the bankrupt will continue to experience financial difficulties to an extent that he or she will be unable to pay the liabilities under the loan, the bankrupt may, at any time ten years after the bankrupt ceases to be a full- or part-time student, apply to the court for an order that section 178(1)(g) does not apply. This hardship application to the court may be made during the administration of the estate or, as is more likely, after the administration of the estate is complete. The obligation is on the student to bring the application and to demonstrate financial hardship.
42. These timeframes, however, are expected to be reduced. An omnibus bill to establish a *Wage Earner Protection Program Act* and to amend the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* has been passed by parliament but is not yet in force. This new legislation would reduce the waiting time for discharge from 10 years to 7 years after the date on which the bankrupt ceased to be a full- or part-time student, and would allow the student to make a hardship application to the court after 5 years.
43. Student loan debts rank among unsecured debts. However, they are not released by an order of discharge.
44. If a debtor were to include student loans in the terms of a voluntary arrangement or proposal with creditors, Human Resources and Skills Development Canada, the government department responsible for Canada Student Loans, would have the opportunity to determine whether the terms of the proposal are acceptable to it.
45. Prior to amendments to the *Bankruptcy and Insolvency Act* in 1992, federal and provincial government or Crown claims were preferred under section 136(1)(j). When a bankrupt owed a debt or obligation for a student loan, the Crown frequently objected to the discharge so that payments could be received on the preferred claim of the Crown.
46. In 1992, the government's preferred status in bankruptcy was removed, consistent with a broader trend in other jurisdictions to limit the priority status of the Crown. When this preference was taken away, however, the government claimed that it was experiencing significant losses as a result of its general unsecured position and the increasing number of students who were going bankrupt with unpaid government student loans. Thus, from 1992 to 1997, student loans were treated in the same manner as most other consumer debts. In general, student loans were discharged along with other debts provided that the trustee or creditor did not believe that the former students were abusing the insolvency system. In the latter case, they could oppose the

debtor's discharge from bankruptcy, or the creditors could refuse to accept the consumer proposal.

47. Based on the high costs to the taxpayers as a result of unpaid government student loans, in 1997, the bankruptcy legislation was further amended to change the treatment of student loan debt. These amendments were in conjunction with the debt relief measures that the government made available to student loan borrowers and provided part of the rationale for the amendments to the insolvency system. With these amendments, student loans were no longer discharged if debtors filed for bankruptcy within two years of leaving full- or part-time studies. For these debtors, section 178 of the *Bankruptcy and Insolvency Act* provided that the discharge of student loans could only occur as the result of a special hearing to be held after two years had passed and only if the hearing resulted in a finding that the debtor had made good faith efforts to repay the student loan debt and that the repayment would result in significant hardship. Debtors who filed for bankruptcy more than two years after leaving school could have their student loans discharged as before.
48. In 1998, in conjunction with the expanded debt-relief measures under the Canada Student Loan Program, the *Bankruptcy and Insolvency Act* was further amended to increase the period during which discharge was not allowed from two years to ten years after the debtor had left full- or part-time study.
49. This ten-year exception to discharge student loans in bankruptcy has been highly criticized by bankruptcy trustees, student groups, and academics as being unduly harsh. In an effort to strike a better balance in the system, in November 2005, Parliament passed legislation that would reduce the waiting period for the ability to have a student loan discharged from 10 years to 7 years after the date on which the bankrupt ceased to be a full- or part-time student, and reduce the waiting period from 10 years to 5 years before which a student could bring a hardship application to the court. This legislation is not yet in force.

Issues arising from current rules

50. No empirical evidence exists to support the claim that student loan debtors use the bankruptcy system as a means to avoid repaying their student loans.
51. The Canadian insolvency system does not have features that would provide an incentive for former students to use bankruptcy to avoid repaying their loans.
52. In fact, the student loans system includes many debt management measures to assist student borrowers who are having difficulty repaying their loans. For example, debtors who are in default in their Canada Student Loans or who have declared bankruptcy and have a family income below a certain level may be eligible for Interest Relief. While receiving Interest Relief, the Government of Canada will pay the interest on the Canada Student Loan, and the student does not need to make any payments on the loan. Interest Relief is normally approved for six-month periods, up to a maximum of 30 months. If a student

has exhausted the 30 month limit of Interest Relief and is still experiencing financial difficulty in repaying the loans, the student may be eligible for Extended Interest Relief for up to an additional 24 months, provided that the application date is within five years of leaving school. Finally, if a student has exhausted all other options, has been out of school for five years and is still unable to make payments toward the loan, the student may apply to have the loan principal reduced if the loan payment exceeds a given percentage of the student's income.

