1986

Goldrich v. New York State Higher Education Services Corp.: A New Burden on Bankruptcy's Fresh Start

Sharon L. King

Follow this and additional works at: https://scholarlycommons.law.case.edu/caselrev

Part of the Law Commons

Recommended Citation
Sharon L. King, Goldrich v. New York State Higher Education Services Corp.: A New Burden on Bankruptcy's Fresh Start, 36 Case W. Rsrv. L. Rev. 557 (1986)
Available at: https://scholarlycommons.law.case.edu/caselrev/vol36/iss3/7

This Note is brought to you for free and open access by the Student Journals at Case Western Reserve University School of Law Scholarly Commons. It has been accepted for inclusion in Case Western Reserve Law Review by an authorized administrator of Case Western Reserve University School of Law Scholarly Commons.
Case Notes

GOLDRICH V. NEW YORK STATE HIGHER EDUCATION SERVICES CORP.: A NEW BURDEN ON BANKRUPTCY'S FRESH START

This Case Note examines the Second Circuit decision of Goldrich v. New York State Higher Education Services Corporation, which permitted the state of New York to require a student to reaffirm previously discharged student loans before the state would guarantee further debt. The case is seen as an anomaly to prior decisions that have broadly construed the “fresh start” policies inherent in section 525 of the Bankruptcy Code which prohibits governmental units from discriminating against individuals because they have sought relief under the bankruptcy laws. The author concludes that Goldrich moves far afield from the policies of the bankruptcy laws and sets a dangerous precedent that may eventually be extended to debts other than student loans.

INTRODUCTION

"ONE OF THE primary purposes of the Bankruptcy Act is to [give honest debtors] a new opportunity in life and a clear field for future effort, unhampere by the pressure and discouragement of preexisting debt."¹

Throughout history, the lives of debtors unable to meet their obligations were spent at their creditors' whims with little or no hope of economic independence. Roman debtors were subject to incarceration in the creditor's house for sixty days without any duty on the part of the creditor to feed the delinquent debtor.² English and early American debtors were jailed in debtor's prisons.³ Although these practices may have resulted in a curious sort of satisfaction to the debtor's creditors, they also burdened the state with

¹. Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934).
the expense of "maintaining the debtor-prisoner and his inevitably destitute dependents." 4

In an attempt to avoid burdening the state, and recognizing that debtors must be given incentive to become independent economic entities after bankruptcy, one of the primary goals of the United States' bankruptcy laws is granting a fresh start to debtors who have had their obligations discharged in bankruptcy. 5 Fundamental to the implementation of this policy is section 525 of the Bankruptcy Code, which prohibits governmental units from discriminating against individuals solely because they turned to the bankruptcy laws for relief from their indebtedness. 6 The section's original pur-

---

6. Section 525 provides in pertinent part:
   (a) . . . [A] governmental unit may not deny, revoke, suspend, or refuse to renew a license, permit, charter, franchise, or other similar grant to, condition such a grant to, discriminate with respect to such a grant against, deny employment to, terminate the employment of, or discriminate with respect to employment against, a person that is or has been a debtor under this title or a bankrupt or debtor under the Bankruptcy Act, or another person with whom such bankrupt or debtor has been associated, solely because such bankrupt or debtor is or has been a debtor under this title, or a bankrupt or debtor under the Bankruptcy Act, has been insolvent before the commencement of the case under this title, or during the case but before the debtor is granted or denied a discharge, or has not paid a debt that is dischargeable in the case under this title or that was discharged under the Bankruptcy Act.
   (b) No private employer may terminate the employment of, or discriminate with respect to employment against, an individual who is or has been a debtor under this title, or a debtor or bankrupt under the Bankruptcy Act, or an individual associated with such debtor or bankrupt, solely because such debtor or bankrupt—
      (1) is or has been a debtor under this title or a debtor or bankrupt under the Bankruptcy Act;
      (2) has been insolvent before the commencement of a case under this title or during the case but before the grant or denial of a discharge; or
      (3) has not paid a debt that is dischargeable in a case under this title or that was discharged under the Bankruptcy Act.
pose was to codify the result in *Perez v. Campbell*\(^7\) and to strengthen the anti-reaffirmation policies of section 524 of the Code.\(^8\)

In the past, the Code's antidiscrimination and anti-reaffirmation provisions have been broadly applied to invalidate a wide range of state activities.\(^9\) In *Goldrich v. New York State Higher Education Services Corp. (In re Goldrich)*,\(^10\) however, the Second Circuit Court of Appeals contradicted that trend by holding that section 525 does not prohibit creditors from refusing to extend credit to an individual whose prior debt has been discharged in bankruptcy.\(^11\)

The immediate effect of *Goldrich* was to allow New York state to require a student whose loans had been discharged in bankruptcy to reaffirm those debts prior to reviewing the individual's application for subsequent loan guarantees.\(^12\) More broadly, the *Goldrich* decision establishes a precedent which could seriously infringe upon a debtor's fresh start. The narrow construction of section 525 espoused by the court in *Goldrich* may pose serious obstacles for debtors trying to obtain credit, a prerequisite to a fresh start. Significantly, the *Goldrich* principle may not be limited to student loans, but may also be applied in the context of businesses applying for credit during reorganization or to any credit or financing arrangement where the applicant has previously had debts discharged in bankruptcy.

---


8. 11 U.S.C. § 524 (1982 & Supp. II 1984). Section 524(a) prohibits creditors from using threats and other harrassments to collect discharged debts. In contrast to section 525, section 524 applies to private individuals as well as public entities. Both sections are intended to prevent discriminatory or coercive treatment of debtors who have received discharges. *See 3 COLLIER ON BANKRUPTCY* § 525.03 (15th ed. 1985). Furthermore, section 524 outlines strict procedures which courts must follow before permitting a debtor to voluntarily reaffirm a debt which has been discharged. *See id.* § 524.02-04. *See infra* notes 36-45 and accompanying text for legislative history on 11 U.S.C. § 525.

9. *See generally* H. MILLER & M. COOK, A PRACTICAL GUIDE TO THE BANKRUPTCY REFORM ACT 414 (1979) (discussing the broad construction given section 525 by the courts and predicting that a wide range of governmental activities will be struck down). For a review of some of the governmental practices which have already been abolished, *see infra* notes 66-112 and accompanying text.


