Catholic Dioceses in Bankruptcy

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The Catholic Church is coping with mass tort liability for sexual abuse of children by priests. As of September 2018, eighteen Catholic organizations have filed for relief in bankruptcy. Fifteen debtors have emerged from bankruptcy after settling with sexual abuse claimants and insurers. During settlement negotiations, sexual abuse claimants and debtors clashed over the extent of the debtors' property and ability to pay claims. Although such disputes are common in Chapter 11 plan negotiations, the Catholic cases required the parties and bankruptcy courts to account for the unique religious attributes of Catholic diocesan debtors. This Article reviews the arguments and outcomes on these issues based on reported decisions, pleadings, plans, and disclosure statements. It explains the key characteristics of Catholic dioceses under canon and secular organization law and the bankruptcy contexts in which these characteristics became hot-button issues. It offers an analysis of the legacy of the Catholic cases for bankruptcy law, religious liberty, and for the relationships among entities within a Catholic diocese.

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I. INTRODUCTION

In January 2002, the Boston Globe reported that a former priest of the Roman Catholic Archdiocese of Boston, John J. Geoghan, had been accused by more than 130 people of sexually abusing children since the mid-1990s.[1] Boston Archbishop Cardinal Bernard Law and five other bishops knew of credible accusations against Geoghan, but did nothing to warn the faithful or bar Geoghan from unsupervised access to children.[2] Six months after the story broke, the U.S. Conference of Catholic Bishops (USCCB) acknowledged responsibility for failure to protect children from clergy

[1] *See* Michael Rezendes, *Church Allowed Abuse by Priests for Years*, BOS. GLOBE (Jan. 6, 2002), http://www.bostonglobe.com/news/special-reports/2002/01/06/church-allowed-abuse-priest-for-years/cSHfGkTIrAT25qKGvBuDNM/story.html; *see also Key Stories from the Boston Globe Spotlight Team Reporting on Clergy Abuse in the Catholic Church*, BOS. GLOBE (Nov. 10, 2015), https://www.bostonglobe.com/2015/11/10/timeline-spotlight-report-stories/SGm67HGOQ7PolOSGZHxs8K/story.html. The Boston Globe investigative series won the 2003 Pulitzer Prize for Public Service. *See The Boston Globe*, PULITZER PRIZES, http://www.pulitzer.org/winners/boston-globe-1 (last visited Feb. 15, 2018). The series became the basis of the 2015 film "Spotlight." *See generally* SPOTLIGHT (Open Road Films 2015).

[2] *See* DAVID FRANCE, OUR FATHERS: THE SECRET LIFE OF THE CATHOLIC CHURCH IN AN AGE OF SCANDAL 129–48 (2004). In 2002, Geoghan was convicted and "sentenced to nine to [ten] years in prison" for indecent assault and battery against a ten-year-old boy that occurred in 1991. *Sex Abuse Priest Killed in Prison*, CNN (Feb. 23, 2004), http://www.cnn.com/2003/US/08/24/geoghan/index.html. He was killed in prison by a fellow inmate in 2004. *Id.*

sexual abuse.[3] As it turned out, the problem was not limited to the Archdiocese of Boston.

In July 2004, after efforts to settle multiple sexual abuse claims collapsed, the Archdiocese of Portland, Oregon became the first Catholic organization to seek bankruptcy protection.[4] Elizabeth Warren (then a law professor) expressed surprise that a Catholic archbishop would be willing to undergo the loss of privacy and control required of debtors in bankruptcy.[5] In retrospect, however, the resort to bankruptcy by the Archdiocese of Portland and the seventeen Catholic dioceses and religious institutes that have followed it into bankruptcy is not surprising. Sexual abuse of children

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[3] *See, e.g.*, U.S. CONFERENCE OF CATHOLIC BISHOPS, CHARTER FOR THE PROTECTION OF CHILDREN AND YOUNG PEOPLE 1 (2002), http://www.bishop-accountability.org/resources/resource-files/churchdocs/DallasCharter.pdf ("[T]he ways in which we bishops addressed these crimes and sins, have caused enormous pain, anger, and confusion."); *see also* Raymond C. O'Brien, *Clergy, Sex and the American Way*, 31 PEPP. L. REV. 363, 365–66 (2004) ("It appeared as if the Church had isolated itself from the state's concern for children, an isolation which appeared arrogant and even sinister."); Associated Press, *Scandals in the Church: Statement by President of the U.S. Catholic Bishops on Sexual Abuse*, N.Y. TIMES (June 14, 2002), http://www.nytimes.com/2002/06/14/us/scandals-church-statement-president-us-catholic-bishops-sexual-abuse.html ("We did not go far enough to ensure that every child and minor was safe from sexual abuse. . . . Both what we have done or what we have failed to do contributed to the sexual abuse of children and young people by clergy and church personnel.").

[4] *See* Doe 130 v. Archdiocese of Portland in Or., 717 F. Supp. 2d 1120, 1130 (D. Or. 2010). The Archdiocese of Portland filed for bankruptcy on the eve of jury selection in a civil sexual abuse trial involving its alleged negligent supervision of a priest who was accused of abusing more than fifty boys between 1950 and 1980. *See* Laurie Goodstein, *Oregon Archdiocese Files for Bankruptcy Protection*, N.Y. TIMES (July 7, 2004), http://www.nytimes.com/2004/07/07/us/oregon-archdiocese-files-for-bankruptcy-protection.html. Four years earlier, the Archbishop of Portland, John Vlazny, had publicly apologized for the sexual abuse of children by the Archdiocese's priests. *See Doe 130*, 717 F. Supp. 2d at 1129–30. In the year before bankruptcy, the Archdiocese paid more than $21 million to settle sexual abuse claims. *See* Letter from John G. Vlazny, Archbishop of Portland, Archdiocese of Portland in Or., to Brothers and Sisters in Christ (July 6, 2004), http://www.bishop-accountability.org/ia-davenport/bankruptcy/2004-07-06-Vlazny-Letter.htm; *see also* Goodstein, *supra*.

[5] *See* Michael Paulson, *Archdiocese Files for Bankruptcy*, SUN-SENTINEL (July 7, 2004), http://articles.sun-sentinel.com/2004-07-07/news/0407070083_1_diocese-bankruptcy-court; *see also* David A. Skeel, Jr., *Avoiding Moral Bankruptcy*, 44 B.C. L. REV. 1181, 1181 (2003) (noting that rumors that the Archdiocese of Boston might file for bankruptcy took him by surprise); Pam Belluck & Adam Liptak, *For Boston Archdiocese, Bankruptcy Would Have Drawbacks*, N.Y. TIMES (Dec. 3, 2002), http://www.nytimes.com/2002/12/03/us/for-boston-archdiocese-bankruptcy-would-have-drawbacks.html (quoting bankruptcy scholar Jay Westbrook that "[f]or the Archdiocese of Boston to [file for bankruptcy] would be stunning"). A bankruptcy filing requires the debtor to open its books to creditors, the courts, and the public, and to be subject to court supervision and public scrutiny of its financial affairs and business operations. *See, e.g.*, 11 U.S.C. §§ 341, 343 (2018) (allowing creditors to question the debtor under oath, and challenge the accuracy and completeness of the debtor's disclosure); *id.* § 1112(b)(1), (4)(G) (stating that failure to comply is grounds for dismissal of the case).

by priests had become a mass tort problem for Catholic organizations, and Chapter 11 was the obvious legal response.[6]

The Catholic bankruptcy cases put a legal spotlight on the secular and ecclesiastical relationships between a diocesan debtor and the parishes, schools, cemeteries, and other entities that operate within the diocese and under the bishop's authority. Although fights about the nature and value of a debtor's property are common in Chapter 11 cases, Catholic dioceses are not ordinary debtors. Skirmishes between sexual abuse creditors and the debtors were unusually aggressive and public. Advocates for sexual abuse claimants stoked the media with plans "to go after . . . parish assets."[7] One attorney described the push to include parish assets as a "'slugfest' [that] must occur 'before people get serious' about settlement."[8] The Catholic debtors pushed back, seeking protection from bankruptcy court-adjudication of property of the estate on religious freedom grounds. They also argued that the property rights subject to their bankruptcy cases did not include property that they attributed to parishes and other diocesan affiliates under secular and religious law.

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[6] By 2004, reorganization in bankruptcy was a common corporate response to mass tort liability. *See* Susan Chandler, *Oregon Archdiocese Takes a Page from Corporate Playbook*, CHI. TRIB. (Aug. 1, 2004), http://articles.chicagotribune.com/2004-08-01/business/0408010031_1_portland-archdiocese-portland-archbishop-john-vlazny-bankruptcy-judge-elizabeth-perris (analogizing sex abuse claims to asbestos claims); *see also* Francis E. McGovern, *The Tragedy of the Asbestos Commons*, 88 VA. L. REV. 1721, 1754 (2002) (noting that bankruptcy is the only way an asbestos defendant could achieve complete and final disposition of claims); Georgene Vairo, *Mass Tort Bankruptcies: The Who, the Why and the How*, 78 AM. BANKR. L.J. 93, 95 (2004) (noting that use of bankruptcy by companies with asbestos liability had become "routine," and predicting use of bankruptcy as response to non-asbestos mass tort issues).

[7] Annysa Johnson, *Parishes' Assets Targeted in Archdiocese Bankruptcy Case*, MILWAUKEE J. SENTINEL (Oct. 18, 2012), http://archive.jsonline.com/news/religion/parishes-assets-targeted-in-archdiocese-bankruptcy-case-tf79a59-174875991.html ("Lawyers for sexual abuse victims . . . telegraphed [that] they intend to go after individual parish assets and proceeds from the Archdiocese's $105 million Faith in Our Future campaign."); *see also Attorneys Want Diocese to Claim Ownership*, SIOUX CITY J. (Oct. 25, 2006), http://siouxcityjournal.com/news/state-and-regional/attorneys-want-diocese-to-claim-ownership/article_9b3d7893-3846-5949-8a5b-859e80ece7dd.html (reporting that lawyers for sexual abuse claimants said that separately incorporated parishes should contribute their property to pay claims, and that they "believe the bishop controls the parishes"); Goodstein, *supra* note 4.

[8] *E.g.*, Donald L. Swanson, *Don't Let This Happen to You: Milwaukee Archdiocese Bankruptcy - Part Three: The In-Court "Slugfest,"* MEDIATBANKRY (May 5, 2016), https://mediatbankry.com/2016/05/05/dont-let-this-happen-to-you-milwaukee-archdiocese-bankruptcy-part-three-the-in-court-slugfest/; *see also* Listecki v. Official Comm. of Unsecured Creditors (*In re* Archdiocese of Milwaukee), 496 B.R. 905, 912 (E.D. Wis. 2013) (noting that decision regarding the fate of the Cemetery Trust litigation "will shape the course of future proceedings in bankruptcy"), *rev'd*, 780 F.3d 731 (7th Cir. 2015).

As of September 2018, of the eighteen organizations that filed for bankruptcy protection, fifteen (seven dioceses, six archdioceses, and two religious institutes) have emerged from bankruptcy after confirming consensual plans.[9] The Archdiocese of San Diego settled with its creditors and dismissed its Chapter 11 case about six months after filing.[10]

This Article considers the arguments and outcomes on property issues in the Catholic bankruptcy cases. Part II explains the unique legal characteristics of Catholic dioceses as debtors in bankruptcy under canon law and secular organizational law. Part III explains the conflicts between advocates for sexual abuse creditors and the debtors over the nature and extent of the debtors' property. Part IV considers the contexts and outcomes of litigation about the debtors' right to religious liberty under the First Amendment and the Religious Freedom Restoration Act (RFRA). Part V looks briefly at the issues that arose in the battle of competing plans in the Saint Paul and Minneapolis case. Part VI reflects on the effects of the Catholic diocesan bankruptcy cases on bankruptcy law, religious liberty, and the relationships among bishops, dioceses, parishes and other entities within the hierarchy of the Catholic Church.

II. CATHOLIC DIOCESES AS DEBTORS

A. *Canon Law*

Bankruptcy cases of non-profit religious organizations are not unusual.[11] The Catholic diocesan debtors, however, are unique among non-profit organizations in bankruptcy because of their affiliation with the Catholic Church. The Church is a worldwide community established over two thousand years ago by Jesus Christ with about 1.25 billion members who hold a common religious creed.[12] The 1983 Code of Canon Law ("canon

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[9] *See* Marie T. Reilly & Rebecca A. Mattson, *Catholic Dioceses in Bankruptcy*, PENN STATE LAW ELIBRARY, https://elibrary.law.psu.edu/bankruptcy/ (last visited Mar. 1, 2019) (archive of plans, disclosure statements, and other selected documents collected from public dockets in the Catholic bankruptcy cases).