53. Under the legislation currently in force, student loan debtors must wait 10 years after leaving school before becoming eligible to request the court to discharge their student loan debt on the grounds of hardship. This long waiting time acts as a deterrent to students who would consider using the bankruptcy system as a means of avoiding paying their student loans.
54. In addition, recent amendments to the student loan system have been implemented to ease the debt burden on student loan borrowers who have participated in a bankruptcy-related event, such as a bankruptcy, a consumer proposal, or a provincial arrangement for the orderly payment of debts. On May 11, 2004, the Canada Student Loans Program implemented program changes that apply to borrowers who declare bankruptcy on or after May 11, 2004. These changes allow full-time students who participate in a bankruptcy-related event to apply for new federal loans and interest-free status while they remain in full-time study. The changes also allow borrowers who participate in a bankruptcy-related event while in repayment to qualify for debt management measures, including Interest Relief and Debt Reduction in Repayment.
55. Interest Relief provides relief to borrowers who are experiencing temporary financial difficulties in repaying their Canada Student Loans. Borrowers who receive Interest Relief are not required to make any payments, of interest or principal, on their Canada Student Loans for periods of 6 months at a time. Interest also does not accrue on the loans while a borrower is receiving Interest Relief. If a borrower chooses to make payments on the student loan while receiving Interest Relief, the entire payment will be applied against the loan principal.
56. Debt Reduction in Repayment is a targeted debt management measure available to assist borrowers who have exhausted Interest Relief and who continue to experience exceptional long-term financial difficulty in meeting their Canada Student Loan repayment obligations. The measure provides a reduction in the principal amount of the borrower's Canada Student Loan and aims to reduce the monthly loan payment to an affordable level relative to the borrower's income. For example, eligible borrowers may be provided with an initial reduction of their loan principal of up to \$10,000. Borrowers who continue to remain in financial difficulty after the initial reduction may apply for a second and third reduction in amounts of up to \$5,000, each in 12-month intervals.

57. In addition, some provinces have loan remission programs that forgive part of the value of student loans in cases where borrowing has been quite heavy.
58. The treatment of student loans in bankruptcy has been an issue of much political debate among trustees, lawyers, student associations, academics and other stakeholders who all believe the ten-year rule to be too harsh. These interest groups are lobbying the government to reduce the time periods before which student loans can be discharged in bankruptcy.
59. Furthermore, the treatment of government student loans in bankruptcy is an issue for public concern given that the government is accountable to the taxpayers for the expenditure of these public funds.
60. Tuition fees have increased substantially over the last decade leading to an increased use of the student loan system. Due to these increases, student loans and the issues surrounding their repayment in general have been receiving more political attention.

Finland

Student loan system

61. Finland has a system of student financial aid, which is available in the form of study grants, housing supplements and government guarantees for student loans. The present system was introduced 1994, former law was from 1972.
62. Study grant and housing supplement are government-financed benefits. Student loans are provided by private banks, but they have a government loan guarantee.
63. Study grants and housing supplements normally relate to accommodation and living costs, loans depend on the needs of an individual student. Tuition fees for university education is financed by the state in Finland.
64. The student is usually required to start repaying the loan soon after completing education.

Rules applying to student loans in bankruptcy

65. Student loans are provable in bankruptcy. Under Finnish law, there is no discharge from any debts in bankruptcy. Student loans have the same priority as other unsecured debts and are treated the same way in voluntary arrangements.

Issues arising from current rules

66. There are no concerns about former students using bankruptcy to avoid repaying student loans as there is no discharge from debts in bankruptcy in Finland.

Hungary

Student loan system

67. The Hungarian Government launched the student loan system in the year 2001, and founded Diákhitel Központ Rt. (Student Loan Centre Ltd.) with the purpose of managing the loans, and providing the financial background of the student loan system.
68. The student loan system is aimed at providing an opportunity for any young person to participate in higher education regardless of the person's or his/her family's ability to take on financial burdens, by allowing the Government to ensure the long-term conditions for a sustainable, high quality, generally available, mass higher education system in order to further the economic development in Hungary. In order to achieve those aims in a manner that is secure and cost-effective in the long run, and owing to the size and the social/fiscal implications of the student loan system, the Government will set up and run the student loan system - including the processes of creating funding sources, credit application, loan disbursement, and repayment - by involving competent state institutions and state-owned organisations, and facilitating a strong cooperation between the Student Loan Centre Joint Stock Company (Diákhitel Központ Részvénytársaság) and the said organisations.
69. Although the Hungarian Student Loan Centre is state-owned, the student loan system is financed by the private sector (throughout bank loans, bond issues and loans from international financing institutions) with the suretyship of the Hungarian Government. So the Student Loan Centre operates as a pass-through institution which, in addition, provides a state suretyship to the creditors and investors.
70. The Hungarian student loan can be withdrawn by those who have a Student Status at any higher education institutions in Hungary, regardless of the costs that the students are covering by the loans.
71. The repayment obligation starts on the first day of the month subsequent to the date when the Student Status is terminated or when the Credit Application Period is elapsed, at the latest. From that time the debtors pay an obligatory repayment monthly which is proportional to their income two years preceding. In the first two years of the repayment period the basis income is the actual 'minimum wage'. Besides the obligatory repayment the debtors can effect voluntary repayments (prepayments) without any restrictions.