I. THE GOLDRICH DECISION

A. Factual Background

In 1969, Goldrich obtained a student loan which was guaranteed by the New York State Higher Education Services Corporation (NYSHESC). In 1971, Goldrich defaulted on the loan, forcing the NYSHESC to pay the full amount of the loan to the issuing bank.

In 1978, NYSHESC obtained a judgment against Goldrich in the amount of the guaranteed loan. Two years later, Goldrich petitioned for a voluntary bankruptcy under Title 11, scheduling the unpaid student loan as one of his debts. In 1981, Goldrich received a discharge from his dischargeable debts, which included the student loan. Prior to and after receiving his discharge, Goldrich attempted to obtain additional student loans. Although his applications were accepted by various New York banks, NYSHESC refused to consider his applications for additional loan guarantees on the ground that they were prevented from doing so under section 616(6)(b) of the New York Education Law. That statute provides that "[a]ny student who is in default in the repayment of any student loan, the payment of which has been guaranteed by the corporation . . . shall not be eligible for any . . . student loan so long as such default status or failure to comply continues."

B. The Bankruptcy Court's Decision

In 1983, Goldrich petitioned the bankruptcy court for injunctive and monetary relief against the state due to its refusal to consider his loan application. The bankruptcy court granted this relief. Subsequently, Goldrich filed a complaint in which he challenged

15. Id.
16. Currently, educational loans which are provided, insured, or guaranteed by a governmental unit, are nondischargeable. Exceptions to nondischargeability are available if the loan first becomes due at least five years prior to filing a bankruptcy petition or if undue hardship to the debtor or his dependents would result. 11 U.S.C. § 523(a)(8) (1982 & Supp. II 1984). It is interesting to note that, beginning in 1985, the Internal Revenue Service will be withholding tax refunds of people who have defaulted on government loans. This includes 656,894 students who failed to repay $1.3 billion in loans. See N.Y. Times, Jan. 10, 1986, at 1, col. 2.
18. Id.
the constitutionality of the state's loan denial pursuant to section 661(6)(b). The bankruptcy court held that section 661(6)(b) unconstitutionally discriminated against former bankrupts by conditioning the award of student loans on the payment of discharged debts.

Relying on Perez v. Campbell, the legislative history of section 525, and previous decisions interpreting that section, the bankruptcy court found that extensions of credit fall within the scope of section 525's mandate against discriminatory treatment. Furthermore, the bankruptcy court ruled that section 661(6)(b) was unconstitutional because it frustrated the underlying policies of the federal bankruptcy laws by "denying [a former bankrupt] the means available to other citizens to acquire a higher education."

C. The Appellate Court Reversal

The Second Circuit Court of Appeals rejected the bankruptcy court's broad application of section 525 because it found a loan guarantee to be dissimilar to any of the enumerated grants contained in section 525. Section 525 provides in pertinent part:

[A] governmental unit may not deny, revoke, suspend, or refuse to renew a license, permit, charter, franchise, or other similar grant to, condition such a grant to, discriminate with respect to such a grant against . . . a person that is or has been a debtor under this title . . . solely because such bankrupt or debtor is or has been a debtor under this title . . . has been insolvent before the commencement of the case under this title, or during the case but before the debtor is granted or denied a discharge, or has not paid a debt that is dischargeable in the case under this title.

20. Id.
22. Goldrich, 45 Bankr. at 519-23.
23. 402 U.S. 637. See infra notes 47-65 and accompanying text.
24. See infra notes 36-46 and accompanying text.
27. Id. at 523.
Adopting a restrictive interpretation of section 525, the court held that a credit guarantee does not fall within the section’s scope because it is not a “license, permit, charter, franchise, or other similar grant.” 29 Reluctant to probe beyond the plain language of the statute, the court asserted that, “[A]lthough the exact scope of the items enumerated [in section 525] may be undefined, the fact that the list is composed solely of benefits conferred by the state that are unrelated to credit is unambiguous.” 30 Applying the rule of *ejusdem generis* 31 to the phrase “other similar grant,” the court held that applications for credit do not fall within the scope of section 525’s protections. 32

The appellate court in *Goldrich* also found that section 661(6)(b) did not conflict with the Bankruptcy Code because the state law was “not intended to coerce payment of defaulted student loans.” 33 Rather, the court found that the New York law was designed to serve the permissible state purpose of “protect[ing] the state coffers against repeated default.” 34

In addition to finding that the legislation served a legitimate state purpose, the court found that the state had not applied section 661(6)(b) in a discriminatory fashion. The language of section 661(6)(b) indicated that the section pertained to all students who failed to repay student loans, whether or not they declare bank-

---

31. *Id.* The court concluded that “[i]n the absence of ambiguity,” no further analysis was necessary. *Id.* (citations omitted). Since, however, the bankruptcy court relied on the legislative history of section 525 in reaching its decision, the appellate court felt compelled to provide further justification for its narrow interpretation of the statute. In continuing its analysis, the court focused on a statement from the Senate Report which accompanied section 525:

> This section permits further development to prohibit actions by governmental or quasi-governmental organizations that perform licensing functions, such as a State bar association or a medical society, or by other organizations that can seriously affect the debtors' livelihood or fresh start, such as exclusion from a union on the basis of discharge of a debt to the union's credit union.

*Id.* at 30 (quoting S. REP. NO. 989, 95th Cong., 2d Sess. 81, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787, 5867). See *infra* note 34 and accompanying text. The court ultimately justified its decision on the grounds that the “extension of credit [was] manifestly different from both examples given in the Senate Report: licensing and exclusion from a union.” *Goldrich*, 771 F.2d at 31.

32. The doctrine of *ejusdem generis* requires that “[w]here general words follow specific words in an enumeration describing the legal subject, the general words are construed to embrace only objects similar in nature to those objects enumerated by the preceding specific words.” *Rose v. Connecticut Housing Fin. Auth. (In re Rose)*, 23 Bankr. 662, 666 n.6 (Bankr. D. Conn. 1982) (citations omitted).
34. *Id.*
ruptency; therefore, since bankrupt and non-bankrupt loan defaulters were treated identically, the court concluded that the statute was not discriminatory on its face or in its application.\textsuperscript{35} It should be noted, however, that by restricting its analysis to the plain language of the statute despite the expressed legislative intent that the courts were to continue developing the \textit{Perez} rule,\textsuperscript{36} the court in \textit{Goldrich} failed to consider whether the effect of the state action conflicted with the underlying policies of the federal bankruptcy laws.