[10] *Id.*

[11] *See* Pamela Foohey, *When Churches Reorganize*, 88 AM. BANKR. L.J. 277 (2014); Pamela Foohey, *When Faith Falls Short: Bankruptcy Decisions of Churches*, 76 OHIO ST. L.J. 1319 (2015).

[12] *See* U.S. CONF. OF CATH. BISHOPS, CATECHISM OF THE CATHOLIC CHURCH ¶ 862 (2d ed. 2000); *The Pontifical Yearbook 2017 and the "Annuarium Statiscum Ecclesiae" 2015*, HOLY SEE PRESS OFF. BULL. (June 4, 2017), http://press.vatican.va/content/salastampa/en/bollettino/pubblico/2017/04/06/170406e.html; Michael Lipka, *A Closer Look at Catholic America*, PEW RES. CTR. (Sept. 14, 2015), http://www.pewresearch.org/fact-tank/2015/09/14/a-closer-look-at-catholic-america/ (about twenty percent of adults residing in the United States report that their primary religious affiliation is Roman Catholic); Cindy Wooden, *Global Catholic Population Tops 1.28 Billion; Half Are in 10 Countries*, NAT'L CATH. REP. (Apr. 8, 2018), https://www.ncronline.org/news/world/global-catholic-

law") governs the conduct of all Catholics.[13] It establishes the internal organizational structure and procedures of the Catholic Church and the property rights and agency relationships of entities within the Church.[14]

Canon law describes the Catholic Church as a complete community.[15] Yet, the Church operates within a distinct secular community, which is subject to secular law. Canon law acknowledges secular law and requires that Catholics must comply with it, except for secular laws that are contrary to divine law[16] or when canon law expressly supersedes it.[17] For example, canon law expressly supersedes civil law on the right of the Church to preach the Gospel and to "announce moral principles, even about the social order . . . ."[18] Conversely, canon law adopts secular law on certain matters, including general and specific regulations on contracts and payments subject to divine law or conflicting canon law.[19] As to most of the matters that secular law regulates, however, canon law is silent.[20] In particular, canon law has nothing to say about the rights of creditors of Catholic organizations against the organizations or their property.

The Catholic Church is not a universal, monolithic corporate organization. Nor is it a Pope-led kingdom with absolute, downward hierarchy, as many suppose. The Church operates through a central leader, the Pope, and through its "particular churches," regional entities including

population-tops-128-billion-half-are-10-countries.

[13] *See generally* 1983 CODE C.11 (ecclesiastical law binding on all baptized Catholics over seven years of age). Catholics are also bound by divine law, revealed in scripture or tradition. *Id.* C.750. Catholics who follow the Eastern Rite follow the 1990 Code of Canons of the Eastern Churches. *See generally* CODE OF CANONS OF THE EASTERN CHURCHES (1990), https://orthocath.files.wordpress.com/2010/01/1990_code_of_canons_of_the_eastern_churc hes.pdf.

[14] *See* 1983 CODE C.96–144; *id.* C.330-572*; id.* C.1259–1310.

[15] *See* Jacques Maritain, *The Catholic Church and Social Progress*, FOREIGN AFF. (July 1, 1939), https://www.foreignaffairs.com/articles/1939-07-01/catholic-church-and-social-progress.

[16] Divine law, also known as natural law, is law enacted by God and made known to man through revelation. *See generally* JEAN PORTER, NATURAL AND DIVINE LAW: RECLAIMING THE TRADITION FOR CHRISTIAN ETHICS (1999); *Moral Aspect of Divine Law*, NEW ADVENT, www.newadvent.org/cathen/09071a.htm (last visited Mar. 1, 2019).

[17] *See* 1983 CODE C.22.

[18] *See, e.g.*, *id.* C.747, § 1 ("The Church . . . has the duty and innate right, independent of any human power whatsoever, to preach the gospel to all peoples.").

[19] *See id.* C.1290. The Catechism of the Catholic Church provides that Catholics are morally bound to observe legitimate secular laws but must disobey laws that are "contrary to the demands of the moral order, to the fundamental rights of persons or the teachings of the Gospel." U.S. CONF. OF CATH. BISHOPS, CATECHISM OF THE CATHOLIC CHURCH 541 c.2242 (2d ed. 2016); *see also* NEW COMMENTARY ON THE CODE OF CANON LAW 84 (John P. Beal et al. eds., 2000) [hereinafter NEW COMMENTARY ON CANON LAW].

[20] NEW COMMENTARY ON CANON LAW, *supra* note 19, at 85.

archdioceses, dioceses, parishes, and religious institutes.[21] Dioceses are geographic areas.[22] An archdiocese is a large diocese[23] in terms of the numbers of Catholics residing within it, and usually covers a large metropolitan area.[24] Residing and operating within the geographic boundaries of a diocese are communities of Catholic faithful known as parishes.[25] Religious institutes are groups of individuals (e.g., priests, nuns, brothers) who undertake certain vows and agree to live in community with other members under a common order or tradition.[26] A religious institute operates independently of a diocese, however, on religious matters, individual members are subject to the authority of the bishop of the diocese in which they reside.[27]

Canon law recognizes corporate agency for entities distinct from the persons who comprise them.[28] Indeed, corporate agency as a legal construct may have originated in early Roman Catholic canon law.[29] Canon law calls

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[21] *See* 1983 CODE C.368–430. The most common form of a particular church is a diocese. NEW COMMENTARY ON CANNON LAW, *supra* note 19, at 506.

[22] *See* 1983 CODE C.369 (a diocese is "a portion of the people of God which is entrusted [for pastoral care] to a bishop . . ."); *see also Diocese and Bishop Addresses*, U.S. CONF. OF CATH. BISHOPS, www.usccb.org/about/bishops-and-dioceses/all-dioceses.cfm (last visited March 1, 2019) (listing of archdioceses and dioceses in the U.S.)

[23] Hereafter, unless the context indicates, "diocese" refers to archdiocese or diocese.

[24] An archdiocese may also be referred to as a "metropolitan see." A "see" is an ecclesiastical province that includes the archdiocese and "suffrage" dioceses within the ecclesiastical province that are also under the authority of the archbishop. *See* 1983 CODE C.431, § 1, C.435, C.436. An archbishop has authority over his own diocese and as the head of the metropolitan see has certain responsibilities to the suffrage dioceses within the see. *See id.* C.473, §1. For example, the Roman Catholic Archdiocese of New York is the metropolitan see of the ecclesiastical province of New York which includes the suffragan dioceses of Albany, Brooklyn, Buffalo, Ogdensburg, Rochester, Rockville Centre and Syracuse. *See* Ecclesiastical Province, *Catholic Dioceses in United States of America*, GCATHOLIC.ORG, http://www.gcatholic.org/dioceses/country/US-province.htm (last visited Mar. 1, 2019). Each diocese is a "particular church" within the "universal church." 1983 CODE C.368; *see also* JOHN J. COUGHLIN, CANON LAW: A COMPARATIVE STUDY WITH ANGLO-AMERICAN LEGAL THEORY 118 (2011). Along with dioceses, juridic entities such as territorial prelatures, abbacies, apostolic vicarates, and prefactures are also "particular churches." 1983 CODE C.368; *see also* HENRI DE LUBAC, *Particular Churches in the Universal Church*, *in* THE MOTHERHOOD OF THE CHURCH 191–211 (Sergia Englund trans., 1983).

[25] *See* 1983 CODE C.515, § 1 ("A parish is a certain community of the Christian faithful stably constituted in a particular church"); *id.* C.374, § 1 ("Every diocese . . . is . . . divided into parishes").

[26] *See id.* C.607, § 2. *See generally* Sister Cecilia Meighan, *Religious Institutes—Property and Tax Issues*, 33 CATH. LAW. 25 (1990). Some religious institutes are authorized by the pope (known as "pontifical right" institutes), and are thus under the authority of the pope rather than the bishop of the geographic diocese in which the institute is located. *Id.* at 25–26.

[27] *See* 1983 CODE C.678, § 1; *see also id.* C.680 (providing for cooperation among institutes and between institute and diocesan clergy under the direction of the bishop).

[28] *See* NEW COMMENTARY ON CANON LAW, *supra* note 19, at 154–55.

[29] *See* John Dewey, *The Historic Background of Corporate Legal Personality*, 35 YALE

entities with such agency "juridic persons."[30] Dioceses, and diocesan-affiliated entities such as parishes, schools, cemeteries, special purpose trusts are all public juridic persons with distinct agency under canon law.[31]

With respect to property rights, canon law recognizes a distinction between ecclesiastical property (the Church's property) and non-ecclesiastical property. "[O]wnership of goods belongs to that juridic person which has acquired them legitimately."[32] All property legitimately acquired by a public juridic person is ecclesiastical property, whereas property acquired by individual persons is not.[33] For example, a monetary contribution by an individual to his or her parish becomes ecclesiastical property once the parish, as juridic person, acquires it.[34] Property that belongs to one juridic person cannot simultaneously belong to another juridic person.[35]

A juridic person's "ownership" of property is limited by canon law, which establishes a hierarchy of authority among juridic persons. The authority of juridic persons within the Church is generally, but not perfectly,

L.J. 655, 665 (1926) (attributing the legal concept of *persona ficta* to Pope Innocent IV who used it to afford monasteries continuous and separate existence from the monks).

[30] *See* 1983 CODE C.113, § 2 ("[B]esides physical persons, there are also juridic persons, that is, subjects in canon law of obligations and rights which correspond to their nature."). Juridic persons have the "innate right . . . to acquire, retain, administer and alienate temporal goods independently of civil power." *Id.* C.1254, § 1. In contrast to a juridic person, a "moral person" is a group of individuals, or assets, with a common purpose but without a canonical legal personae distinct from the persons who comprise it. *See* NEW COMMENTARY ON CANON LAW, *supra* note 19, at 154–55; *see also* 1983 CODE C.310 (A private association not established as a juridic person has no agency of its own, but individual members of the association can "jointly contract obligations and can acquire and possess rights and goods as co-owners and co-possessors"). Goods held jointly by a private association are not "ecclesiastical goods" and are not subject to canonical norms regulating such goods. *See* 1983 CODE C.1257; *id.* C.515, § 3 (stating the same as to parishes); *id.* at C.373 (stating the same as to diocese); *id.* C.634, § 1 (stating the same as to religious orders); NEW COMMENTARY ON CANON LAW, *supra* note 19, at 408.

[31] *See* 1983 CODE C.116, § 1. A juridic person founded to serve the public good is a "public juridic person." *Id*. Hereafter, all juridic persons within a diocese shall be referred to collectively as "parishes" for simplicity.

[32] *Id.* C.1256.

[33] *See id.* C.1257, § 1 ("All temporal goods which belong to the universal Church, the Apostolic See, or other public juridic persons in the Church are ecclesiastical goods and are governed by the following canons and their own statutes."); *see also id.* C.1254–1310 (regulating the purchase, ownership, administration, and sale of Church property by juridic persons to whom it belongs).

[34] *See id.* C.1267, § 1 (offerings given to an administrator of a public juridic person are presumed to be offerings to the public juridic person the individual administers); *id.* C.1267, § 3 ("Offerings given by the faithful can" only be used for the purpose for which they were given).

[35] *See* ADAM J. MAIDA & NICHOLAS P. CAFARDI, CHURCH PROPERTY, CHURCH FINANCES, AND CHURCH-RELATED CORPORATIONS: A CANON LAW HANDBOOK 26 (1983) ("[A]ll property is the property of one public juridic person or another.").

hierarchical. The Pope is the bishop of Rome, successor in that position to Saint Peter.[36] The Pope appoints bishops for each diocese.[37] The bishop has authority over each parish within the geographic boundaries of the diocese.[38] In turn, the bishop appoints a pastor, typically a priest, to manage a parish.[39]

As noted above, canon law recognizes ownership of property in the juridic person who acquired it.[40] At the same time, that property is typically administered by a juridic person senior in the hierarchy, for the benefit of the juridic person.[41] The Pope has plenary authority over all ecclesiastical goods.[42] The bishop is the administrator for property belonging to the diocese, the juridic person that the bishop administers.[43] The bishop does not administer parish property—rather, a pastor (appointed by the bishop) "exercises direct power of governance" over the parish[44] and administers the property belonging to the parish.[45] The bishop's role with respect to parish property is indirect through his authority over the pastor who administers it. The bishop is "to exercise careful vigilance over the administration of all goods which belong to public juridic persons subject to him . . . ."[46]

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[36] *See Roman Catholicism: Structure of the Church*, ENCYCLOPAEDIA BRITANNICA https://www.britannica.com/topic/Roman-Catholicism/Structure-of-the-church (last visited Feb. 11, 2019).

[37] 1983 CODE C.377, § 1; Pope Paul VI, *Christus Dominus: Decree Concerning the Pastoral Office of Bishops in the Church*, HOLY SEE PRESS OFF. BULL. (Oct. 28, 1965), http://www.vatican.va/archive/hist_councils/ii_vatican_council/documents/vat-ii_decree_19651028_christus-dominus_en.html.