Rules applying to student loans in bankruptcy

72. According to the Hungarian law the institution of bankruptcy cannot be applied to natural persons. However the Hungarian student loan system has several regulations on the delinquent debtors.
73. The arrears from the student loans are primarily collected by the Collection Department of the Student Loan Centre. Debtors with longer than six months

delinquency are handed over to the State Tax Authority, and their loans become debts exacted as taxes. The collected amounts are transferred to the Student Loan Centre, while the Student Loan Centre pays a minimal charge per person to the Tax Authority. (So the student loan debts have a higher priority than other unsecured creditors). However, the debtors have the possibility to get payment facilities. In addition, the delinquent debtors are added to the database of the Interbank Information System (BAR).

74. These rules were introduced at the same time as the student loan system, but default period, after which a debtor is handed over to the Tax Authority, was changed from one year to six months. The provisions, repayments and defaults on payments have not been an issue of any public and political concern yet in Hungary.

Ireland

Student loan system

75. There is no formal system for the provision of loans to students to cover their education. Private commercial financial institutions provide student loans at market rates where such loans are necessary. There is no separate statutory scheme for the provision of student funding
76. However, Ireland does not in general charge citizens of Ireland for the provision of second level or third level (university) education. Ireland also provides a system of grants for economically underprivileged persons for accommodation and living expenses. Consequently, the number and quantum of student loans in Ireland is minimal compared with other jurisdictions.
77. Loans where required are provided by private commercial financial institutions at market rates. In general, these loans depend on the needs of the individual student and normally relate to accommodation or living expenses.
78. Repayment arrangements depend on the terms of the loan as agreed between the parties. In general, student loans are repaid either by the student when they commence work or such repayment may also be made by the other persons (normally the student's parents who normally act as guarantors) during the period of the loan.

Rules applying to student loans in bankruptcy

79. Student loans are provable in bankruptcy and are treated in the same way as other unsecured debts.
80. There is no procedure for automatic discharge under Irish Bankruptcy law. Consequently, student loans cannot be automatically discharged.
81. Where there is a voluntary arrangement (which is seldom used) all debts including student loans would be treated as a normal unsecured loan for the consideration of approval of the scheme of arrangement by creditors.

Issues arising from current rules

82. There is no evidence that former students are using bankruptcy to avoid repaying student loans. There were six (6) proven bankruptcies in Ireland in the past 12 months, none of which related to student loans.
83. There are no features of the Irish bankruptcy system which could provide an incentive for former students to use bankruptcy to avoid repaying their loans.
84. The Irish bankruptcy system is such that self-declaration of bankruptcy is virtually impossible. Financial institutions will only declare an individual bankrupt as a matter of last resort and in particular, only in circumstances where there are substantial debts and the possibility of a return on the institution of bankruptcy proceedings. The likelihood of a student being placed in bankruptcy solely as a result of student loans is minimal.
85. Whilst the treatment of student loans has not caused controversy, the provision of free third level education has caused difficulties. However, substantial changes in this system appear not to be envisaged immediately.
86. Ireland has had to consider the financing of education especially third level education on a number of occasions. Since the provision of free second and third level education has been seen as a matter of social concern and has in effect formed one of the pillars upon which the Irish economy has been regenerated, it is unlikely that a system for the provision of student loans will be introduced in the near future. Consequently, the interaction of bankruptcy and student loans is not a major concern in Ireland.

Jersey

Student loan system

87. There is no formal system for student loans in Jersey although means tested grants are available. These grants are funded by the Government. These grants largely cover tuition fees and are not usually repayable by the student.

Rules applying to student loans in bankruptcy

88. In principle, a student loan would be provable in bankruptcy and treated in the same way as other unsecured debts. If students were to procure loans from a non-central source, these would be claimable in a bankruptcy of the student in the normal way.

Issues arising from current rules

89. As Jersey operates a grant system, there are no issues arising from the way in which student loans are treated in bankruptcy.

Latvia

Student loan system

90. Latvia introduced a formal student loan system on 1 December 1995. The loans are financed by the Government (the Study Fund of the Republic of Latvia) and by private institutions (for example, credit institutions).
91. The system for providing loans to students has a dual nature:
 - 1) the loans for studies in the university;
 - 2) the loans for the casual (everyday) expenses of the student.
92. The student has to start repaying the loans one year after completion of education or three months after expulsion from the university.