\section*{II. \textbf{SECTION 525'S PROTECTION AGAINST DISCRIMINATORY TREATMENT}}

Facially, section 525 does not encompass the denial of credit or financing. In fact, as one expert in the field has noted:

\textit{The prohibition against discriminatory treatment does not affect decisions to grant credit to the debtor since future financial responsibility may be taken into account by a creditor. It had been feared that discriminatory treatment might be interpreted to include the granting of credit. \textit{However, consideration of a past discharge in determining whether to grant the debtor credit does not violate the Code to the extent that the decision is made by a non-governmental entity, or is based on purely economic criteria, such as future financial responsibility}.}\textsuperscript{37}

On the other hand, section 525's legislative history clearly indicates that Congress did not intend to enumerate all of the forms of discrimination by government organizations which conflict with the policies of the bankruptcy laws. Both the Senate and House Committee Reports which accompanied section 525 indicate that Congress intended that the courts expand upon the enumerated forms of discrimination and continue developing the \textit{Perez} rule.\textsuperscript{38}

\textit{[T]he section is not exhaustive. The enumeration of various forms of discrimination against former bankrupts is not intended to permit other forms of discrimination. The courts have been developing the \textit{Perez} rule. This section permits further develop-}

\textsuperscript{35.} \textit{Id.}  
\textsuperscript{36.} \textit{Id.}  
\textsuperscript{37.} \textit{Id.} The Senate Committee Report accompanying the legislation which became section 525 stated,  
\textit{The section is not exhaustive. The enumeration of various forms of discrimination against former bankrupts is not intended to permit other forms of discrimination. The courts have been developing the \textit{Perez} rule. This section permits further development to prohibit actions by governmental or quasi-governmental organizations that... can seriously affect the debtors' livelihood or fresh start...}. S. REP. NO. 989, 95th Cong., 2d Sess. 81, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787, 5867 [hereinafter cited as S. REP.]. See infra notes 36-39 and accompanying text.  
\textsuperscript{38.} \textit{COLLIER ON BANKRUPTCY, supra} note 8, § 525.02 (emphasis added).
ment to prohibit actions by governmental or quasi-governmental organizations . . . that can seriously affect the debtor's livelihood or fresh start . . . .

Congress also declared that the effect of section 525 and further judicial enunciations of the Perez doctrine should strengthen the anti-reaffirmation policy of section 524(b) of the Bankruptcy Code. Discrimination which results solely from nonpayment of discharged debts runs counter to section 524's expressed policy of protecting the debtor's discharge.

An examination of section 525's legislative history reveals that Congress sought to limit the application of the antidiscrimination provision to government actions which discriminate solely on the basis of bankruptcy. Congress emphasized that the prohibition does not prevent the examination of factors leading to the bankruptcy or of prospective financial or managerial ability. Bankrupts may also be subject to nondiscriminatory "requirements such as net capital rules" or "financial responsibility rules."

The overriding objective of section 525 is to "prevent an automatic reaction against an individual for availing himself of the protection of the bankruptcy laws" and to prohibit all discrimination of the character condemned in Perez. Even so, a state may impose regulations which fall short of coercing payment, so long as they do not conflict with the bankruptcy laws. An examination of Perez provides some indication of the scope of this permissive regulation.

---

40. S. REP., supra note 37, at 5867.
41. Id. See also COLLIER ON BANKRUPTCY, supra note 8 and accompanying text (discussion of 11 U.S.C. § 524(b) (1982 & Supp. II 1984)).
42. S. REP., supra note 37, at 5867.
43. Id.
44. H. REP., supra note 39, at 6126.
45. S. REP., supra note 37, at 5867.
46. H. REP., supra note 39, at 6126, quoted in Duffey v. Dollison, 734 F.2d 265, 273 (6th Cir. 1984) (upholding Ohio's "imposition of financial responsibility requirements, so long as they are not discriminately applied to bankrupts."). See infra notes 125-32 and accompanying text (discussing Duffey).
47. H. REP., supra note 39, at 6126. The policy is based on Congress' belief that, "[m]ost bankruptcies are caused by circumstances beyond the debtor's control. To penalize a debtor by discriminatory treatment as a result is unfair and undoes the beneficial effects of the bankruptcy laws." Id. (footnote omitted).
48. See infra notes 125-31 and accompanying text. See also Note, Supremacy of the Bankruptcy Act: The New Standard of Perez v. Campbell, 40 GEO. WASH. L. REV. 764, 771-72 n.51 (1972). The main test appears to be whether the state actions coerce bankrupts into making payment on their discharged debts by "leaving no real choice but to pay his judgment creditor." Id.
III. The Supremacy of the Debtor’s Fresh Start: The Perez Decision

In Perez v. Campbell,\(^4^9\) the Supreme Court struck down a section of Arizona’s Motor Vehicle Safety Responsibility Act which required the suspension of a judgment debtor’s driver’s license if a tort judgment arising out of an automobile accident remained unpaid for sixty days.\(^5^0\) The Court held that the Arizona statute frustrated operation of the Bankruptcy Act and was therefore invalid under the supremacy clause of the Constitution.\(^5^1\) In so holding, the Court adopted a new test for determining whether a state law impermissively conflicts with the discharge and anti-reaffirmation policies of the bankruptcy laws.\(^5^2\)

Relying on the rule in supremacy clause cases drawn from Hines v. Davidowitz,\(^5^3\) the Court in Perez ruled that the function of its analysis should be to determine whether the Arizona statute stood as “an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.”\(^5^4\) If so, the state law must be found to be invalid.\(^5^5\) Such a determination “is essentially a two-step process of first ascertaining the construction of the two statutes and then determining the constitutional question [of] whether they are in conflict.”\(^5^6\) In its analysis, the Court determined that the principle purpose of the Arizona statute was “the protection of the public using the highways from financial hardship which may result from the use of automobiles by financially irresponsible persons.”\(^5^7\) The Court determined, however, that the effect of the state Act was to provide creditors with leverage to collect tort debts even though the debts had been discharged in bankruptcy.\(^5^8\)