[38] 1983 CODE C.515.

[39] *Id.* C.515, § 1 ("[P]astoral care is entrusted to a pastor . . . under the authority of the diocesan bishop."); *see also* NEW COMMENTARY ON CANON LAW, *supra* note 19, at 676 ("[T]he diocesan bishop . . . has authority over the pastor of each parish [within the diocese].").

[40] 1983 CODE C.1256.

[41] *Id.* c.1279, § 1; *see also* NEW COMMENTARY ON CANON LAW, *supra* note 19, at 1474.

[42] The Pope is the "supreme administrator and steward of all ecclesiastical goods." 1983 CODE C.1273.

[43] NEW COMMENTARY ON CANON LAW, *supra* note 19, at 1477.

[44] 1983 CODE C.532; THE CANON LAW SOC'Y OF GR. BRIT. & IR., THE CANON LAW LETTER AND SPIRIT: A PRACTICAL GUIDE TO THE CODE OF CANON LAW 295 (Gerard Sheehy & Francis G. Morrisey eds.,1996).

[45] 1983 CODE C.531, C.1276, C.532; *see also id.* at C.515, § 1; NEW COMMENTARY ON CANON LAW, *supra* note 19, at 1477.

[46] 1983 CODE C.1276, § 1. The bishop designates certain transactions involving parish property by type or size as extraordinary, for which the pastor must obtain the bishop's permission. *Id.* C.1281. Unlike parishes, religious institutes administer property outside the supervisory authority of the bishop of the diocese in which they are geographically located. *Id.* C.586, § 1 (acknowledging "a just autonomy of life, especially of governance . . . for individual institutes"). Members of a religious institute, however, are subject to the bishop's authority "in those matters which regard the care of souls, the public exercise of divine worship, and other works of the apostolate." *Id.* C.678, §1.

The Catholic bankruptcy cases opened wide the obvious tension between the independence of parishes from the bishop as distinct juridic persons and the bishop's indirect authority over parishes and parish property. One commenter described the question of whether parishes "own" property as an example of how extreme interpretations of canon law are either as "antinomian" or "legalistic," and concluded that to attempt to translate canon law hierarchical ownership rights into secular terms "disrupt[s] the unity of law and theology" expressed in canon law.[47] Another commenter put the issue in much plainer terms, asserting that, under canon law, "[p]arishes are not plums for the diocesan bishop to pick when he has debts to pay."[48]

B. *Organizational Law*

Not all Catholic dioceses are organized alike. The differences among them became key issues in their bankruptcy cases. State law varies on the corporate forms available to religious organizations.[49] Depending on state law, Catholic organizations may choose among corporate forms, including charitable trusts, unincorporated associations, corporation sole, religious non-profit corporations, or general non-profit corporations.[50]

In the late nineteenth and early twentieth centuries, legislatures extended special corporate sole charters for religious organizations including Catholic dioceses, which otherwise could not incorporate.[51] The corporation sole form places all the management control of the organization in a single person as agent for the corporation sole, e.g., the bishop of a Catholic diocese and his successors.[52] Like the ordinary non-profit corporate form, the

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[47] *See* COUGHLIN, *supra* note 24, at 176–79.

[48] *See, e.g.*, Nicholas P. Cafardi, *The Availability of Parish Assets for Diocesan Debts: A Canonical Analysis*, 29 SETON HALL LEGIS. J. 361, 368 (2005).

[49] *See generally* Patty Gerstenblith, *Associational Structures of Religious Organizations*, 1995 BYU L. REV. 439 (1995).

[50] *Id.* at 441–42 (discussing that a 1995 survey revealed that eighty-seven percent of religious organizations chose "the religious not-for-profit corporate form"). To qualify for tax-exempt status, a non-profit corporation's organizing documents must ensure that the "members, officers, and directors . . . do not receive any profit" from the organization's operations. *Id.* at 442. This "nondistribution constraint" is also required for federal tax-exempt status under the Internal Revenue Code. *See* 26 U.S.C. § 501(c)(3) (2018); Henry B. Hansmann, *The Role of Nonprofit Enterprise*, 89 YALE L.J. 835, 838 (1980).

[51] For example, Washington's corporation sole statute was enacted in 1915 to provide a means for religious organizations to hold title to property distinctly from their members and enjoy perpetual existence. Comm. of Tort Litigants v. Catholic Diocese of Spokane (*In re* Catholic Bishop of Spokane), 329 B.R. 304, 317 (Bankr. E.D. Wash. 2005), *aff'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, No. CV-05-0274-JLQ, 2006 U.S. Dist. LEXIS 6025 (E.D. Wash. Jan. 24, 2006), *and rev'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, 364 B.R. 81 (E.D. Wash. 2006).

[52] Statutes typically provide that the sole manager of the corporation must have been duly elected or chosen, and must act in accordance with the rules of the organization of which the manager is a part. MAIDA & CAFARDI, *supra* note 35, at 128; *see also* Tort Claimants Comm.

corporate sole form permits the survival of the corporation in perpetuity and continuous ownership of property.[53] The corporate sole form is loosely consistent with the bishop's supervisory responsibility over parishes and other juridic persons within the diocese, but it is inconsistent with recognition of parishes as juridic persons with the agency to own property distinct from the bishop.[54]

In the 1980's as state legislatures extended corporate status to non-profit religious corporations, canonists considered whether the corporate sole form continued to be appropriate, and, if so, whether parishes within corporation sole dioceses should separately incorporate and hold title to the property that canon law attributed to them. Advocates for the status quo (diocese as corporation sole with centralized title to property) lauded it as an efficient means for the bishop to use parish property as collateral for diocesan or parish projects at capital costs more favorable than could be achieved by individual parishes borrowing against parish property.[55] An author of a handbook on Church property and finance opined that a Catholic diocese could be organized variously as a corporation sole, a non-profit religious corporation, or as an entity without corporate form. He offered no guidance for a bishop to choose among these forms, or how the diocese and its parishes should hold title to property within the secular corporate structure he chose.[56] He opined blithely that secular law was irrelevant. Secular courts would apply canon law to supply the terms of implied trusts in favor of parishes "because it is that law which governs the use of these Church assets."[57] No doubt, the author was unconcerned about the prospect of diocesan bankruptcy cases.

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v. Roman Catholic Archbishop of Portland in Or. (*In re* Roman Catholic Archbishop of Portland in Or.), 345 B.R. 686, 697 (Bankr. D. Or. 2006) (finding a distinction between the Archdiocese of Portland and the "office of the Archbishop" for purposes of interpretation of an express trust, as the former is the corporate entity whereas the latter is the ecclesiastical office of the Archbishop under Canon law); Gerstenblith, *supra* note 49, at 454 (noting that, as of 1995, twenty-six states permitted incorporation of a religious organization as a corporation sole).

[53] *See, e.g.*, Cty. of San Luis Obispo v. Ashurst, 194 Cal. Rptr. 5, 8 (Ct. App. 1983) ("The creditors of the corporation sole may not look to the assets of the individual holding office, nor may the creditors of the individual look to the assets held by the corporation sole."); *see also* Gerstenblith, *supra* note 49, at 455.

[54] NEW COMMENTARY ON CANON LAW, *supra* note 19, at 164, 1457.

[55] *See* R. Kealy, *Methods of Diocesan Incorporation*, CANON LAW SOC'Y OF AM. PROCS. 163–77 (1986); *see also, e.g.*, Baxter v. McDonnell, 49 N.E. 667, 668 (N.Y. 1898) (finding that where Catholic bishop held title to an unincorporated church in his name, "[t]he purpose of this arrangement is to exclude the laity from that power of interference which they would have were the title vested in a corporation").

[56] *See* Kealy, *supra* note 55, at 163–77. In any case, the bishop holds title to parish assets "in accordance with canon law . . . as civil law trustee for the parish . . . [under] an amalgam of these individual parish trusts." *Id.*

[57] *Id.* at 131 (citing 1983 CODE C.1257).

Today, in light of the clergy sexual abuse scandal, the financial advantages of bishop-centered control over property have disappeared, swamped by the liability risk. In 2000, two years before the Archdiocese of Boston scandal broke, canon law scholars noted that organization of a diocese as a corporation sole with centralized title to property, and without separate incorporation of parishes, is "[i]ncompatible with the law of the Church [and] long ago disapproved by the Holy See."[58] Perhaps wryly, they noted that bishops and their financial officers and advisers "should make every effort to see that the laws of the Church . . . are faithfully followed."[59]

As Professors Henry Hansmann and Reinier Kraakman have recognized, organizational law defines the set of assets to which an organization's creditors have recourse and shields from those creditors other property not within that set.[60] Unlike canon law, which governs rights and relationships *among* juridic persons within the Church, a bankruptcy proceeding reveals the external effect of secular organizational law on the organization's creditors. In no other legal setting is scrutiny of organizational form, property rights, and agency more energetically undertaken.

III. PARISH PROPERTY AS PROPERTY OF THE ESTATE

A. *Property of the Estate Basics*

Consider the importance of property of the estate issues in bankruptcy cases generally. In a Chapter 7 case, the trustee for the estate marshals, liquidates, and distributes property of the estate to creditors in satisfaction of the debtor's pre-petition debts[61] In contrast, in a Chapter 11 case, the debtor and creditors engage in bankruptcy court-supervised negotiation towards a plan of reorganization that can preserve at least some of the debtor's going concern value, settle creditors' claims, and provide for discharge of pre-petition debts.[62]

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58 NEW COMMENTARY ON CANON LAW, *supra* note 19, at 164 (footnote omitted).

59 *Id.* at 164, 1457.

60 Henry Hansmann & Reinier Kraakman, *The Essential Role of Organizational Law*, 110 YALE L.J. 387, 390 (2000) ("[T]he essential role of all forms of organizational law is to provide for the creation of a pattern of creditors' rights—a form of 'asset partitioning'—that could not practicably be established otherwise." (footnote omitted)).

61 *See* 11 U.S.C. § 501 (2018) (claims allowance process); *id.* § 506 (secured claims); *id.* § 507 (priority among unsecured creditors); *id.* § 725 (distribution of property to holders of secured claims; *id.* § 726 (priority of distribution of property of the estate.).

62 *See Chapter 11 - Bankruptcy Basics*, U.S. CTS., http://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-11-bankruptcy-basics (last visited Aug. 15, 2018).

Property of the estate issues frame negotiation among the parties in a Chapter 11 case.[63] Among other requirements, to confirm a plan of reorganization over the objection of a creditor, a Chapter 11 plan of reorganization must provide a payout to the objecting creditor with a present value at least equal to the payout that creditor would receive upon liquidation of property of the estate in a hypothetical Chapter 7 case.[64] This confirmation requirement is called the "best interest test." It protects a dissenting creditor from the consequences of a Chapter 11 plan if the plan payout is not in its "best interest' relative to the alternative hypothetical Chapter 7 liquidation payout.[65] To satisfy the requirement, the disclosure statement accompanying a plan must provide a hypothetical valuation of property of the estate so creditors can determine whether the plan satisfies the test.[66] Given the best interest test, the more property included within the estate and the greater its value, the more leverage for unsecured creditors in the Chapter 11 plan negotiation.[67]

The legal contexts in which property of the estate issues arose in the Catholic bankruptcy cases differed depending on the debtor's organizational structure, the organizational structure of parishes within the diocese subject to the bishop's canonical authority, and the respective rights of the debtors and parishes in property under secular law.

Filing a petition in bankruptcy creates an estate that includes, with certain exceptions, "all legal or equitable interests of the debtor in property as of the commencement of the case."[68] Section 541 defines "[p]roperty of

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[63] To confirm a plan in a Chapter 11 case, the plan must meet the requirements of § 1129. If the debtor is a non-profit corporation, any "transfers of property under the plan shall be made in accordance with any applicable provisions of nonbankruptcy law that govern the transfer of property." 11 U.S.C. § 1129(a)(16) (2018).

[64] *Id.* § 1129(a)(7).

[65] *Id.* A Chapter 11 plan proponent ordinarily must include a hypothetical liquidation analysis in the disclosure statement accompanying the plan so that creditors can determine if the proposed plan is in their best interest. *Id.* § 1125(b) (to solicit votes on a plan, the plan proponent must provide a disclosure statement containing "adequate information"); *In re* Roman Catholic Archbishop of Portland in Or., No. 04-37154, 2007 Bankr. LEXIS 1180, at *19–20 (Bankr. D. Or. Apr. 13, 2007) (finding that the plan provided that the objecting creditors would be paid in full, so no hypothetical liquidation analysis was required); CHARLES JORDAN TABB, THE LAW OF BANKRUPTCY 1123–24 (2d ed. 2009) (observing that most disclosure statements include a hypothetical liquidation analysis).

[66] § 1125(a)–(b).