Rules applying to student loans in bankruptcy

93. The insolvency law in Latvia does not extend to natural persons. There have not yet been any issues of concern about repayment of these loans.

Malaysia

Student loan system

94. In its early years after Independence, tertiary education in the country was almost fully sponsored by the Public Services Department. Later, a major part of it was converted to study loans as more individuals were enrolled in universities. As the country develops, demands for higher education became apparent to supply the nation with its human resource needs. As such, more institutions of higher learning were set up both private and public. Along with it, a formal system was put in place; various statutory schemes were made available under the Ministry of Higher Education to cater for the financial needs to pursue higher education.
95. Loans where required are provided by both the government and private institutions. Loans provided by the government and its statutory bodies are more flexible with a fixed lower financial costs of 0% or 4% per annum. On the other hand financial institutions charge a much higher rate which varies from one to another.
96. Loans provided are dependent upon a student's needs and also his or her financial background (or financial background of parents). Underprivileged students are given full loans covering everything from tuition fees to accommodation and living expenses. Other students may be given only partial tuition fees.
97. Repayment depends on the terms of the loan as agreed between the parties ranging between 4 to 6 months after completion of studies or upon being employed, whichever is earlier.

Rules applying to student loans in bankruptcy

98. Student loan debts are provable in bankruptcy as normal unsecured debts. They have the same priority as other unsecured debts. There is no procedure for automatic discharge under Malaysian Bankruptcy law. Consequently, student loans cannot be automatically discharged. In this jurisdiction, a discharge of the bankruptcy however does not discharge him from a debt due to the government. As such study loans provided by the government will have to be paid in full.
99. After the making of the Receiving Order, a first meeting of creditors is summoned as an avenue for proposal for composition or scheme of arrangement prior to the making of the Adjudication Order. The same rules of non priority of student loans apply.
100. The Bankruptcy Act treated student loans as normal debts prior to the introduction of the study loan system.
101. Section 5(3) was introduced in 2003 which amongst others provides that petitioning creditors shall commence bankruptcy proceedings against social guarantors (student loans inclusive) after he has exhausted all avenues to recover debts owed to him by the debtor
102. These changes were made as creditors were seen to prefer making guarantors (who are normally easier to trace) bankrupts even before proceeding with bankruptcy against the borrowers.

Issues arising from current rules

103. There is no evidence that former students use bankruptcy as a means to avoid repaying their student loans. To date, no bankruptcies made on debtors' petitions relate to student loans. Over the years, there have been cases of bankruptcies for failure to repay student loans but the number is very small and does not reflect the use of bankruptcy as a means to avoid repayment of student loans.
104. There are no features of the Malaysian bankruptcy system which could provide an incentive for former students to use bankruptcy to avoid repaying their loans or which could discourage former student from applying for bankruptcy.
105. There have been no public or political concerns about the treatment of student loans in bankruptcy.
106. More generally, repayments of these loans have been discouraging and have been an issue of public and political concern as funds were depleting and requiring further injection. New modes of collection were introduced. Reviews and changes in policies were made to make collection more effective. Loans for full time long term certificate level courses were given without any

administrative costs. Clauses on bankruptcy were also introduced into the loan contract.

107. To educate and to assist parents in preparing for their children's higher education financially, a new scheme known as The National Education Saving Scheme was introduced in 2004 providing avenue for parents of lower income group to prepare for their children's higher education. Apart from dividends, parents of deserving students will also be given financial incentive in the form of a matching grant based on amount saved at the time the student is enrolled in any local university. These students will also be given priority for study loans.

Mexico

Student loan system

108. There is no formal system of student loans in Mexico although both private institutions and the Government, through various agencies, grant loans to students. The costs covered by these loans differ from case to case but generally cover some part of the student's tuition costs. Repayment arrangements also differ from case to case.

Rules applying to student loans in bankruptcy

109. Student loans have the same priority and are treated in the same way as other unsecured debts in bankruptcy. There is no automatic discharge from bankruptcy in Mexico.

Issues arising from current rules

110. There is no evidence that former students use bankruptcy as a means to avoid repaying student loans. It would be very difficult for a judge to accept a bankruptcy case regarding a student. Most bankruptcy cases arise when a person, either a company or an individual has commercial activities. It is not common for a non-merchant to be involved in bankruptcy proceedings.
111. There is a public entity dedicated to funding scientific research and investigation (CONACYT). It grants a large amount of student credits, mostly to post graduate students and researchers. This is the only government agency concerned with student loans, and it is public that they have always had trouble when it comes to the repayment of the loans it grants.