\(^4^9\) 402 U.S. 637 (1971).
\(^5^1\) Perez, 402 U.S. at 652. The governing principle of the supremacy clause, U.S. Const. art. VI, cl. 2, is that “acts of the State Legislatures . . . [which] interfere with, or are contrary to the laws of Congress, made in pursuance of the Constitution,” are invalid under the Supremacy Clause.” Perez, 402 U.S. at 649 (quoting Gibbons v. Ogden, 22 U.S. (1 Wheat.) 1, 92 (1824)). See also Hines v. Davidowitz, 312 U.S. 52, 67 (1941) (state statutes which stand as “obstacle[s] to the accomplishment and execution of the full purposes and objectives of Congress” must be struck down).
\(^5^2\) For a discussion of the Perez decision, the limits of the rule, and imposing consequences on bankrupts, see generally Note, supra note 48.
\(^5^3\) 312 U.S. 52 (1941). See supra note 51.
\(^5^4\) Perez, 402 U.S. at 649 (quoting Hines, 312 U.S. at 67).
\(^5^5\) Id. at 644.
\(^5^6\) Id.
\(^5^7\) Id. (quoting Schecter v. Killingsworth, 93 Ariz. 273, 280, 380 P.2d 136, 140 (1963)).
\(^5^8\) Perez, 402 U.S. at 646-47.
Contrasting the goals of the federal bankruptcy laws with the policies underlying the state law, the Court noted that the Bankruptcy Act seeks to give debtors a “new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt,” including discharged tort judgments.\(^6\) As a result, the Court held that the Arizona statute was unconstitutional because it had the effect of frustrating the fresh start policy of the bankruptcy laws. The Court's conclusion directly conflicted with other courts' conclusions regarding similar legislation. Specifically, Utah and New York courts had used a test which focused on the purpose of the state legislation, rather than its effect, to uphold automotive financial responsibility acts similar to Arizona's because the purpose of the state legislation had not been to "circumvent the Bankruptcy Act but to promote highway safety."\(^6\)1 Criticizing these earlier cases, the Court in Perez stressed that the "plain and inevitable effect" of the Utah and New York laws was to "create a powerful weapon for collection of a debt from which [the] bankrupt [had] been released by federal law."\(^6\)2 Characterizing such a result as "aberrational," the Court held that it could no longer adhere to a doctrine whereby a state could frustrate operation of federal law simply because the state's law promoted a legitimate state purpose.\(^6\)3

Perez clearly indicates that a state cannot "deprive a bankrupt of the benefits of a discharge by later utilizing its power to obtain payment of the bankrupt's debts."\(^6\)4 In other words, regardless of a state law's purported purpose, it will be found to be invalid if its effect frustrates the objectives of the bankruptcy laws.\(^6\)5

\(^{59}\) Id. at 648 (quoting Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934)).

\(^{60}\) Id. ("There can be no doubt . . . that Congress intended this 'new opportunity' to include freedom from most kinds of pre-existing tort judgments.").

\(^{61}\) Id. at 650. In two earlier cases, Kesler v. Department of Public Safety, 369 U.S. 153 (1962), and Reitz v. Mealey, 314 U.S. 33 (1941), the Supreme Court upheld Utah's and New York's financial responsibility laws despite the fact that they admittedly left the "bankrupt to some extent burdened by the discharged debt," since the Court did not look to the effect of the state legislation, but rather to the purpose of the statutes which were said not to "aid collection of debts but to enforce a policy against irresponsible driving." Kesler, 369 U.S. at 169. See also the Supreme Court's discussion of these cases in Perez, 402 U.S. at 650-54.

\(^{62}\) Perez, 402 U.S. at 650 (quoting Kesler, 369 U.S. at 183) (Black, J., dissenting) (emphasis added).

\(^{63}\) Id. at 651. The Court went on to find that the stated purpose of the Arizona statute, as expressed in Schecter v. Killingsworth, 93 Ariz. 273, 380 P.2d 136 (1963), would be impermissible even under the purpose test of Kesler and Reitz. Perez, 402 U.S. at 652-54. See also Note, supra note 48, at 771 n.49.

\(^{64}\) Note, supra note 48, at 771.

\(^{65}\) Perez, 402 U.S. at 648-49.
Perez also reaffirms the view that the bankruptcy laws are designed to insure that debtors receive a fresh start, free from the burdens of past obligations. Perez dictates that the bankruptcy law's "fresh start" objective is to be employed in conjunction with the supremacy clause on a case-by-case basis to invalidate acts by states which frustrate the purposes and objectives of the bankruptcy laws and to actualize Congress' intent to provide debtors with a chance to recover from financial disaster.  

IV. INTERPRETATIONS OF THE PEREZ RULE AND THE SCOPE OF SECTION 525

Since Perez and its codification in section 525, the courts have continued to develop the parameters of the antidiscrimination provisions and have invalidated a wide range of acts by governmental and quasi-governmental agencies. Such invalidated practices include discrimination in the form of universities withholding student transcripts, as well as discrimination in the letting of public contracts, mortgage financing, and eviction. Section 525 has been applied to chapter 13 reorganization cases, as well as to "straight liquidations" under chapter 11.

Some of the state actions which have been struck down have fallen within the "plain language" of the statute, but many have not. No case prior to Goldrich has construed the statute as narrowly as the Second Circuit has. The Goldrich court refused to address prior precedent involving actions beyond the "plain language" of the statute.

An examination of some of the cases where section 525 has been applied demonstrates the Goldrich court's inability to grasp the un-

---

66. Id. See also Comment, Student Loans and the Withholding of Transcripts Under the Bankruptcy Reform Act of 1978, 30 U. KAN. L. REV. 265, 276 (1982) (discussing fresh start policy of Perez in conjunction with private and state university discrimination and attempts by these institutions to collect on defaulted loans by withholding transcripts).

67. See infra notes 73-90 and accompanying text.

68. See infra notes 91-100 and accompanying text.

69. See infra notes 101-06 and accompanying text.

70. See infra notes 107-12 and accompanying text.

71. See, e.g., In re Heath, 3 Bankr. 351 (Bankr. D. Ill. 1980) (discussed infra notes 77-80 and accompanying text).

72. For examples of instances in which the state action at issue did not fall within the plain language of section 525, see infra notes 73-112 and accompanying text. See also Goldrich, 771 F.2d at 31 n.1, where the court stated that, since credit applications did not fall within the "plain language" of the statute, it felt no need to reconcile its reasoning with other cited cases which had concluded that section 525 should be broadly construed.