[67] *See, e.g.*, Comm. of Tort Litigants v. Catholic Diocese of Spokane (*In re* Catholic Bishop of Spokane), 329 B.R. 304, 317 (Bankr. E.D. Wash. 2005), *aff'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, No. CV-05-0274-JLQ, 2006 U.S. Dist. LEXIS 6025 (E.D. Wash. Jan. 24, 2006), *and rev'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, 364 B.R. 81 (E.D. Wash. 2006) ("Resolution of this adversary proceeding in favor of the plaintiff would result in the debtor having more assets with which to pay the claims held by the members of the plaintiff.").

[68] 11 U.S.C. § 541(a)(1) (2018) ("The commencement of a case . . . creates an estate . . .

the estate;" state law defines what rights qualify for the status of "a legal or equitable interest of the debtor in property."[69]

Although the definition of property of the estate in § 541 is straightforward, application of § 541 is complicated because property rights are complicated. The general rule under bankruptcy law is that parties who hold rights in property of the estate maintain their rights notwithstanding the debtor's bankruptcy. For example, a creditor with a valid security interest in property of the estate with priority over the estate's interest in that property under state law is generally entitled to priority of its interest over the estate's interest in that property.[70] Similarly, a third party who holds a valid beneficial interest in property subject to a trust under which the debtor holds legal title maintains that beneficial interest in property notwithstanding the debtor's bankruptcy. Only the debtor's legal title to property becomes property of the estate; the third party's beneficial interest in the property does not.[71]

The Archdiocese of Portland and the Dioceses of Tucson, Spokane, San Diego, Fairbanks, Gallup, Stockton, Helena and Great Falls-Billings were organized as corporations sole at the time of their filings.[72] Except for those within the Diocese of Stockton, the parishes were not separately incorporated.[73] The respective bishops, as the lone agents for the

comprised of all of the following property, wherever located and by whomever held: (1) [subject to certain exceptions,] all legal or equitable interests of the debtor in property as of the commencement of the case."). The estate also includes property the trustee recovers by exercise of the statutory powers. *Id.* § 541(a)(3), (4). Section 541(b) excludes certain of the debtor's property interests from the estate and thereby protects such interests from creditors' claims. *Id.* § 541(b). Hereafter, all references to section numbers refer to Chapter 11 of the United States Code, unless otherwise indicated.

[69] *See id.* § 541(a); Butner v. United States, 440 U.S. 48, 55 (1979), *superseded in part by statute*, Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, 108 Stat. 4106 (codified at 11 U.S.C §§ 100–112 (2018)), *as recognized in* Airadigm Commc'ns, Inc. v. FCC (*In re* Airadigm Commc'ns, Inc.), 519 F.3d 640 (7th Cir. 2008); Tort Claimants Comm. v. Roman Catholic Archbishop of Portland in Or. (*In re* Roman Catholic Archbishop of Portland in Or.), 335 B.R. 842, 854 (Bankr. D. Or. 2005) (noting that § 541 defines property of the estate, but state law defines what is property).

[70] 11 U.S.C. § 724(b)(1) (2018).

[71] § 541(d) ("Property in which the debtor holds . . . only legal title . . . becomes property of the estate . . . only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold."); *see, e.g.*, Hunter v. St. Vincent Med. Ctr. (*In re* Parkview Hosp.), 211 B.R. 619 (Bankr. N.D. Ohio 1997) (finding a fund that was subject to a charitable trust excluded from debtor's estate under § 541(d)).

[72] *See infra* Appendix A: Case Information (listing corporate form for each debtor based on information provided by debtors in disclosure statements).

[73] *Id.* Although the Diocese of Stockton was organized as a corporation sole, each of the parishes were also organized as separate corporations sole. *See In re* Roman Catholic Bishop of Stockton, No. 14-20371, 2017 WL 118013, at *5 (Bankr. E.D. Cal. Jan. 10, 2017); Debtor's Disclosure Statement Regarding Plan of Reorganization at 12, *In re* Roman Catholic Bishop

corporations soles, were the record title holders to all ecclesiastical property without differentiation as to whether it "belonged" to the diocese or to the parishes under canon law.

The Archdioceses of Milwaukee, Saint Paul and Minneapolis, and the Dioceses of Davenport, Wilmington, Stockton, Helena, Duluth, New Ulm, and Great Falls-Billings were organized as non-profit or religious corporations at the time of filing.[74] Within these archdioceses and dioceses, parishes and other affiliated entities were separately incorporated and held record title to property.[75] The three religious institute debtors, (Oregon Province, Society of Jesus (the Jesuits), Christian Brothers of Ireland, New York and Crosier Fathers and Brothers), were all organized as non-profit corporations. One of these debtors, the Oregon Province, Society of the Jesus, was comprised of individual communities, many of which were not separately incorporated.[76]

For debtors organized as corporations sole with title to property centralized in the bishop, the debtors asserted that they held only legal title to certain property in trust for parishes, schools, cemeteries or other juridic persons whose separate interests the bishop must safeguard and respect under canon law. Sexual abuse claimants argued that state law and the Bankruptcy Code exclusively governed property rights, effectively stripping parishes of any rights in property formally titled in the bishop's name, notwithstanding their beneficial "ownership" of property under canon law.

Sexual abuse creditors used a reverse strategy in cases of debtors organized as religious corporations with separately incorporated parishes with their own legal title to property. In these cases, the debtors did not include in their estates property titled in the names of separately incorporated parishes. Sexual abuse creditors tried to capture parish property into the debtors' estates using a variety of legal arguments, all of which elevated the substance of the bishop's canonical authority over parishes and their

of Stockson, No. 14-20371 (Bankr. E.D. Cal. Jan. 15, 2014); *see also In re Roman Catholic Archbishop of Portland in Or.*, 335 B.R. at 849; Comm. of Tort Litigants v. Catholic Diocese of Spokane (*In re* Catholic Bishop of Spokane), 329 B.R. 304, 310 (Bankr. E.D. Wash. 2005), *aff'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, No. CV-05-0274-JLQ, 2006 U.S. Dist. LEXIS 6025 (E.D. Wash. Jan. 24, 2006), *and rev'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, 364 B.R. 81 (E.D. Wash. 2006).

[74] *See infra* Appendix A: Case Information.

[75] *Id.* Parishes within the Diocese of Stockton held title to property separately from the diocese. Although the Diocese of Stockton was organized as a corporation sole, parishes within the diocese were organized separately as corporations sole yielding a decentralized property structure analogous to that in dioceses organized as religious corporations with separately incorporated parishes. *See In re Roman Catholic Bishop of Stockton*, 2017 WL 118013.

[76] *See* Disclosure Statement Regarding First Modified Joint Plan of Reorganization at 20–24, *In re* Soc'y of Jesus, Or. Province, No. 3:09-bk-30938 (Bankr. D. Or. 2011).

property over parishes' independent corporate status and separate title to property under secular law.

B. *Corporations Sole*

Debtors organized as corporations sole listed in their schedules all property titled in the name of the bishop. They asserted that the bishop's title to property attributed to parishes under canon law was subject to a trust in favor of the parishes to whom the property belonged under canon law. Because parish property was subject to a trust in favor of the parishes, it was not included in the estate under § 541(d).[77] For parishes (not separately incorporated) to hold a valid beneficial interest in property, however, they had to have the legal capacity to hold title to it.

The Diocese of Tucson asserted that the closest analogy for the legal status of its parishes was unincorporated associations.[78] The diocese noted that Arizona law does not recognize legal agency for an unincorporated association to own property and, for that reason, the diocese held title to parish property.[79] Even so, it asserted, "the Diocese does not have any equitable, beneficial or proprietary interest in the Parish Real Property."[80]

Unsecured creditors' committees representing sexual abuse claimants in both the Spokane and Portland cases objected to their respective debtor's trust theories regarding parish property.[81] In particular, they argued that the alleged trusts were invalid under state law and not entitled to respect under bankruptcy law.[82] The stakes were high. Attorneys for sexual abuse

[77] In *In re Archbishop of Portland in Or.*, the debtor asserted that, "although it holds legal title to approximately $98 million in deposits and investment accounts and an extensive amount of real estate, most of that property is held in trust." 335 B.R. at 848. In *In re Catholic Bishop of Spokane*, the debtor similarly asserted that, with certain exceptions, property listed on its schedules was held for the benefit of parishes, schools, cemeteries, and other diocesan entities. 329 B.R. at 310. The Diocese of Spokane explained in its Statement of Financial Affairs that the diocese "has no equitable beneficial or proprietary interest in this [parish] property, but, in some cases, holds mere legal title[,]" and also that some property "is subject to a restriction imposed by the donor or grantor." *Id.*

[78] Third Amended and Restated Disclosure Statement Regarding Plan of Reorganization at 31, *In re* Roman Catholic Church of the Diocese of Tucson, No. 4:04-bk-04721-JMM (Bankr. D. Ariz. 2005).

[79] *Id.*

[80] *Id.*

[81] *See* Comm. of Tort Litigants v. Catholic Diocese of Spokane, No. CV-05-0274-JLQ, 2006 U.S. Dist. LEXIS 6025, at *3–4 (E.D. Wash. Jan. 24, 2006); *In re Archbishop of Portland in Or.*, 335 B.R. at 848. In *Catholic Diocese of Spokane*, the district court affirmed the bankruptcy court's conclusion that the tort claimants' committee had standing to challenge by adversary action the debtor's characterization of property of the estate. 2006 U.S. Dist. LEXIS 6025, at *15.

[82] In *In re Archbishop of Portland in Or.*, the sexual abuse claimants' committee sought a declaration that property listed on the debtors' schedules was "held in trust" for parishes was property of the estate free of any third-party interests. 335 B.R. at 848. In *In re Catholic*

claimants in the Portland case estimated that including property the debtor attributed to trusts in favor of 124 diocesan parishes and schools would yield an estate of about $500 million dollars compared to assets valued at about $19 million which debtor had scheduled as property of the estate.[83]

In both cases, the parishes organized into informal committees with standing to intervene in the adversary actions over property of the estate.[84] In the Spokane case, parishes contended that the diocese held the disputed property in a constructive trust either for their benefit or for the benefit of individual parishioners.[85] The court rejected the contention that *parishioners* could hold a beneficial interest in parish property. Even though parishioners made gifts to their parishes with the understanding that the parish would use the gifts exclusively for the parish, the donor parishioners acquired no property interest in the gifted property.[86] As to whether *parishes* could be beneficiaries of a constructive trust, the threshold question was the legal status of parishes as entities distinct from the debtor. The bankruptcy court assumed without deciding that the parishes were distinct legal entities.[87] Even so, there could be no constructive trust in favor of parishes because the deeds that named the bishop as sole title holder were the exclusive source of evidence of title. The court declined to consider the affidavit evidence from pastors, parishioners, and other benefactors in support of a constructive trust for parishes.[88] It entered partial summary judgment in favor of the creditors'

Bishop of Spokane, the committee challenged the debtors' characterization of twenty-two parcels of real property as held in trust for parishes, and moved for an order consolidating the non-debtor defendants with the debtor. 329 B.R. at 310–11.

[83] *See* Steve Woodward, *Class Action Possible in Church Case*, OREGONIAN (May 26, 2005), http://www.bishop-accountability.org/news2005_01_06/2005_05_26_Woodward_ClassAction.htm; *see also* Joe Feuerherd, *Portland Bankruptcy Seen as High-Risk Strategy*, NAT'L CATH. REP. (July 30, 2004) (noting that archdiocesan attorneys reported at a hearing $100 million in investment accounts, most held for the accounts of parishes and affiliated entities). In the Tucson case, the diocese was smaller (seventy-five parishes), but the differential was proportionately large. Sexual abuse claimants estimated the value of property of the estate, including parish property, at $110 million dollars compared with $16 million listed by the diocese. *See* Stephanie Innes, *Diocese Files Bankruptcy*, ARIZ. DAILY STAR (Sept. 21, 2004), https://tucson.com/lifestyles/faith-and-values/diocese-files-bankruptcy/article_87a37557-4fc0-5da5-b408-bef688bef24d.html; Stephanie Innes, *Diocese Set to Split with Its Parishes*, ARIZ. DAILY STAR (Sept. 23, 2004), http://www.bishop-accountability.org/news2004_07_12/2004_09_23_Innes_DioceseSet.htm.

[84] *In re Archbishop of Portland in Or.*, 335 B.R. at 848–49; *In re Catholic Bishop of Spokane*, 329 B.R. at 331; *see also* Theresa J. Pulley Radwan, *Keeping the Faith: The Rights of Parishioners in Church Reorganizations*, 82 WASH. L. REV. 75, 91–110 (2007).

[85] *In re Catholic Bishop of Spokane*, 329 B.R. at 329 n.8.

[86] *Id.* at 330 (citing RESTATEMENT (SECOND) OF TRUSTS § 25 cmt. a, § 125, § 37 cmt. a (AM. LAW INST. 1959)).