New Zealand

Student loan system

112. The Student Loan Scheme was established in 1992 to assist students to overcome financial barriers to undertaking tertiary study. Three separate government agencies are responsible for the policy and delivery of the

scheme; these are the Ministry of Education, Inland Revenue, and the Ministry of Social Development. The loans are funded by the Government.

113. The Student Loan can be used to finance course fees, course-related costs (for example, purchasing text books) and living costs while under-taking tertiary studies.
114. The borrower must start repaying the loan once they start earning more than the repayment threshold, which is currently \$16,588.00 (for the tax year 1 April 2005 to 31 March 2006). The borrower is required to start making repayments towards the loan - even if they are still studying if they are earning more than the repayment threshold. Extra repayments can be made at any time.
115. Minimum repayment of 10% of borrower's gross income is deducted by the employer and paid to the Inland Revenue Department who collects loan repayments after money is borrowed.
116. Interest is charged daily and continues to be applied to a student loan until the loan is repaid in full. For the tax year 1 April 2005 to 31 March 2006 the interest rate on Student Loans in New Zealand is 7%.
117. Two components make up this interest rate:
 - base interest rate (4.2% from 1 April 2005) - the total interest rate less the interest adjustment rate
 - interest adjustment rate (2.8% from 1 April 2005) - based on the consumer price index from the previous year. This rate is affected each year by inflation.

Rules applying to student loans in bankruptcy

118. Student loans are provable in bankruptcy. They are regarded as normal unsecured debts for the purposes of bankruptcy proceedings. All provable debts are extinguished upon discharge from bankruptcy (currently a period of 3 years in New Zealand, unless the term is altered by the Court).
119. Under all other arrangements outside of bankruptcy, the student loan is not discharged.
120. There are a number of informal arrangements that a debtor may wish to undertake to repay their debts (eg a Creditor's Pool or a Compromise with Creditors).
121. In New Zealand there is a formal procedure called a Summary Instalment Order (SIO). A debtor may apply to the District Court for an SIO if their total debts are less than \$12,000. This is a formal procedure where a District Court Judge makes an order, binding on creditors, that allows a person to pay back their debts in regular instalments without the threat of further legal action while the order is in force. A third party supervisor, such as a budget advisor,

an accountant or a financial advisor administers the procedure. The duration of the SIO is usually between 3 to 5 years. However, as noted above, the student loan is not extinguished at the conclusion of the SIO if any debt remains.

122. It should be noted that in many cases the size of the student loan would prevent a debtor entering into the SIO procedure in the first place.
123. These rules (pertaining to SIO's) are subsections of the Insolvency Act 1967 – so were introduced before the Student Loan Scheme (which was introduced in 1992).
124. The most recent update to the qualification threshold for the Summary Instalment Order was made on 19 March 1990 where the Summary Instalment Order qualification threshold was raised to a maximum debt level of \$12,000 from \$4,000 (on 1 January 1982 this was raised to \$4,000 from \$1,000).

Issues arising from current rules

125. Although many bankrupts in NZ have a student loan, little to no evidence exists to suggest the main reason for the bankruptcy was to avoid repaying the student loan. There is sometimes discussions concerning the idea that former students use bankruptcy as a means to avoid repaying their student loans, however as discussed above, although many bankrupts in NZ have a student loan, little to no evidence exists to suggest the main reason for the bankruptcy was to avoid repaying the student loan.
126. There were 2995 bankruptcy adjudications in New Zealand between 1 July 2004 and 30 June 2005. Of these, no bankrupt identified their student loan as the main reason for their adjudication.
127. More generally, student loans and more particularly the interest charged on the loan, is often discussed and debated by politicians and various interest groups, especially before a general election.
128. The Ministry of Economic Development is currently working on reforming insolvency legislation in New Zealand. As part of the reform, it is also proposed to institute an additional insolvency regime alternative known as the “No Asset Declaration”. This regime will assist in the administration of consumer debt and will have a one year duration (compared to the full term of bankruptcy which is, and is expected to remain, 3 years). There are certain restrictions on entering this “No Asset Declaration” procedure, amongst them is not having debt in excess of \$40,000 and if the debtor has a student loan, then the student loan debt will not be extinguished at the end of the one year term.
129. Student loans are expected to remain provable debts and will still be extinguished in the current way should a debtor enter a full bankruptcy once the new insolvency legislation is passed.

130. Under the proposed legislation, the SIO threshold is expected to increase from \$12,000 to \$40,000 as well.
131. It is also understood that the Government is examining the way it charges interest on student loans in New Zealand. Possibilities include charging no interest on the student loan as long as the borrower remains a tax payer in New Zealand.
132. Further information on the Student Loan Scheme in New Zealand may be found at the following New Zealand government websites:
- www.studylink.govt.nz
www.ird.govt.nz/studentloans
www.moe.govt.nz
133. There are no features of the New Zealand bankruptcy system which could provide an incentive for students to use bankruptcy as a means to avoid repaying student loans.