73. See Goldrich, 771 F.2d 28.
derlying objectives of Perez. This failure caused the court to render an opinion which not only conflicts with precedent, but also undercuts Congress' objectives in codifying Perez in section 525.

A. The Transcript Cases

Universities have often been accused of discriminating against debtors by withholding the academic transcripts of students whose loans have been discharged in bankruptcy. In the leading pre-Code case of Handsome v. Rutgers University,74 a state university withheld the transcript and refused to permit registration of a student whose student loans had been discharged in bankruptcy.75 Invalidating the university's actions under Perez, the supremacy clause, and the fourteenth amendment, the Handsome court held that the university's actions were designed to serve its own ends as a creditor, thereby encouraging reaffirmation of discharged loans.76 These ends impermissibly transgressed upon the fresh start policy of the bankruptcy laws. The court ordered the University to turn over the student's transcript and permit her to register and permanently enjoined further use of such practices.77

In In re Heath,78 the bankruptcy court extended the principles enunciated in Handsome, ruling that section 525 prohibited a state college from withholding the transcript of a debtor whose prepetition student loans had been scheduled as part of his chapter 13 re-


75. The facts of Handsome were compelling. The plaintiff attended a division of Rutgers University from 1968 to 1974. During that time, she borrowed $4,600 in the form of National Defense Student Loans and National Direct Student Loans. Subsequently, she suffered severe health problems, incurred large medical bills, and in 1975, she was forced to withdraw from school. After withdrawal, her student loans became due, but she was unable to pay them as a result of her medical bills. In 1977, she filed a bankruptcy petition. Her student loans were part of over $25,000 in liabilities, most of which were medical expenses. At the same time, her total net worth was $368.85. Handsome, 445 F. Supp. at 1363.

In 1977, she received a discharge of her loans without objection from Rutgers University. Later that year, she applied for readmission to Rutgers. The admissions committee informed her that, while she had been readmitted, Rutgers' policy was to "place hold" notices upon the records of students more than three months delinquent in their debts to the university; therefore, she was precluded from registering and the university would not release her official transcripts. Id. at 1363-64.

76. Id. at 1367. See infra notes 86-90 and accompanying text for a discussion of the court's equal protection analysis.

77. Handsome, 445 F. Supp. at 1367. For a general discussion of the transcript cases, see Comment, supra note 66.

habilitation plan.\textsuperscript{79} The Heath court rejected the school's contention that section 525 applies only after a debtor has received a discharge, stating it would be "anomalous to grant a debtor protection from discriminatory actions in a liquidation proceeding and deny him the same protection in a rehabilitation (chapter 13) proceeding."\textsuperscript{80}

The Heath court reasoned that the debtor's ability to fulfill his obligations under a composition plan largely depends upon his ability to obtain employment, which in turn requires access to his transcript.\textsuperscript{81} In a similar case, Howrev v. Board of Trustees of the University of Alabama,\textsuperscript{82} the court went one step further, holding that a state university cannot withhold a debtor's transcript for the sole purpose of compelling him to repay student loans, even if the dischargeability of such loans has not been finally determined.\textsuperscript{83}

The most recent transcript case Johnson v. Edinboro State College,\textsuperscript{84} held, however, that a state educational institution is not required to turn over a student's transcript where that student has failed to repay nondischargeable student loans. While concurring with the result in the previous transcript cases,\textsuperscript{85} the court in Johnson refused to expand the applicability of section 525 to nondischargeable debts. Thus, though the courts have broadly construed section 525 in the student transcript context, there are at least a few instances in which courts have restricted its applications.\textsuperscript{86}

\textsuperscript{79} The court had approved a 10\% composition plan for Heath under which he could be discharged from his remaining debts once he satisfied the plan's conditions. Despite the court's approval of Heath's composition plan, the University refused to release his transcript until his prepetition debt to the school was paid. In holding that the University's actions were unconstitutional, the court noted that the University had not filed an objection to the confirmation plan alleging that it was not "proposed in good faith" prior to its approval by the court. Therefore, the court ruled that the University had no basis for demanding full payment of the loans. \textit{Id.} at 351-52. \textit{See also In re Resse}, 38 Bankr. 681 (Bankr. N.D. Ga. 1984) (state university prohibited from retaining transcript of debtor undergoing chapter 13 reorganization prior to debtor's having obtained a discharge).

\textsuperscript{80} \textit{Heath}, 3 Bankr. at 354.

\textsuperscript{81} \textit{Id.} The University argued that application of Perez should be limited to chapter 7. The court held, however, that the Perez ruling was not limited to chapter 7 liquidation proceedings; rather, it was intended to prevent any discriminatory action which "tends to frustrate Bankruptcy policy as a whole," including "Congress's intent to allow debtors to proceed, subsequent to Bankruptcy, unhampered by preexisting debts." \textit{Id.} (citations omitted).

\textsuperscript{82} 10 Bankr. 303 (Bankr. D. Kan. 1980).

\textsuperscript{83} The court specified, however, that, while a debtor need not have been granted a discharge, bankruptcy proceedings must be initiated for section 525 to apply. \textit{Id.} at 305.

\textsuperscript{84} 728 F.2d 163 (3d Cir. 1984).

\textsuperscript{85} \textit{See supra} notes 73-82 and accompanying text.

\textsuperscript{86} Similarly, courts have consistently refused to extend application of section 525 to
Equal protection arguments have also been utilized to strike down state university actions which discriminate against bankrupts. In *Handsome*, the court held that the Rutgers University classification which included "all persons more than three months delinquent in their debts to the school," insofar as it included bankrupts, "ran afoul of the equal protection clause." The court acknowledged that education is not a fundamental right and that, therefore, the state need only show that the classification at issue is "reasonably related to a legitimate government interest." Nevertheless, the court concluded:

[A] state cannot claim a legitimate interest in securing the repayment of loans discharged in bankruptcy. . . . [A] citizen's status as a bankrupt is *per force*, an impermissible criterion. That is not to say that [a university] may not in the future validly decline to extend credit to one who has previously discharged his debts in bankruptcy, but it cannot deny a citizen so vital a privilege as an education on the basis of his status as a bankrupt.