[87] *Id.* at 330–31; *see also* Comm. of Tort Litigants v. Catholic Diocese of Spokane, 364 B.R. 81, 91 (E.D. Wash. 2006) (noting that the bankruptcy court's assumption was "correct" and that "the Parishes are unincorporated associations").

[88] *In re Catholic Bishop of Spokane*, 329 B.R. at 331; *see also In re Catholic Diocese of*

committee, finding that the disputed parish real property was property of the estate free of any trust.[89] Even if the parishes could establish a trust in their favor under Washington law, because constructive or resulting trusts are equitable remedies, the parishes' interest was at best an "inchoate right" as of the filing of the petition and not a beneficial interest in property distinct from the estate's interest.[90] Finally, even if under Washington law a constructive or resulting trust was a property interest, it was unrecorded and therefore subject to the trustee's power to avoid unrecorded interests under § 544(a)(3).[91] The decision was a stunning and significant setback for the Diocese of Spokane, and for Catholic dioceses organized as corporations sole with similarly centralized title to property.[92]

Ten months later, the district court reviewing *de novo* reversed.[93] It found issues of fact on the validity of a trust in favor of parishes under Washington law based on the distinction between constructive trust and a resulting trust.[94] A constructive trust arises as a remedy for fraud by the title holder on the constructive trust beneficiary.[95] In contrast, a *resulting* trust arises in favor of the person who paid to acquire property (the beneficiary) when a title to property is conveyed to a record title holder who is someone

Spokane, 364 B.R. at 91 (noting that the bankruptcy court did not consider the affidavit testimony).

89 *In re Catholic Bishop of Spokane*, 329 B.R. at 333.

90 *Id.* at 332 (citing Airwork Corp. v. Markair Express, Inc. (*In re* Markair, Inc.), 172 B.R. 638, 642 (B.A.P. 9th Cir. 1994)).

91 11 U.S.C. § 544(a)(3) (2018); *In re Catholic Bishop of Spokane*, 329 B.R. at 333 (recognizing that the debtor in possession can exercise the trustee's power to avoid unrecorded interests in real property and that the court could grant derivative standing to exercise that power to the creditors' committee). The trustee's strong arm power to avoid unperfected interests in property reinforces state law that requires public notice of non-possessory property interests (for example, real property recording laws and public filing requirements for personal property security interests). *See generally* David Gray Carlson, *The Trustee's Strong Arm Power Under the Bankruptcy Code*, 43 S.C. L. REV. 841 (1991).

92 *See, e.g.*, Joe Feuerherd, *Diocesan Bankruptcies Raise Church Ownership Issues*, NAT'L CATH. REP. (Sept. 9, 2005), www.natcath.org/NCR_Online/archives2/2005c/090905/090905a.php ("The settlement dollars just went up dramatically . . . and the claimants hold all the cards." (quoting Sam Gerdano, Exec. Dir. of the Am. Bankr. Inst.)); Seattle Times Staff, *Bankruptcy Judge Rules Parish Assets Available to Victims*, SEATTLE TIMES (Aug. 26, 2005), https://www.seattletimes.com/seattle-news/bankruptcy-judge-rules-parish-assets-available-to-victims/ (reporting that "Barbara Blaine, president of the Survivors Network of those Abused by Priests ("SNAP"), said . . . that she hoped the ruling would prompt leaders of other dioceses to stop fighting victims").

93 *In re Catholic Diocese of Spokane*, 364 B.R. at 91, 95.

94 *Id.* at 92–95.

95 *E.g.*, Harris Tr. & Sav. Bank. v. Saloman Smith Barney, Inc., 530 U.S. 238, 250–51 (2000) ("Whenever the legal title to property is obtained through means or under circumstances 'which render it unconscientious for the holder of the legal title to retain and enjoy the beneficial interest, equity impresses a constructive trust on the property thus acquired in favor of the one who is truly and equitably entitled to the same . . . .'" (quoting 2 J. POMEROY, EQUITY JURISPRUDENCE § 103, 628-29 (1886).

other than that person (the trustee).[96] Washington courts recognize a resulting trust based on the circumstances of the conveyance of title, and not exclusively based on the deed.[97] The district court came close to calling the bankruptcy court's disregard of the affidavit evidence the parishes had submitted absurd—if only the record of title is relevant as to whether property is subject to a resulting trust, then no resulting trust would ever arise.[98]

The district court further held that a resulting trust could survive the trustee's power to avoid unrecorded interests in real property under § 544(a)(3).[99] Under some states' laws, the circumstances that give rise to a resulting trust may amount to constructive notice of the beneficiary's interest, which as a matter of state law precludes the possibility of a bona fide purchaser.[100] Section 544(a)(3) relieves the trustee from the effect of *actual knowledge* of an unrecorded interest, but does not relieve the trustee of the effect of constructive notice.[101] The court held that summary judgment on this issue was inappropriate because of fact issues as to whether, under Washington law, the circumstances surrounding parishes' acquisition of parish property constituted constructive notice of the parishes' beneficial

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96 *In re Catholic Diocese of Spokane*, 364 B.R. at 92–93 (citing Brown v. State, 924 P.2d 908 (Wash. 1996)); *see also* RESTATEMENT (SECOND) OF THE LAW OF TRUSTS § 448 (AM. LAW INST. 1959) (describing circumstances in which a "resulting trust" arises).

97 *In re Catholic Diocese of Spokane*, 364 B.R. at 92 (citing *Brown*, 924 P.2d at 911–12).

98 *Id.* at 93, 95. Moreover, if a resulting trust arose, it could be a property interest (and not merely an inchoate right) at the time of filing. Under Washington law, a resulting trust arises at the time of the conveyance to the title holder and, unlike a constructive trust, does not depend on a court order. *Id.* at 93 (citing GEORGE G. BOGERT, TRUSTS & TRUSTEES 327 (2d ed. rev. 1979)).

99 *Brown*, 924 P.2d at 93 (citing *In re* Torrez, 827 F.2d 1299 (9th Cir. 1987)).

100 For example, under California law, there can be no bona fide purchaser of property from the holder of legal title to property that is held subject to a resulting trust if the beneficiary's possession of the property constitutes constructive notice of his equitable interest. *See, e.g.*, *In re* Weisman, 5 F.3d 417, 420 (9th Cir. 1993) (stating that under California law, a trustee takes free of actual knowledge but not constructive notice, and that a trustee's constructive notice of a prior interest precludes bona fide purchaser status); Brady v. Pohlman (*In re* Bittner), No. 08-43037, 2009 Bankr. LEXIS 2530, at * 12 (Bankr. N.D. Cal. June 9, 2009) (holding that the trustee had constructive notice of a resulting trust and thus lacked bona fide purchaser status under 11. U.S.C. § 544(a)(3)).

101 *See, e.g.*, Stern v. Am. Home Mortg. Servicing, Inc. (*In re* Asher), 488 B.R. 58, 73 (Bankr. E.D.N.Y. 2013) (finding under New York law, the trustee's avoiding power under § 544(a)(3) is subject to constructive notice). A few courts have limited the trustee's avoiding power under § 544(a)(3) against the holder of an implied equitable lien based on the equities of the situation. *See, e.g.*, *In re* 28th Legislative Dist. Cmty. Dev. Corp., No. 10-14804, 2011 Bankr. LEXIS 4411 (Bankr. E.D. Tenn. Nov. 10, 2011) (holding debtor non-profit community development organization held properties purchased with grant funding in trust for grant providers under federal law, beneficial interests of trust beneficiaries not subject to avoidance under § 544(a)(3)); *In re* W. Cent. Hous. Dev. Org., 338 B.R. 482, 486 (Bankr. D. Colo. 2005) (same); Gaffney v. U.S. Dep't of Transp. (*In re* Premier Airways, Inc.), 303 B.R. 295 (Bankr. W.D.N.Y. 2003) (same).

interest in it.[102]

Meanwhile, during the interval between the bankruptcy and district court opinions in the Spokane case, the Portland bankruptcy court considered the creditors' committee's request for a ruling that the parishes were legally indistinct from the debtor, and therefore could not be beneficiaries of an implied trust.[103] The bankruptcy court held that under Oregon law, unincorporated parishes had no capacity to sue, be sued, or hold title to real property.[104] However, it held that parishioners and other donors who contributed to the acquisition and maintenance of parish real property might have a beneficial interest in it.[105]

C. *Religious Corporations with Separately Incorporated Parishes*

1. Transfer Avoidance

Advocates for sexual abuse creditors in the cases of debtors organized as religious corporations with separately incorporated parishes sought to use tools available under bankruptcy law to capture property titled in separately incorporated parishes as part of property of the diocesan debtor's estate. The Bankruptcy Code includes statutory provisions known collectively as the "trustee's avoiding powers" under which the bankruptcy trustee, as agent for the estate, may avoid certain property interests of third parties, or reverse certain pre-petition transfers of property by the debtor to third parties.[106] By exercising an avoiding power, the trustee can capture a property interest from its holder and thereby augment the estate.[107] In the cases where the debtor was incorporated separately from parishes that held title to their own property, transfer avoidance litigation focused on the trustee's power to avoid fraudulent transfers under § 544(b)(1) and § 548.[108]

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102 *In re Catholic Diocese of Spokane*, 364 B.R. 81 at 95.

103 Tort Claimants Comm. v. Roman Catholic Archbishop of Portland in Or. (*In re* Roman Catholic Archbishop of Portland in Or.), 335 B.R. 842, 868 (Bankr. D. Or. 2005). The debtor argued only that the parishes were separate entities from the debtor and apparently conceded that schools were not separate entities. *Id.* at 865.

104 *Id.* at 866 (citing F.E.L. Publ'ns, Ltd. v. Catholic Bishop of Chi., 754 F.2d 216, 221 (7th Cir. 1985) (holding the archbishop not liable for tortious interference in a business relationship between the parish and a third party because the parish was not legally distinct from the archbishop)).

105 *Id.* at 862–63.

106 *See* TABB, *supra* note 65, at 465.

107 *See id.* at 474 (noting that one of the purposes of the avoiding powers is to maximize the value of the estate available for distribution to all creditors). *See generally* Thomas H. Jackson, *Avoiding Powers in Bankruptcy*, 36 STAN. L. REV. 725 (1984) (asserting that the avoiding powers fall into two categories, one that adjusts the rights of creditors relative to each other, and the other that adjusts the rights of creditors relative to the debtor).

108 Section 548 provides a uniform federal fraudulent transfer avoiding power. *See* 11 U.S.C. § 548 (2018). Section 544(b) gives the trustee the right to avoid a transfer that a

The onslaught of fraudulent transfer challenges in their bankruptcy cases could not have been a surprise to the debtors. Intense national media attention to the clergy sexual abuse scandal following the Boston Archdiocese story in 2002 provided Catholic bishops with powerful incentive to consider the organizational structure and property holdings of entities within their dioceses and to take action to protect parish assets from diocesan creditors.[109] The media noted dioceses' asset-protective transfer activity.[110] In the media and in court, the debtors characterized the pre-petition transfers as benign acts to conform the parishes' formal title to property with their "ownership" right in such property under canon law.[111] In contrast, sexual abuse claimants' lawyers and the media characterized such transfers as malevolent actions to defraud sexual abuse claimants.[112]

creditor of the estate could avoid under state fraudulent transfer law. *See id.* § 544(b)

[109] *See* Jill S. Manny, *Governance Issues for Non-Profit Religious Organizations*, 40 CATH. LAW. 1, 1 (2000) (recommending that corporation sole dioceses separately incorporate parishes, dioceses, and fund-raising entities that support them to protect such entities from diocesan liability).

[110] *See, e.g.*, Frank Gibney, Jr., *Can a Church Go Broke?*, TIME (May 26, 2002), http://content.time.com/time/magazine/article/0,9171,250016,00.html ("[S]everal dioceses have persuaded plaintiffs to accept reduced settlements, on the grounds that they could not afford to pay more" while "leaders divide church property among dozens if not hundreds of separate corporations, charities and other institutions."); Laurie Goodstein, *Dolan Sought to Protect Church Assets, Files Show*, N.Y. TIMES (July 1, 2013), https://www.nytimes.com/2013/07/02/us/dolan-sought-vatican-permission-to-shield-assets.html; Jean Guccione, *Diocese Accused of Moving Assets to Avoid Paying Sex-Abuse Claims*, L.A. TIMES (Aug. 18, 2004), articles.latimes.com/2004/aug/18/local/me-priests18 (reporting that several California dioceses transferred title to property held by the bishop to parishes to shield it from sexual abuse creditors); Jean Hopfensperger & Jennifer Bjorhus, *Minn. Archdiocese Transfer of Assets May Protect It from Bankruptcy Creditors*, STAR TRIB. (Feb. 2, 2015), http://www.startribune.com/archdiocese-shifted-assets-before-filing-bankruptcy/290400991/.