Northern Ireland

Student loan system

134. Northern Ireland introduced a formal system of student loans in 1990. The loans are provided by a UK company which is wholly owned and funded by the Government. The loans provided cover tuition fees and living costs. The student is required to start repaying the loan when earning income above a specified level.

Rules applying to student loans in bankruptcy

135. Prior to 15 January 2005 student loan debts were provable in bankruptcy. Due to a change in legislation, student loan debts are no longer a provable debt in bankruptcy in the case of bankruptcies which commenced on or after that date. Student loan debts are now not discharged in bankruptcy. The rules were changed to prevent students with loans from filing for bankruptcy as a means of avoiding the repayment of a student loan.
136. Balances owed on student loans can be included in voluntary arrangements, although there is no statutory provision to allow this. If the voluntary arrangement is approved by the necessary majority of creditors the Student Loans Company will be bound by it. Should the voluntary arrangement fail the Student Loans Company will, like other creditors be able to pursue the debt due to it.

Issues arising from current rules

137. Prior to the legislative change in 2005, there was some evidence that students were using bankruptcy as a means to avoid repaying student loans although this was not thought to be widespread.

138. There are no particular bankruptcy rules which act as a disincentive to bankruptcy specifically in relation to student loans. However, members of certain professions are subject to bars preventing them practicing if they become bankrupt. Otherwise former students, in common with everyone else, are discouraged from becoming bankrupt through the consequences in terms of for example loss of assets, including any interest they have in a dwelling house.
139. The treatment of student loans in bankruptcy did become an issue of any public concern. This led to the UK government identifying the need to close the loophole whereby former students could escape liability to repay loans through being declared bankrupt.
140. More generally in relation to student loans, concerns were expressed when the previous system of grants was being replaced with a system of student loans that this would be a disincentive to the less-well off entering higher education. There are concerns that current plans to allow universities in Northern Ireland to charge tuition fees of up to £3,000 per annum, with the student being given the option of borrowing the money from the student loan company will be an even greater deterrent to those from less-well off backgrounds.
141. Due to an expansion in the number of university places, numbers of graduates are increasing with the result that many are being forced to take jobs at a level and income below what would normally be expected in the case of a university graduate. The result is that a large number are in jobs where their income is below the level at which they would be expected to start to make repayments, or else the repayments they are making are small and will last for a longer period.

Singapore

Student loan system

142. Singapore does not have a formal system of student loans supported by the Government. Loans are made to students by private financial institutions to cover tuition fees, accommodation costs and some living expenses. Students generally start repaying these loans one year after tuition is completed.

Rules applying to student loans in bankruptcy

143. Student loan debts are provable in bankruptcy. The student loan debt is discharged along with other unsecured debts when the debtor is discharged from bankruptcy. Student loans have the same priority as other unsecured debts and are treated the same way in voluntary arrangements. There has been no particular consideration of special rules applying to student loans in bankruptcy.

Issues arising from current rules

144. There have been no specific issues of concern in relation to the treatment of student loans in bankruptcy.
145. The creditor would usually insist on a guarantor for the loan. The person standing as guarantor is usually a close friend or relative of the student. When the former student becomes a bankrupt, the creditor will look to the guarantor to repay the loan. If the guarantor is unable to repay, the creditor may initiate bankruptcy proceedings against the guarantor. The student generally will not want members of his family to become bankrupt because of him. This could act as a disincentive and discourage the former student from becoming a bankrupt.

Thailand

Student loan system

146. Thailand introduced a system of Government funded student loans 3-4 years ago. The loans cover tuition fees and all necessary expenses. The loan becomes repayable at a time agreed between the parties.

Rules applying to student loans in bankruptcy

147. Student loans are provable in bankruptcy and are discharged at the end of bankruptcy. It is open to a third party to agree to repay the loan on the student's behalf (as an alternative to bankruptcy).

Issues arising from current rules

148. There have been no issues of public concern arising from the way in which student loans are treated in bankruptcy in Thailand.

United Kingdom

(These answers refer to the system in place in England and Wales – Scotland and Northern Ireland have their own systems.)

Student loan system

149. The United Kingdom initially introduced a formal student loan system in 1990. Loans are financed by The Student Loan Company which is wholly owned by the government.
150. The loans are for tuition and living expenses. There are no restrictions placed on what the loans can be spent on. The loans have a financial limit – at present maximum of £4,195 per annum (£5,175 in London) of which a quarter is means tested.

151. At present the loan does not need to be repaid until the April after the student has left or finished the course and the student earns above the threshold income of £15,000 per annum.