**B. Public Letting of Contracts**

Section 525's antidiscrimination provisions have been interpreted broadly enough to prohibit discrimination in the context of the letting of public contracts. In *Marine Electric Railway Products Division v. New York City Transit Authority (In re Marine Electric Railway Products Division)*, the court held that the New York City Transit Authority could not discriminate against bankrupts in awarding contracts. See *Girardier v. Webster College, 563 F.2d 1267 (8th Cir. 1977)* (private institution may withhold transcripts to coerce repayment of debts discharged in bankruptcy). See also *In re Coachlight Dinner Theater, 8 Bankr. 656* (Bankr. S.D.N.Y. 1981) (radio station is a private entity, not a governmental unit under section 525 and can, therefore, refuse to accept advertising of a debtor in chapter 11); *In re Northern Energy Prod., 7 Bankr. 473* (Bankr. Minn. 1980) (section 525 not applicable to discrimination by Better Business Bureau of Minnesota since it is a private corporation).

88. Id. at 1367.
89. Id. See *San Antonio School Dist. v. Rodriguez, 411 U.S. 1* (1973) (education not a fundamental right or a suspect classification).
90. *Handsome, 445 F. Supp. at 1367. See Reed v. Reed, 404 U.S. 71, 76* (1971) (where a fundamental right not at issue, the state need only show that the classification is reasonably related to a legitimate governmental purpose).
92. 17 Bankr. 845 (Bankr. E.D.N.Y. 1982). See also *In re Coleman Am. Moving Servs.,
City Transit Authority (NYCTA) could not reject a debtor’s bid on a public contract solely on the ground that the debtor was a chapter 11 debtor in possession. The NYCTA contended that section 525 specifically enumerates activities in which governmental units cannot discriminate and noted that the letting of public contracts was not included. Emphasizing that “the legislative history of section 525 indicates that Congress sought to broadly attack discriminatory practices by governmental entities,” the court rejected the NYCTA’s argument and instead applied the Perez test, weighing the effect of the suspected governmental activities against the purposes of the bankruptcy laws.

The court recognized that a primary purpose of the bankruptcy laws is to “relieve the honest debtor from the weight of oppressive indebtedness and permit him to start afresh free from the obligations and responsibilities consequent upon business misfortunes.” Asserting that enabling a debtor to rehabilitate itself through either individual or corporate reorganization furthered this fresh start policy, the Marine Electric court noted that the debtor’s ability to compete against financially sound individuals and businesses on an equal level is essential to a reorganization debtor’s successful rehabilitation.

The NYCTA tried to justify its actions by arguing that the contract was too important to risk its letting to a contractor who might end up in a chapter 7 liquidation proceeding. Despite the validity of this concern, the court held that it did not “outweigh the vital

---


93. Marine Elec., 17 Bankr. at 853. The code’s rehabilitation provisions (chapters 11 and 13) differ from bankruptcy liquidation proceedings in that, in a rehabilitation proceeding, creditors look to the bankrupt’s future earnings rather than taking his property to satisfy their claims. In order to be successfully rehabilitated, the debtor is allowed to keep the assets he needs to run his business. Such a debtor is known as a debtor in possession.


95. Id. See supra notes 36-46 and accompanying text for a discussion of the legislative history of section 525.


97. Marine Elec., 17 Bankr. at 853 (quoting Williams v. United States Fidelity & Guaranty Co., 236 U.S. 549, 554-55 (1915)).

98. Id. at 853. See supra note 93 for a discussion of the policies underlying reorganization.


100. Id. NYCTA sought to justify its rejection of the plaintiff’s bid on the ground that,
rehabilitative purposes embodied in chapter 11 and in the Code as a whole." Discrimination based solely on the debtor's status as a bankrupt was found, therefore, to violate section 525.

C. Mortgage Financing and Wrongful Eviction

In *Rose v. Connecticut Housing Finance Authority (In re Rose)*, a former bankrupt charged that the Connecticut Housing Finance Authority's (CHFA) refusal to approve his application for a state-funded home mortgage violated section 525 of the Bankruptcy Code. The CHFA argued, however, that the denial of a mortgage loan was not a transaction which fell within the explicit language of section 525 since it was not a "license, permit, charter, franchise or other similar grant."  

Rejecting the CHFA's argument that the plain language of the statute and *ejusdem generis* doctrine precluded application of section 525 to mortgage financing, the bankruptcy court concluded:

> If a state has chosen to enact a program of home financing for its citizens, section 525 prohibits that state from exempting debtors or bankrupts from those benefits solely because of bankruptcy and without taking into account present financial capability. To hold to the contrary would frustrate the Congressional policy of granting the debtor a fresh start by denying him a means open to other citizens of acquiring a home.

While the *Rose* court ultimately found that Rose had not been denied financing solely because of his previous bankruptcy, their analysis indicates that the court assumed that section 525 applied to mortgage financing. This is true even though mortgage financing is not one of the enumerated grants in section 525. It should be noted that *Rose* reaffirms the idea that section 525 does not prevent exami-

---

1. 23 Bankr. 662 (Bankr. D. Conn. 1982).
2. In 1977, Rose had discharged unpaid student loans in a bankruptcy liquidation proceeding. The Housing Authority asked Rose to reaffirm those loans prior to granting him home financing. *Id.* at 663-65.
3. *Id.* at 665.
4. *See supra* note 32 and accompanying text.
6. Members of the CHFA testified that Rose was found to be "not creditworthy" because he had only $108.00 in cash, had no other significant assets, had overdrawn his checking account eight times in the year prior to his application, owed a credit union $1350.00, needed a second mortgage for the balance of the purchase price on the house, and had no way to pay the closing costs. Based upon this evidence, the court could not find that Rose was denied financing solely on account of his prior bankruptcy. *Id.* at 667-68.
nation of the circumstances surrounding the bankruptcy or the debtor's present creditworthiness prior to a government agency's decision to grant or deny financing.