[111] *See, e.g.*, Objection and Response to Motion for Official Comm. of Unsecured Creditors for Authority to Commence, Prosecute and Settle Litigation on Behalf of Bankr. Estate Against the Holy See and Diocese-Related Entities at 5–6, Unaatuq, LLC v. Green (*In re* Catholic Bishop of N. Alaska), 509 B.R. 229 (Bankr. D. Alaska 2014) [hereinafter Northern Alaska Debtor's Objection and Response] (explaining the transfer of $3 million contributed to and held by the diocese in trust for parishes to the Catholic Trust of Northern Alaska as formalizing a pre-existing trust), *aff'd*, 525 B.R. 723 (D. Alaska 2015), *aff'd*, 668 F. App'x 269 (9th Cir. 2016); *Archdiocese Clarifies 7th Circuit Court Ruling on Cemetery Trust in Chapter 11*, ARCHDIOCESE OF MILWAUKEE (Mar. 10, 2015), http://www.archmil.org/News-2.0/Archdiocese-Clarifies-7th-Circuit-Court-Ruling-on-Cemetery-Trust-in-Chapter-11.htm [hereinafter *Archiodece Clarifies 7th Circuit Court Ruling*].

[112] *See, e.g.*, Milo Gyelin, *As Sex-Abuse Suits Mount, Church Tries to Protect Real-Estate Assets*, WALL ST. J. (May 15, 2002), https://www.wsj.com/articles/SB1021421244584746560 (quoting counsel for tort plaintiffs accusing dioceses of "going through their assets and shoving them back to local parishes"); Hopfensperger & Bjorhus, *supra* note 110 (quoting David Clohessy, the national director of Survivors Network of Those Abused by Priests ("SNAP"), as characterizing the Archdiocese of St. Paul and Minneapolis's pre-petition transfers as "self-serving financial maneuvers" and asking whether anyone could "honestly claim that Jesus would have spent time and energy shielding assets?").

2. Derivative Standing

Under the Bankruptcy Code, the power to avoid transfers belongs to the bankruptcy trustee[113] or, in a Chapter 11 case, to the debtor in possession exercising the powers of the trustee.[114] Neither individual creditors nor a committee of creditors can assert the trustee's avoiding powers without a grant of derivative standing from the bankruptcy court.[115] Bankruptcy courts grant derivative standing if the particular avoidance action the committee wants to pursue is "colorable" and if the debtor in possession is "unjustified" in failing to pursue it based on a cost-benefit analysis.[116]

The cost-benefit test for derivative standing was an issue in the Diocese of Northern Alaska case. Like the dioceses of Spokane and Portland, the Diocese of Northern Alaska had held title to all property, including the real property used by parishes and other diocesan affiliates.[117] In 2007, the year before the diocese filed for relief, it amended its articles of incorporation to

[113] *See* § 544(a) ("The trustee shall have . . . the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor . . . ."); *id.* § 547(b)("Except as provided . . . the trustee may avoid any transfer of an interest of the debtor in property . . . ."); *id.* § 548(a)(1) ("The trustee may avoid any transfer . . . .").

[114] *See* 11 U.S.C. § 1107(a) (2018)("[A] debtor in possession shall have all the rights . . . and powers, and shall perform all the functions and duties . . . of a trustee serving in a case under this chapter."). The debtor in possession is the fiduciary and legal representative for the estate in a Chapter 11 case, with the power to sue and be sued. *See* 11 U.S.C. § 323(b) (2018). The debtor in possession, as the "trustee," also has primary standing to bring avoidance actions. *See* TABB, *supra* note 65, at 1055.

[115] *See, e.g.*, Estate of Spirtos v. One San Bernardino Cty. Superior Court, 443 F.3d 1172, 1175–76 (9th Cir. 2006) (finding that a creditor cannot assert a Racketeer Influenced and Corrupt Organizations Act (RICO) claim on behalf of the estate without authorization from the court or the Chapter 7 trustee); Official Comm. of Unsecured Creditors of Cybergenics Corp. *ex rel.* Cybergenics Corp. v. Chinery, 330 F.3d 548, 567 (3d Cir. 2003) (holding that Congress approved of derivative standing for committees to exercise the trustee's avoiding powers and that bankruptcy courts could grant derivative standing as an exercise of general equitable powers where the debtor in possession unreasonably refused to pursue an avoidance claim); Fogel v. Zell, 221 F.3d 955, 965 (7th Cir. 2000) (finding creditor may obtain bankruptcy court permission to bring an adversary action if the trustee unjustifiably refuses to do so).

[116] *See, e.g.*, PW Enters., Inc. v. N.D. Racing Comm'n (*In re* Racing Servs., Inc.), 540 F.3d 892, 901 (8th Cir. 2008) (stating that determination of whether the trustee unjustifiably refuses to bring an avoidance action requires the court to perform a cost benefit analysis); Unsecured Creditors Comm. of STN Enters., Inc. v. Noyes (*In re* STN Enters.), 779 F.2d 901, 904 (2d Cir. 1985) (recognizing that a committee must show that the action it seeks to take on behalf of the debtor in possession is a colorable claim and that the debtor in possession unjustifiably failed to pursue it, with unjustifiability turning on a cost-benefit analysis as to whether pursuit of the action is likely to benefit the estate); Unsecured Creditors' Comm. v. Farmers Savs. Bank (*In re* Toledo Equip. Co.), 35 B.R. 315, 320 (Bankr. N.D. Ohio 1983) (finding that a committee must show that the debtor in possession's refusal to bring an action is "unjustifiable or abusive of their discretion").

[117] *See infra* Appendix A: Case Information.

clarify that it held title to parish property in an express trust for parishes.[118] In the bankruptcy case, the creditors' committee moved for derivative standing to avoid the express trusts as fraudulent transfers.[119] The court denied the motion.[120] The Diocese of Northern Alaska covered 410,000 square miles with forty-six parishes and seventeen priests, but only eight parishes raised enough from contributions of parishioners to cover their expenses.[121] Given the insolvency of parishes and the low likelihood of recovery even if the avoidance action was successful, the cost of litigation to avoid transfers from the diocese to the parishes was simply not worth the candle.[122]

In the Archdiocese of Milwaukee case, the creditors' committee tried and failed to obtain derivative standing to recover $35 million in pre-petition transfers the Archdiocese had made to parishes out of a diocesan investment fund ("the Fund"). The Archdiocese held title to the Fund into which parishes made deposits—a pooled-investment account. About seven years before it filed for bankruptcy, the Archdiocese dissolved the Fund and transferred to parishes the amounts each had deposited into it.[123] The committee alleged that the transfers were avoidable fraudulent transfers under § 544(b)(1) and Wisconsin fraudulent transfer law.[124]

The bankruptcy court denied the committee's motion for derivative standing to challenge the transfers out of the Fund because the proposed

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[118] *See* Northern Alaska Debtor's Objection and Response, *supra* note 111, at 4–5. At the same time, each parish recorded a "notice of beneficial interest" in real property in the local property records reflecting the parish's beneficial interest in parish real property titled in the name of the bishop. *Id.*

[119] *See* Motion for Official Committee of Unsecured Creditors for Authority to Commence, Prosecute and Settle Litigation on Behalf of Bankruptcy Estate Against the Holy See and Diocese-Related Entities at 5–8, Unaatuq, LLC v. Green (*In re* Catholic Bishop of N. Alaska), 509 B.R. 229 (Bankr. D. Alaska 2014) [hereinafter Northern Alaska Creditors' Committee Motion] *aff'd*, 525 B.R. 723 (D. Alaska 2015), *aff'd*, 668 F. App'x 269 (9th Cir. 2016).

[120] *See* Memorandum Regarding Committee's Motion to Pursue Litigation and Debtor's Motion to Strike at 13–14, Unaatuq, LLC v. Green (*In re* Catholic Bishop of N. Alaska), 509 B.R. 229 (Bankr. D. Alaska 2014) [hereinafter Memorandum Regarding Committee's Motion] *aff'd*, 525 B.R. 723 (D. Alaska 2015), *aff'd*, 668 F. App'x 269 (9th Cir. 2016).

[121] *See* Northern Alaska Debtor's Objection and Response, *supra* note 111, at 8. Most of the parish property at issue was inaccessible by road and about one-third of the target parishes lacked running water. *Id.* at 15.

[122] *See id.* at 16. The court did grant the committee derivative standing to pursue an avoidance action regarding a $3 million transfer between a pooled investment fund the diocese had operated for the benefit of parishes and a trust the diocese created to administer the fund within a year before it filed for relief. *See id.*

[122] The court found that the cost-benefit analysis for pursuit of this cash transfer was relatively straightforward, and that the debtor was unjustified in its refusal to pursue a fraudulent transfer avoidance action against the trust. *See id.* at 16–17.

[123] *See In re* Archdiocese of Milwaukee, 483 B.R. 855, 864 (Bankr. E.D. Wis. 2012).

[124] *See id.* at 858.

action was not colorable. First, it was time-barred under the Wisconsin statute of limitations.[125] Second, the parishes were good faith transferees expressly protected from fraudulent transfer avoidance under Wisconsin law.[126] Moreover, assuming the avoidance action was colorable, the debtor's failure to sue parish transferees was not unjustified. The committee had conceded that litigation against parishes would cost the estate more than $1 million in legal fees.[127] The court considered the overall impact of fraudulent transfer litigation against parish transferees. To pay their fraudulent transfer debts, parishes would turn to parishioners, students, and benefactors to provide funds, which would "have an adverse effect" on their willingness to support the debtor which was critical to the debtor's ability to continue to operate and fund a Chapter 11 plan.[128] Moreover, if the committee prevailed, the parishes would file claims for reimbursement against the debtor, adding to the pool of creditors and diluting the effect of recovery from parishes for sexual abuse claimants.[129]

After this defeat, sexual abuse claimants in the Milwaukee case raised a second fraudulent transfer challenge to a pre-petition transfer. This

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[125] *See id.* at 866; *see also* WIS. STAT. § 893.425(1) (2017) ("An action with respect to a fraudulent transfer . . . shall be barred unless the action is commenced . . . within 4 years after the transfer is made . . . or, if later, within one year after the transfer . . . is or could reasonably have been discovered by the claimant.").

[126] *See In re Archdiocese of Milwaukee*, 483 B.R. at 866 ("In short, the status of the Archbishop as president and board member of the Parish corporations does not, without more, render the Parishes bad faith transferees . . . ."); *see also* WIS. STAT. § 242.08(1) (2017) (providing a defense for a "person who took in good faith and for a reasonably equivalent value").

[127] *In re Archdiocese of Milwaukee*, 483 B.R. at 869–70. About a year earlier, a pooled investment account, was a hot button issue in the *Diocese of Wilmington case.* Official Comm. of Unsecured Creditors v. Catholic Diocese of Wilmington, Inc. (*In re* Catholic Diocese of Wilmington, Inc.), 432 B.R. 135 (Bankr. D. Del. 2010). The debtor disclosed in its schedules that it held title to a $120 million pooled investment account ("the PIA"), $45 million of which was property of the estate, and the balance was subject to a trust in favor of thirty-one parish depositors, albeit without an express trust agreement. *Id.* at 143. The committee challenged the validity of the trust under Delaware law. The bankruptcy court held that under Delaware law, the investment account was subject to a resulting trust in favor of the parish depositors. *Id.* at 148 (noting that the relationship between the parish depositors and the debtor was analogous to that between investor and broker); *see also* E. Lake Methodist Episcopal Church, Inc. v. Trs. of the Peninsula-Del. Annual Conference, 731 A.2d 798, 809 (Del. 1999) (holding that, even without an express trust agreement, the diocese held investment funds delivered to it by parishes in a "resulting trust" so that the funds were not property of the estate). Under bankruptcy law, however, because the Wilmington parishes' deposits were commingled with property of the estate and untraceable, the entire $120 million PIA was property of the estate free and clear. *See In re Catholic Diocese of Wilmington*, 432 B.R. at 149–50, 158–61. In contrast, in the Milwaukee case, the Fund was a parish-only investment account segregated from any diocesan funds, so that the parishes could easily trace their property interests in it. *See In re Archdiocese of Milwaukee*, 483 B.R. at 863–64.

[128] *In re Archdiocese of Milwaukee*, 483 B.R. at 870.

