

Practice Update

# Colleges' Liability for Defaulting Parents Narrowing?

March 30, 2018

Good news for colleges: Connecticut may be on the leading edge of a trend to bar bankruptcy trustees from pursuing colleges when parents default on their “Parent PLUS” loans.

When a parent signs a “Parent PLUS” loan to help her child pay for college and she later finds herself in bankruptcy, bankruptcy trustees often sue the child’s college to recover loan disbursements as a fraudulent transfer. Over the last several years, the law has allowed such claims.

Until recently, Connecticut was home to many of the most aggressive of these “Parent PLUS” claims. Although the bankruptcy cases were pending in Connecticut, trustees threatened or brought fraudulent transfer actions against schools all over the country, including at least three schools in Florida. But last year, the State of Connecticut recently outlawed these causes of action. *See* Conn. Gen. Stat. § 52-552i(f) (“A transfer or obligation is not voidable... if the transfer was made or obligation incurred by a parent or guardian on behalf of a minor or adult child in furtherance of the child’s undergraduate education”). And just last month, in two decisions issued on the same day, the Connecticut Bankruptcy Court rejected two of these claims because, it found, the funds were earmarked for the schools.

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In other words, the trustees could not pursue the loan proceeds because they never actually belonged to the parents/debtors and they could not have been used to pay the parents/debtors' creditors. In making its decisions, the Connecticut Bankruptcy Court recognized a "clear consensus forming in the courts." These recent developments should be useful in defending against this type of "Parent PLUS" fraudulent transfer claim.

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