In Gibbs v. Housing Authority (In re Gibbs), the Bankruptcy Court for the District of Connecticut held that section 525 could be used to prevent a city housing authority from evicting a debtor whose debts had been discharged in a chapter 7 proceeding. The agency which rented housing to persons under a state-aided program for moderate income families threatened to evict Gibbs unless she renewed a discharged debt of $74.00 owed to the agency.

Like the defendants in many similar cases, the Housing Authority noted that the word "lease" was omitted from section 525 and claimed that this was an indication of Congress' intention "not [to] regulate the leasing practices of local public housing authorities."

Relying on the congressional belief that "discrimination based solely on nonpayment of debts would encourage reaffirmation contrary to the expressed policies of sections 525 and 524," the court in Gibbs held that the antidiscrimination provisions applied to leasing agreements and precluded eviction of a debtor solely for nonrepayment of a discharged debt. The court felt that the Housing Authority's actions represented a clear example of the type of discrimination prohibited by section 525, even though such action was not specifically enumerated in the statute.

D. The Examination of Circumstances Surrounding Bankruptcy, Creditworthiness and Future Financial Responsibility

While section 525 has been broadly applied, the legislative history of that section clearly points out that Congress fully intended to permit governmental organizations to inquire into a debtor's prospective financial condition and examine the circumstances surrounding a bankruptcy when deciding whether to grant certain privileges to former bankrupts. In re Gahan illustrates such an inquiry into the circumstances of a debtor's bankruptcy. In that case, the Supreme Court of Minnesota held that section 525's prohi-

109. Id. at 763.
110. Id. at 764.
111. Id. See supra notes 38-39 and accompanying text for a discussion of the interaction between sections 524 and 525.
112. Gibbs, 9 Bankr. at 764.
113. Id.
114. See supra notes 36-46 and accompanying text.
115. 279 N.W.2d 826 (Minn. 1979). See also Florida Bd. of Bar Examiners (In re
bition on discriminatory treatment does not prevent a bar association from investigating the circumstances surrounding an applicant's discharge of student loans in bankruptcy to determine whether there was evidence of bad moral character.\footnote{G.W.L.), 364 So.2d 454 (Fla. 1978). See generally B. WEINTRAUB & R. RESNICK, supra note 90, § 3.06 at 3-23 to 3-24.}

In \textit{In re Richardson},\footnote{117. The Minnesota Supreme Court upheld a Board of Law Examiners' denial of Gahan's bar application. Shortly after graduating from law school, Gahan filed a petition in bankruptcy to discharge almost $14,000 in student loans. Although Gahan's actions fell within the legal limits of the bankruptcy laws, the Board felt that his conduct evidenced bad moral character, and that this provided sufficient grounds for denying him admission to the bar.} the bankruptcy court was faced with a factual situation similar to that in \textit{Goldrich}. Richardson applied to the Pennsylvania Higher Education Assistance Agency (PHEAA) for a student loan guarantee, but the PHEAA regulations prohibited the agency from considering the application because an earlier loan to Richardson had been discharged in bankruptcy.\footnote{118. The PHEAA regulation at issue stated: Eligibility for a loan guaranty shall be denied to any person who has allowed his loan to mature through purchase from the lender by the Agency under the guaranty of a previous loan in the Loan Guaranty Program, unless in the judgment of Agency staff such loan should be guaranteed and one of the following has occurred: (1) The defaulted loan has been repaid in full. (2) An approved lending institution has purchased the outstanding balance of the defaulted loan. (3) The student has taken positive steps toward repayment of the loan or toward supplying reasons in justification of the failure to repay. . . . \textit{Richardson}, 15 Bankr. at 928 (quoting 22 Pa. Code § 121.4(b) (1981)). This section was amended in 1981, but both versions were held unconstitutional by the lower court. \textit{Id.} at 929-30.} Richardson sought declaratory and injunctive relief against PHEAA for the anticipated denial of his loan application.

The bankruptcy court granted the requested relief against PHEAA, holding that the agency's regulation violated the antidiscrimination provisions of section 525. Relying on a construction of section 525's legislative history adopted in \textit{Henry v. Heyison}, the court held that the PHEAA regulations were unconstitutional because they treated "a person who has had his student loan obliga-
tion discharged in bankruptcy different from a person who has never incurred a student loan debt.”

On appeal, the district court reversed. The court focused on the fact that section 525 permits agencies such as PHEAA to “inquir[e] into the future financial responsibility of a loan applicant . . . prior to the extension of additional credit in the form of a guaranteed student loan.” The court found that a legitimate basis existed for the denial of Richardson’s application apart from his bankruptcy or his failure to repay the discharged loan and held that the PHEAA had not discriminated against Richardson solely because of his previous bankruptcy.

Section 525 has also been held to permit a state to impose uniform substantive financial responsibility requirements as a condition precedent to the restoration of driving privileges suspended as a result of an individual’s involvement in an automobile accident. In Duffey v. Dollison, the Sixth Circuit Court of Appeals held that Ohio’s financial responsibility law was not preempted by the Bankruptcy Code. Ohio’s first Financial Responsibility Act had required repayment of discharged tort debts prior to restoration of driving privileges and was invalidated in Perez. The law upheld in Duffey, however, required all judgment debtors to post proof of financial responsibility before their driving privileges are reinstated. The Duffey court ruled that “bankruptcy [does] not relieve [a] judgment debtor of the requirement of posting proof of future financial responsibility.”

The court’s analysis focused on Congress’ expression that “the effect of . . . section [525], and of further interpretations of the Perez rule, is to strengthen the anti-reaffirmation policy found in section 524(b).” Finding that the Ohio law did not require satisfaction of a debt discharged in bankruptcy, the court felt that the state statute did not give creditors “leverage for the collection of dam-

120. Id. at 929. See also In re Goldrich, 45 Bankr. 514, 522 (Bankr. E.D.N.Y. 1984), rev’d, 771 F.2d 28 (2d Cir. 1985) (discussing Richardson).
121. Richardson, 27 Bankr. at 564.
122. The court felt that there were sufficient independent grounds for rejecting Richardson’s application. Following his departure from college in 1976, he made no payments on his PHEAA loan and did not contact the lender about readjusting the repayment schedule. Richardson also failed to give notice to the lending institution, thereby forfeiting a grace period. Id. at 565.
123. 734 F.2d 265 (6th Cir. 1984).
125. OHIO REV. CODE ANN. §§ 4509.31-.45 (Page 1982).
126. Duffey, 734 F.2d at 269.
127. Id. at 271. See supra notes 36-46 and accompanying text.
The court noted that the Duffeys could not have "regained their driving privileges without furnishing proof of financial responsibility even by reaffirming the judgments." Reasoning that Congress intended to permit the imposition of financial responsibility requirements so long as they were not discriminatorily applied to bankrupts, the court felt that the statute did not treat judgment debtors who resorted to bankruptcy any differently than it treated other judgment debtors.