[129] *See id.* at 871.

challenge, known as the "Cemetery Trust" litigation, became the subject of fierce and protracted litigation through appeal to the Seventh Circuit.[130] The committee sought to avoid as fraudulent a pre-petition transfer by the Archdiocese of about $55 million to an express trust known as the Cemetery Trust ("the Trust"). The Archdiocese owned eight Catholic cemeteries and seven mausoleums in the Milwaukee area since 1857. For decades before its bankruptcy, it held an investment account known as the Cemetery Fund to maintain its cemeteries. In 2007, less than a year after settling a group of sexual abuse claims for $17 million, the Archdiocese created the Cemetery Trust to provide for maintenance of the cemetery property.[131] In March 2008, with approval from the Pope, the Archbishop transferred about $55 million from the Cemetery Fund into the Cemetery Trust.[132] The transfer was plainly part of a strategy to shield the funds from archdiocesan creditors. In a 2008 letter to the Holy See requesting approval for the transfer, the Archbishop wrote that "[b]y transferring these assets to the Trust, I foresee an improved protection of these funds from any legal claim and liability."[133]

The transfer to the Cemetery Trust provided sexual abuse creditors a much better chance at obtaining derivative standing than their previous attempt. Unlike the multiple transfers from the pooled investment account to various parish depositors, the transfer from the Archdiocese to the Cemetery Trust presented a single $55 million transfer to a single transferee. Moreover, the Archbishop made the transfer with the express intention, as he explained to the Pope, to shield cash from the impending claims of sexual abuse claimants.

The committee's challenge to the $55 million Cemetery Trust transfer put the Archbishop in an unusual situation. In his capacity as trustee of the Cemetery Trust, he was the transferee. In his capacity as archbishop, he was the agent for the transferor. The Archdiocese, as debtor in possession, had no incentive to assert its transfer-avoiding powers against the Archbishop to avoid the transfer to the Trust.[134] To rectify this conflict, with the agreement of the parties, the bankruptcy court granted the sexual abuse creditors'

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130 *See* Listecki v. Official Comm. of Unsecured Creditors, 780 F.3d 731 (7th Cir. 2015).

131 Listecki v. Official Comm. of Unsecured Creditors (*In re* Archdiocese of Milwaukee), 485 B.R. 385, 387 (Bankr. E.D. Wis. 2013), *rev'd*, 496 B.R. 905 (E.D. Wis. 2013), *rev'd and remanded*, 780 F.3d 731 (7th Cir. 2015).

132 *Id.*

133 *Listecki*, 780 F.3d at 734. The Archdiocese explained that the transfer was not an "actual fraud" intended to hinder its creditors, but rather a formalization of the trust for the perpetual care of cemeteries under which the Archdiocese had always held the funds that were transferred in 2008 into the Cemetery Trust. *See Archdiocese Clarifies 7th Circuit Court Ruling*, *supra* note 111.

134 *See In re Archdiocese of Milwaukee*, 485 B.R. at 387.

committee derivative standing.[135] The Cemetery Trust litigation proceeded with the Archbishop and the committee at odds as to the Archbishop's protection from avoidance on religious liberty grounds as discussed below in Part V.

3. Substantive Consolidation

In the Saint Paul and Minneapolis case, sexual abuse creditors tried to augment the debtor's estate not by challenging individual transfers from the debtor to parishes, but rather by dismantling the legal distinction between the debtor and the separately incorporated parishes. Seventeen months after the case commenced, the sexual abuse creditors' committee moved for substantive consolidation of the debtor with about 200 separately incorporated entities including 187 parishes, none of which were debtors in bankruptcy.[136]

The district court held that substantive consolidation of the debtor with separately incorporated, non-debtor parishes would be inconsistent with § 303(a) of the Bankruptcy Code, which prohibits commencement of an involuntary bankruptcy case against a non-profit corporation.[137] The Eighth Circuit similarly held in favor of the debtor.[138] Section 105 only confers equitable powers that do not conflict with an explicit mandate of another provision of the Bankruptcy Code.[139] Substantive consolidation would, in effect, force parishes into involuntary bankruptcy and would violate § 303(a) which expressly protects non-profit organizations (like parishes) from

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[135] Listecki v. Official Comm. of Unsecured Creditors (*In re* Archdiocese of Milwaukee), 496 B.R. 905, 916–17 (E.D. Wis. 2013), *rev'd*, 780 F.3d 731 (7th Cir. 2015); *see also In re Archdiocese of Milwaukee*, 485 B.R. at 391 ("The Committee, acting derivatively through the Debtor as debtor in possession, is defending a lawsuit concerning property of the bankruptcy estate.").

[136] *See* Official Comm. of Unsecured Creditors v. Archdiocese of Saint Paul & Minneapolis (*In re* Archdiocese of Saint Paul & Minneapolis), 888 F.3d 944, 948 (8th Cir. 2018). Bankruptcy courts can order substantive consolidation of a debtor with other legally distinct entities as an exercise of their general equitable power under § 105. 11 U.S.C. § 105(a) (2018) ("The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title."). *See generally*, TABB, *supra* note 65, at 242.

[137] *See* Official Comm. of Unsecured Creditors v. Archdiocese of Saint Paul & Minneapolis, 562 B.R. 755, 762–63 (D. Minn. 2016) (describing substantive consolidation as "effectively involuntary bankruptcy" for the non-debtors), *aff'd*, 888 F.3d 944 (8th Cir. 2018); *see also* 11 U.S.C. § 303(a) (2018). The circuit court also affirmed the bankruptcy court's finding that, even if the court had authority to order substantive consolidation under § 105, the facts did not support it. *See Archdiocese of St. Paul & Minneapolis*, 562 B.R. at 763–64 (applying Eighth Circuit precedent on substantive consolidation as set forth in in First Nat'l Bank of El Dorado v. Giller (*In re* Giller), 962 F.2d 796 (8th Cir. 1992)).

[138] *See In re Archdiocese of St. Paul & Minneapolis*, 888 F.3d at 954.

[139] *Id.* at 952.

involuntary bankruptcy.[140]

The Eighth Circuit "le[ft] for another day" the question of whether a bankruptcy court could order substantive consolidation of a debtor with a non-profit non-debtor if the latter was an alter ego or otherwise not entitled to be treated as legally distinct from the debtor under state law.[141] The committee had asserted that the parishes were legally indistinct from the Archdiocese based on the Archbishop's supervisory role over parishes under canon law and the provisions of Minnesota law governing religious corporations which expressly recognized the role of the Archbishop in organizing and operating parish corporations.[142] The court found that the committee did not allege facts that could support disregard of the separate incorporation of the parishes under Minnesota law. Even if an alter ego theory under state law was viable for substantive consolidation of non-profit non-debtors, the committee had not alleged facts sufficient to survive a motion to dismiss.[143]

IV. RELIGIOUS LIBERTY

A. *The First Amendment and the Religious Freedom Restoration Act*

Debtors defended against sexual abuse claimants' efforts to expand property of the estate by asserting protection from the application of certain aspects of bankruptcy law under the First Amendment and RFRA. Like the litigation over property of the estate, the legal contexts in which religious liberty issues arose depended on organizational structure, title to property, and property transfers unique to each debtor.

Before the Supreme Court's decision in *Employment Division v. Smith*,[144] the Court applied the First Amendment to protect against imposition of a substantial burden on religious expression unless the government could show that the burden was necessary to serve a compelling governmental interest.[145] In *Smith*, the Court held the Free Exercise Clause does not protect against enforcement of "neutral, generally applicable law[s]" that impose a substantial burden on religious expression even when those laws are not "justified by a compelling governmental interest."[146]

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140 *Id.*

141 *Id.* at 953.

142 *Id.* at 948–49.

143 *Id.* at 953.

144 494 U.S. 872 (1990), *superseded by statute*, Religious Freedom Restoration Act of 1993, Pub. L. No. 103-141, 107 Stat. 1488 (codified at 42 U.S.C §§ 2000bb–2000bb-4 (2018)), *as recognized in* Holt v. Hobbs, 135 S. Ct. 853, 859 (2015).

145 *See, e.g.*, Frazee v. Ill. Dep't of Emp't Sec., 489 U.S. 829 (1989); Wisconsin v. Yoder, 406 U.S. 205 (1972); Sherbert v. Verner, 374 U.S. 398 (1963).

146 494 U.S. at 890; *see also* Burwell v. Hobby Lobby Stores, Inc., 573 U.S. 682, 694

In 1990, Congress enacted RFRA to supersede the Supreme Court's decision in *Smith*.[147] Under RFRA, "[g]overnment shall not substantially burden a person's exercise of religion even if the burden results from a rule of general applicability."[148] The general prohibition on substantial burden on the exercise of religion under RFRA is subject to an exception that permits "[g]overnment" to substantially burden a person's exercise of religion if it demonstrates that "application of the burden to the person (1) is in furtherance of a compelling governmental interest; and (2) is the least restrictive means of furthering that compelling governmental interest."[149] Under either First Amendment doctrine or RFRA, a party seeking protection from government enforcement of a neutral, generally applicable law must show that enforcement of that law imposes a substantial burden on the exercise of religion.[150]

B. *The Bankruptcy Code as Neutral, Generally Applicable Law*

In the Cemetery Trust litigation in the Milwaukee case, Archbishop Jerome Listecki sought declaratory judgment on his religious liberty defense under RFRA to the committee's action by derivative standing to avoid the $55 million Cemetery Trust Transfer as a fraudulent transfer.[151] The Archbishop conceded that the Bankruptcy Code was a law of general application, but he contended that it was not "neutral" to religion because it

(2014) (quoting City of Boerne v. Flores, 521 U.S. 507, 514 (1997)).

147 *See* § 2000bb(a)(4), (b)(1) (noting that the Supreme Court in *Smith* "virtually eliminated" the compelling interest test, and that one of the purposes of RFRA was to restore the compelling interest test as set forth in *Verner* and *Yoder*); *see also* Gonzales v. Centro Espirita Beneficente Uniao do Vegetal, 546 U.S. 418, 424 (2006) (recounting the history of RFRA as Congressional action to supersede *Smith*). RFRA does not apply to the states. *See* § 2000bb-2 (providing that RFRA applies only to the United States, its territories and possessions, the District of Columbia, and Puerto Rico); *see also Flores*, 521 U.S. at 534 (holding an earlier version of RFRA unconstitutional as applied to the states). Thirty-three states have either enacted similar state legislation or interpreted their state constitutions to require a heightened level of judicial scrutiny for state government action that imposes a burden on free expression of religion. *See* Douglas Laycock, *Religious Liberty and the Culture Wars*, 2014 U. ILL. L. REV. 839, 844–45 nn.22 & 26 (2014) (citing to state legislation and court decisions).

148 § 2000bb-1(a).

149 *Id.* § 2000bb-1(b). Subsection 1(c) provides for relief "against a government." *Id.* § 2000bb-1(c).

150 *See id.* § 2000bb-1(a); Church of the Lukumi Babalu Aye v. City of Hialeah, 508 U.S. 520, 531–32 (1993) (holding that the First Amendment does not protect against application of a neutral, generally applicable law that has only an incidental effect on exercise of religious beliefs); Tort Claimants Comm. v. Roman Catholic Archbishop of Portland in Or. (*In re* Roman Catholic Archbishop of Portland in Or.), 335 B.R. 842, 860 (Bankr. D. Or. 2005) (providing that RFRA puts the burden on the person who invokes it to show the neutral law imposes a substantial burden).

151 *See* Listecki v. Official Comm. of Unsecured Creditors, 780 F.3d 731, 735 (7th Cir. 2015).

contains three subsections which recognize exceptions from a general transfer avoidance rule for certain transfers to charitable or religious transferees.[152] Particularly, the Archbishop argued that these subsections are "religious" under *Church of Lukumi Babalu Aye v. City of Hialeah*[153] because they "refer[] to a religious practice [i.e., charitable or religious contributions] without a secular meaning discernible from the language or context."[154] The Seventh Circuit rejected the Archbishop's contention because the exceptions from avoidance for certain charitable contributions do not prohibit the practice of religion, but rather encourage it and thus do not implicate the First Amendment.[155] Moreover, the Bankruptcy Code provisions that establish property of the estate apply without regard to religion or religious beliefs.[156]

C. *Substantial Burden on Free Exercise of Religion*

As to whether application of bankruptcy law governing property of the estate substantially burdens Catholic debtors' free exercise of religion, a recurring consideration was the *choice* of the debtor to seek relief in bankruptcy. In the Portland case, the bankruptcy court noted that the debtor's choice to organize as a corporation sole and to hold record title to property, including property attributed to parishes under canon law, was the cause of its problems, not application of the Bankruptcy Code. The court noted that, "[i]f a religious organization's manner of holding property fails under neutral civil law to protect its internal view of property ownership, but such internal view could have been accommodated by civil law, the burden on the exercise of religion is caused not by the neutral law but by the religious organization's own choice."[157]

Similarly, in the Spokane case, the bankruptcy court reasoned that, because the debtors chose the benefits of bankruptcy, they could not legitimately complain that the statutory constraints that come with it imposed

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[152] *Id.*; *see also* 11 U.S.C. § 548(a)(2) (2018) (providing an exception from fraudulent transfer avoidance for certain charitable contributions); *id.* § 548(d)(4) (defining qualified charitable contributions); *id.* § 544(b)(2) (providing an analogous protection for certain charitable contributions from avoidance under state fraudulent transfer law).

[153] 508 U.S. 520 (1993).