Rules applying to student loans in bankruptcy

152. Since 2004, student loan debts have not been provable in, and are not discharged by, bankruptcy. Previously, they had been treated in the same way as other unsecured debts.
153. Student Loans can be included within Individual Voluntary Arrangements. If 75% (in value) of the creditors who vote agree to the terms of the arrangement then this is binding on the Student Loan Company.
154. It was intended when the initial legislation was brought in the student loans were not to be a provable debt, however poor drafting meant that this was not the case and this was corrected in 2004.

Issues arising from current rules

155. As it is no longer possible to prove the loans within bankruptcy, there is no evidence that former students are using bankruptcy to avoid repaying student loans. However, the UK is currently looking at whether former students are taking out alternative forms of finance to repay their loans prior to making themselves bankrupt in order that they may include this alternative finance within the bankruptcy and avoid their student loan.
156. There have been a few instances where Official Receivers have identified this practice and this conduct is considered sufficiently serious to merit a Bankruptcy Restrictions Order, a civil court procedure lengthening the period of time under which an individual is subject to the restrictions placed upon them by Bankruptcy.
157. There is no incentive for former student to use bankruptcy to avoid repaying student loans since these debts are no longer provable in bankruptcy.
158. There are no specific features that would discourage former students in particular apart from the factor that their student debts are not provable.
159. The treatment of student loans came to prominence during the passage of the Enterprise Act 2002. One of the provisions of this legislation was to reduce the discharge period in bankruptcy. Concerns were raised that this would encourage students to “dump” their loans upon graduation by declaring themselves bankrupt. The Education department had been aware that these loans were not provable but did not have a suitable vehicle to make the necessary changes to primary legislation until the Higher Education Act 2004 which received Royal Assent on 1 July 2004.
160. The various changes to the student loan system including and since 1990 have attracted major political attention not least because of the increasing

importance placed in certain areas by certain parties on attracting the “student vote”.

United States of America

Student loan system

161. Students in the US generally apply for federal government-backed student loans in the financial aid office of their university by filling out a Free Application for Federal Student Aid (“FAFSA”) form. The FAFSA form is used to determine the student’s financial need, and establishes the student’s eligibility both for government loans and government grants. The current federal loan system is derived from the Guaranteed Student Loan Program, a part of the Higher Education Act of 1965.
162. There are two types of federal government backed student loans: commonly known as Perkins and Stafford. The student receives Perkins loan proceeds from his or her university. The university receives most of the funds used for Perkins loans from the government, but contributes some of its own funds as well. The student can receive Stafford loan funds directly from the government, or, alternatively, from a participating private financial institution. Stafford loans received from private financial institutions are guaranteed by the government.
163. There are yearly maximums that a student can borrow under the Perkins and Stafford loan programs, and many students will get both types of loans to help pay for college. If the student needs additional money beyond the yearly maximums, the student’s parents can apply for a “Stafford Plus” loan. The Stafford Plus loans work similarly to Stafford loans except that the parents are direct obligors on the notes.
164. Private loans are also available to students. Such loans are not administered through the FAFSA form and are generally more expensive than Perkins and Stafford loans.
165. Proceeds will first be used to pay for tuition or any bills owed to the student’s university (i.e., university housing or meal plans). The student will receive the balance of the loans to pay for ongoing university expenses (such as textbooks), or other expenses. Loan proceeds are distributed one academic period at a time to ensure that payments to the university are current.
166. Repayment for Perkins loans begins 9 months after the student stops attending university. Interest on Perkins loans first begins to accrue when the repayment period starts.
167. Repayment of the principal on Stafford loans begins 6 months after the student stops attending university. Interest on Stafford loans begins accrue when the money is lent (i.e., while the student is in school). Depending upon the student’s financial means at the time the loan was made, a Stafford loan might be “subsidized” which means the government will pay the accruing interest

until the repayment period begins. The student is immediately responsible for the accruing interest on an unsubsidized Stafford loan. The student can either begin paying the interest on an unsubsidized Stafford loan while in school, or elect to capitalize the interest into the debt and begin repaying it along with the principal beginning six months after leaving school.