As Gahan, Richardson, and Duffey demonstrate, governmental bodies may, in some situations, scrutinize certain factors surrounding a bankruptcy, as well as a former bankrupt's financial responsibility. They are forbidden from discriminating solely on the grounds that an individual sought relief under the bankruptcy laws.

V. THE SCOPE OF THE ANTIDISCRIMINATION PROVISIONS

Some guiding principles can be drawn from Handsome, Marine, Rose, Gibbs, and Duffey. These cases vividly demonstrate that application of the Bankruptcy Code's antidiscrimination provisions is not always limited to situations which fall within the plain language of the statute. For example, university transcripts, public contracts, leases, and mortgage financing do not fall within the literal language of section 525 but have been held to be within the scope of the statute nonetheless. In order to justify their broad interpretation of the parameters of section 525, courts have followed the reasoning set forth in Perez and looked to the effect of a particular state action to see if it frustrates the policies of

128. 734 F.2d at 272 (quoting Perez, 402 U.S. at 646). The court distinguished Ohio's present Financial Responsibility Act from the one declared unconstitutional in Perez by stating, "[S]ince the present Ohio Act provides that a judgment stayed or discharged in bankruptcy need not be satisfied by the judgment debtor as a condition to the restoration of driving privileges, it clearly is consistent with the immediate holding in Perez." Id.

129. Id.

130. Id. at 273.

131. 279 N.W.2d 826 (Minn. 1979).


133. 734 F.2d 265 (6th Cir. 1984).


136. 23 Bankr. 662 (Bankr. D. Conn. 1982).


138. 734 F.2d 265 (6th Cir. 1984).

139. The literal language of section 525 restricts application of the antidiscrimination provision to "licenses, permits, charters or franchises." See supra note 6.

140. See supra notes 47-65 and accompanying text.
the federal bankruptcy laws. While Congress did not intend that debtors filing for bankruptcy escape all debts, it did intend that debtors have a fresh start within the scope of the bankruptcy laws, including the right to act without being under pressure to reaffirm discharged debts. While the state has an interest in collecting student loans, placing government contracts in the hands of financially secure businesses, and ensuring payment of state-guaranteed housing loans, these interests have not been permitted to impinge on the fresh start policies of the Bankruptcy Code.

VI. **Goldrich Revisited**

The effect of the Second Circuit’s decision in *Goldrich* is to force a bankrupt who needs a loan guarantee to repay a debt he is otherwise not required to pay under federal bankruptcy laws. The fundamental flaw in the court’s decision in *Goldrich* is the fact that the court considered the purpose rather than the effect of the New York law. The court upheld the law since the provision had what it deemed to be a permissible state purpose, that of protecting “the state coffers against repeated defaults.”

Despite acknowledging that section 525 was meant to codify the result of *Perez*, the Court in *Goldrich* appears to lose sight of that result.

The rule established in *Perez* was that a state may not pressure a debtor into reaffirming a discharged debt or discriminate against a debtor solely on the basis that he has previously discharged debts in bankruptcy. A state may not frustrate operation of these rules merely because it claims to have a legitimate purpose for doing so.

Under section 661(6)(b) of the New York Education Law, there is no way for a debtor who has had his loans discharged in bankruptcy to get new loans guaranteed until the old loans are repaid. While student loans are generally nondischargeable, the New York law clearly discriminates against those students with discharged loans, since it denies them loan guarantees without any effort to investigate their current or prospective financial

141. *See supra* note 57 and accompanying text.
142. 771 F.2d 28 (2d Cir. 1985).
143. *Id.* at 31.
145. 771 F.2d 28 (2d Cir. 1985).
146. *Id.; Perez*, 402 U.S. at 651-52.
147. *See supra* note 17 and accompanying text.
creditworthiness or the circumstances surrounding their bankruptcy. This result contradicts the Supreme Court's declaration in *Perez* that discrimination based solely on the debtor's status as a former bankrupt is not justified by an otherwise legitimate state purpose.\(^{149}\) The Code's antidiscrimination provisions do not purport to guarantee that debtors will receive credit. Instead, the provisions prohibit debtors from being denied consideration for credit solely because they were once bankrupt. The "consideration of a past discharge in determining whether to grant the debtor credit does not violate the Code to the extent that the decision is made by a non-governmental entity, or is based on purely economic criteria, such as future financial responsibility."\(^{150}\) Because the Code does not prevent private credit sources from discriminating,\(^{151}\) former bankrupts in need of financing will often be forced to look to the state.

In *Goldrich*,\(^{152}\) a governmental agency was permitted to discriminate against a bankrupt without any consideration of the former bankrupt's future financial responsibility simply because the debtor had not repaid a discharged debt.\(^{153}\) This action directly conflicts with the rule established in *Perez*,\(^{154}\) as will any discrimination by governmental agencies when the determinations are not supported by economic criteria other than the simple fact of a former bankruptcy.

**VII. CONCLUSION**

Nonconsideration for credit or financing can severely interfere with a debtor's fresh start. For example, to refuse to even consider a former bankrupt's application for credit, solely because five years earlier he discharged a student loan in bankruptcy, is to completely undercut the fresh start policies of the bankruptcy laws. Such actions do not give a debtor a "new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of preexisting debt."\(^{155}\) Instead, they render the debtor's opportunity for future economic vitality virtually nonexistent. This is

---

149. *Perez*, 402 U.S. at 652. In *Perez*, the otherwise legitimate state purpose was promoting highway safety.

150. *Collier on Bankruptcy*, *supra* note 8, at 525-26 (emphasis added).

151. *See supra* note 86 and accompanying text.

152. 771 F.2d 28 (2d Cir. 1985).

153. *See supra* notes 17-18 and accompanying text.


the unhappy result accepted in the Goldrich decision; it ought not become its legacy.

Sharon L. King