Rules applying to student loans in bankruptcy

168. Student loans are provable in bankruptcy and have the same priority as other unsecured debts.
169. Discharge is not automatic. The debtor carries a heavy burden of establishing that repaying the student loan debt would cause an “undue hardship” on the debtor and his or her dependants.
170. In the US, chapter 13 allows the debtor to discharge debts through a repayment plan rather than through a liquidation of assets.
171. The debtor must generally pay student loan debt at the same rate through a chapter 13 plan as other unsecured debt. For example, the court might approve a chapter 13 plan that pays 30% of the general unsecured debt and 30% of the student loan debt over the course of the plan. The difference is that when the plan is completed, the debtor will receive a discharge from the general unsecured claims, but will still have to pay back the remaining 70% due on the student loan (unless he or she can prove that repayment would be an “undue hardship”). The Bankruptcy Code does not allow the debtor to propose a plan that repays student loan debt at a more favourable rate than other unsecured debt.
172. The rules have become less debtor-friendly over time. Prior to 1998, older student loans could be discharged without a showing of undue hardship. The initial test was loans that “first became due” 5 years before the bankruptcy filing. The time frame was later changed to 7 years, and in 1998 the provision for automatic discharge of old student loan debts was eliminated. Elimination of this provision was likely due to student loan default rates and to a perception that some students unfairly received the financial benefits of a higher education through higher lifetime earnings, but were not paying for that benefit because of a bankruptcy discharge early in their careers.
173. Until recently, student loans made by private financial institutions that were not government guaranteed loans (i.e. Stafford loans) were not subject to the “undue hardship” test. This exception was eliminated in the 2005 amendments to the Bankruptcy Code, without comment in the legislative history.

Issues arising from current rules

174. There is no evidence that former students are using bankruptcy as a means to avoid repaying student loans. There are no features of the system which could provide an incentive to former students to use bankruptcy to avoid repaying

these debts. Because undue hardship standard is very difficult to show, it is unlikely that debtors file bankruptcy solely to avoid repaying student loan debt.

175. Generally in relation to student loans, the US Department of Education tracks student loan default rates in the aggregate and by participating school. According to its most recent report, the default rate on government backed student loans had dropped from a high of 22.4% in 1992 to 4.5% in 2003. Under the loan program, universities with default rates over 25% are put on sanctions and, unless the default rate improves, are eliminated from the loan program. In 1992, 642 schools were on sanctions and in danger of being eliminated from the loan program. By 1998 only 11 schools were on sanctions and in 2003 no schools were on sanctions.

Appendix A

TREATMENT OF STUDENT LOANS IN BANKRUPTCY

At its 2005 meeting in Helsinki, the IAIR agreed to undertake a project examining the treatment of student loans in bankruptcy across member jurisdictions. The Insolvency and Trustee Service Australia agreed to conduct this project and present a report at the next IAIR meeting.

Background

Many countries have in place a system providing for loans to students to allow them to undertake university education. These loans are provided by the Government and the student becomes liable to repay them once they are employed. In some cases, the repayments commence only after the student is earning above a minimum threshold income.

If the student becomes bankrupt and has not paid off the student loan, how is that debt treated in the bankruptcy? This is becoming a significant issue for some countries as the amount of debt owed by former students has increased substantially. If the debt is completely or automatically discharged in bankruptcy, this increases the cost of providing student loans, particularly in countries with high numbers of consumer bankruptcies.

The purpose of this project is to prepare a report which provides details of how these student loans are treated in bankruptcy around the world. The report will also explain, where possible, the rationale for the approaches taken by different countries. The attached questionnaire contains some questions which ask members to explain the rules applying to student loans and other questions which ask members to outline their experience in applying these rules. The results will be collated into a comprehensive report which will be available for consideration at the next IAIR meeting.

Please send your responses to david.bergman@itsa.gov.au by 31 January 2006.

IAIR Member/Country details	
Country	
Agency name	
Contact person	

Part A – Student loan system

A1. Does your country have a formal system for providing loans to students to cover the cost of their education? If yes, when was this system introduced?
A2. Are the loans financed by the Government or by private institutions?
A3. What costs are covered by the loans?
A4. When does the student have to start repaying the loan? For example, do repayments start immediately upon completion of education, when the student starts to earn an income, or at some other time?

Part B – Rules applying to student loans in bankruptcy

B1. Are student loan debts provable in bankruptcy?
B2. Are student loan debts discharged in bankruptcy? If yes, is this discharge automatic?
B3. Do student loan debts have the same priority as other unsecured creditors?
B4. Are the rules the same for arrangements other than bankruptcy (for example, voluntary arrangements with creditors)? Please provide details.
B5. Were these rules introduced at the same time as the student loan system or at some later time?
B6. Have the rules for treatment of student loans in bankruptcy changed? If yes, please provide details including the reasons for these changes.

Part C – Issues arising from current rules

C1. Is there any evidence that former students use bankruptcy as a means to avoid repaying their student loans?

C2. Are there any features of your system which could provide an incentive for former students to use bankruptcy to avoid repaying their loans?

C3. Are there any features of your system which could discourage insolvent debtors who are former students from becoming bankrupt?

C4. Has the treatment of student loans in bankruptcy been an issue of any public or political concern?

C5. Has the provision and repayment of student loans generally (that is, outside bankruptcy) been an issue of any public or political concern?

Part D – Miscellaneous

Are there any other comments you would like to make about the treatment of student loans in your country (including any proposals for reform in this area)?