[154] *Listecki*, 780 F.3d at 743 (alteration in original omitted); *see also Lukumi*, 508 U.S. at 533–34.

[155] *Listecki*, 780 F.3d at 744.

[156] *See id.* The Seventh Circuit identified the provisions of the Bankruptcy Code that together establish "property of the estate" including § 541 (defining "property of the estate") and the avoiding powers by which the trustee augments the estate. *Id.* at 743.

[157] *In re Roman Catholic Archbishop of Portland in Or.*, 335 B.R. at 862. "It is not for the civil courts to enforce canon law if the actions of the religious organization under applicable civil law do not effectuate what canon law requires." *Id.*

a substantial burden on their free exercise right.[158] "It is not a burden on a religious organization which voluntarily seeks the protection of the bankruptcy laws to require it to treat its creditors in the same manner as any other debtor."[159] If the debtor found the application of bankruptcy law to be a burden on its religious liberty, "the appropriate remedy would be dismissal of the bankruptcy case."[160]

In the Portland case, the bankruptcy court delivered a small victory to the debtor. The court considered whether exercise of the trustee's power under § 544(a)(3) to avoid parishes' unrecorded beneficial interests in *all* real property could substantially burden the debtor's free exercise of religious belief.[161] It held that parishioners' c*omplete loss* of access to places for Catholic worship and education could be a substantial burden on the exercise of religion for purposes of the application of RFRA.[162] This possibility raised an issue of fact precluding summary judgment in favor of the committee.[163]

Because the bankruptcy court in the Portland case held that avoidance under § 544(a)(3) of *all* unrecorded parish interests in real property could substantially burden exercise of religion, it reached the question of whether the government's interest in the enforcement of the trustee's power under § 544(a)(3) was compelling. It grappled with the purpose of § 544(a)(3): "It gives to the bankruptcy trustee . . . the ability to avoid certain interests in real property that would not be avoidable under state law if there were no actual bona fide purchaser of real property."[164] A few paragraphs later, the court described the purpose of the avoiding powers generally to "maximize the bankruptcy estate and . . . the recovery for creditors."[165] The court observed that the Bankruptcy Code provides for exceptions that do not further this

158 Comm. of Tort Litigants v. Catholic Diocese of Spokane (*In re* Catholic Bishop of Spokane), 329 B.R. 304, 324 n.5 (Bankr. E.D. Wash. 2005), *aff'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, No. CV-05-0274-JLQ, 2006 U.S. Dist. LEXIS 6025 (E.D. Wash. Jan. 24, 2006), *and rev'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, 364 B.R. 81 (E.D. Wash. 2006). The bankruptcy court noted that "[b]ankruptcy debtors who voluntarily choose to participate in that statutory scheme, even those of a religious nature, should not be able to 'pick and choose' among Code sections." *Id.*

159 *Id.* at 325.

160 *Id.* at 324 n.5.

161 *In re Roman Catholic Archbishop of Portland in Or.*, 335 B.R. at 863–64. The debtor argued that wholesale avoidance of parishes' beneficial interests would result in the loss to parishioners of access to places for religious worship and education. *Id.* at 859.

162 *Id.* at 863. "The possibility that the result of the [sexual abuse claimants'] § 544(a)(3) claim could be the loss of all parish church and Archdiocesan school properties titled in the debtor's name raises a question of fact regarding whether application of § 544(a)(3) would impose a substantial burden on the parishioners' exercise of religion." *Id.*

163 *Id.*

164 *Id.*

165 *Id.* at 864.

policy and concluded that the government's interest in enforcement of § 544(a)(3) in this circumstance would not be compelling.[166]

D. *The Cemetery Trust Litigation*

In the Cemetery Trust litigation in the Milwaukee case, the Archbishop argued that the committee's exercise (by derivative standing) of the trustee's fraudulent transfer avoiding power would impose a substantial burden on the free exercise of religion, against which RFRA protected him, absent a compelling governmental interest.[167] The Archbishop argued that exercise of fraudulent transfer avoiding powers to recapture the corpus of the Cemetery Trust for the estate would interfere with his canonical obligation to maintain cemetery property as consecrated Catholic burial grounds.[168] It would also divert funds intended by the faithful for cemetery maintenance to payment of sexual abuse claims, inconsistently with canon law which requires donations to be applied as the donors intend.[169] Both effects would substantially burden the Archbishop's exercise of religion as protected under the First Amendment and RFRA.[170]

1. Avoidance Actions as Action by the "Government" under RFRA

The committee responded to the Archbishop's RFRA defense by raising a statutory interpretation issue under RFRA that the parties in the Spokane and Portland cases had not raised. It asserted that RFRA applies only to actions by the "government," the committee was not the "government," and therefore, RFRA did not apply to protect the Archbishop at all.[171]

RFRA defines "government" to include a "branch, department, agency, instrumentality and official (or other person acting under color of law) of the United States."[172] The committee contended that the committee, in its capacity as an official committee in a bankruptcy case, exercising the trustee's fraudulent transfer avoiding power via derivative standing, was not

166 *Id.*

167 Listecki v. Official Comm. of Unsecured Creditors, 780 F.3d 731, 735 (7th Cir. 2015).

168 *Id.*; *see also* Corrected Response Brief of Appellee at 6–8, Listecki v. Official Comm. of Unsecured Creditors, 780 F.3d 731 (7th Cir. 2015) (No. 13-2881) [hereinafter Appellee's Corrected Brief].

169 Listecki v. Official Comm. of Unsecured Creditors (*In re* Archdiocese of Milwaukee), 496 B.R. 905, 911 (E.D. Wis. 2013), *rev'd*, 780 F.3d 731 (7th Cir. 2015); *see also* 1983 CODE C.1267, § 3 (providing that offerings given by the faithful for a particular purpose may be applied only for that purpose).

170 *See Listeck*i, 780 F.3d at 735.

171 *Id.* at 736.

172 42 U.S.C. § 2000bb-2 (2018).

"acting under color of law" so as to constitute the "government" for purposes of triggering RFRA protection.[173]

Nearly two decades earlier, when the Eighth Circuit in *In re Young*[174] considered whether RFRA protected a church from a Chapter 7 trustee's fraudulent transfer action, the parties did not dispute whether the Chapter 7 trustee was the "government" for purposes of RFRA protection, and the court did not address it. The Eighth Circuit noted only that "[t]he bankruptcy code is federal law, the federal courts are a branch of the United States, and our decision in the present case would involve the implementation of federal bankruptcy law."[175]

The Seventh Circuit in *Listecki* concluded that RFRA applied only to "government" action.[176] It recognized a distinction on this point between RFRA protection and protection under the First Amendment, which provides protection against a lawsuit initiated by a private party.[177] As to whether the committee was the "government," the Seventh Circuit noted that the phrase "under color of law" in the definition of "government" in RFRA should be interpreted consistently with the term "under color of [law]" in § 1983.[178] A private person who acts "under color of law" is a governmental actor.[179] Whether a person acts "under color of law" depends on the presence of a "close nexus between the State and the challenged action" such that the action "may be fairly treated as that of the State itself."[180]

The Archbishop argued that the committee was the "government" for RFRA purposes because as an official committee appointed by the United States Trustee, it was a "government-created, government-supervised,

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173 *Listecki*, 780 F.3d at 736.

174 Christians v. Crystal Evangelical Free Church (*In re* Young), 82 F.3d 1407, 1420 (8th Cir. 1996), *vacated*, 521 U.S. 1114 (1997).

175 *Id.* at 1417.

176 *Listecki*, 780 F.3d at 737; *see also* § 2000bb-1(a) ("Government shall not substantially burden a person's exercise of religion even if the burden results from a rule of general applicability, except as provided . . . ."); *id.* § 2000bb-2(1) ("[T]he term 'government' includes a branch, department, agency, instrumentality, and official (or other person acting under color of law) of the United States, or of a covered entity.").

177 *Listecki*, 780 F.3d at 741.

178 *Id.* at 738; *see also* 42 U.S.C. 1983 (2018) ("Every person who, under color of any statute, ordinance, regulation, custom, or usage, of any State or Territory or the District of Columbia . . . ."); Tanvir v. Tanzin, 889 F.3d 72, 85 (2d Cir. 2018) (noting that Congress intended for courts to apply the meaning of "under color of law" from § 1983 when construing the term "government" as used in RFRA), *amended and superseded by* 894 F.3d 449 (2d Cir. 2018).

179 *See Listecki*, 780 F.3d at 737.

180 *Id.* at 738 (citation omitted). In *Lugar v. Edmondson Oil Co.*, the Court held that conduct is under color of law for purposes of § 1983 when the conduct is "the exercise of some right or privilege created by the [s]tate . . . or by a person for whom the [s]tate is responsible," and when the actor "may fairly be said to be a state actor." 457 U.S. 922, 937 (1982).

government-empowered, statutorily protected entity."[181] Moreover, the committee acted "under color of law" by exercising, via derivative standing, the trustee's statutory avoiding powers, which are "exclusively held by a public actor."[182] The creditors' committee argued that it was representing the private, non-governmental interests of sexual abuse claimants and therefore was not the "government." [183]

The Seventh Circuit rejected both of the Archbishop's arguments and held in favor of the committee.[184] It held that an official creditors' committee is not a government actor even though the U.S. Trustee's office appoints it and monitors its activities as part of the Trustee's responsibility to supervise a bankruptcy case.[185] Rather, the committee was "a combination of private decisions, United States Trustee appointment, and court supervision, with private actions providing the qualifying criteria for appointment."[186] The court drew an analogy between the role of a committee in a bankruptcy case and a public defender in a criminal case.[187] "Although some of [the committee's] activities are subject to governmental and court supervision, its core function is to act on behalf of, and advance the undivided interest of, its clients, namely the private creditors."[188]

The analogy the court drew is inapt. Although a bankruptcy trustee in a Chapter 7 case is typically an individual, he or she does not represent any private interests, or hold a private interest in the case apart from compensation for services rendered as trustee.[189] The Bankruptcy Code provides that the "estate" is a separate and distinct legal entity from the debtor or any of its creditors.[190] The district court has exclusive jurisdiction

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181 Appellee's Corrected Brief, *supra* note 168, at 17; *see also Listecki*, 780 F.3d at 782.

182 Appellee's Corrected Brief, *supra* note 168, at 23 (citing Christians v. Crystal Evangelical Free Church (*In re* Young), 82 F.3d 1407, 1420 (8th Cir. 1996), *vacated*, 521 U.S. 1114 (1997)).

183 *Listecki*, 780 F.3d at 737–38.

184 *Id.* at 738.

185 *Id.*; *see also* 28 U.S.C. § 586(a)(3)(E) (2018).

186 *Listecki*, 780 F.3d at 738. The court noted that once appointed, a committee "takes on a life of its own" independent of the government. *Id.* at 739. It can retain counsel and obtain compensation from the estate, not the government, although the "[t]rustee can weigh in, and the court has input" on the attorney client relationship and fees. *Id.*

187 *Id.* at 740–41 (citing Polk Cty. v. Dodson, 454 U.S. 312, 318–19 (1981)).

188 *Id.* at 741 (citations omitted).

189 *See* 11 U.S.C. § 326(a) (2018) (noting that "the court may allow reasonable compensation . . . for the trustee's services" not to exceed certain percentages of the "moneys disbursed or turned over in the case by the trustee to parties in interest"); *id.* § 701 (providing that "the United State's trustee shall appoint" an interim trustee who is a "disinterested person" in a chapter 7 case); *id.* § 1106(a) (same in a chapter 11 case).

190 *Id.* § 541(a) (providing that commencement of a case "creates an estate . . . comprised of all of the following property, wherever located and by whomever held").

over property of the estate.[191] Unlike a public defender who represents a non-governmental criminal defendant, the bankruptcy trustee acts solely as representative for the estate.[192] The Bankruptcy Code describes some of the trustee's avoiding powers as coextensive with the rights of certain hypothetical private creditors under state law. For example, the trustee's "strong arm" powers to avoid certain unrecorded liens are expressed as coextensive with the rights of a hypothetical lien creditor or bona fide purchaser of real property under non-bankruptcy law.[193] That the Bankruptcy Code sometimes defines the limits of the trustee's avoiding powers as analogous to those of certain hypothetical private creditors does not change the trustee into an individual creditor nor does it not affect the trustee's essential function as a disinterested agent for the estate.[194]

The court similarly dismissed the Archbishop's assertion that the committee's derivative standing to assert the rights of the bankruptcy trustee made it the "government" for RFRA purposes without addressing the merits of his argument. The court concluded that because the Archbishop had *agreed* to derivative standing for the committee to resolve his conflict as both agent for the debtor/transferor and trustee of the Cemetery Trust/transferee, the committee's exercise of avoiding powers by derivative standing was the result of "private ordering" not exercise of governmental powers.[195]

2. Compelling Governmental Interest

Before the appeal to the Seventh Circuit, the district court had reached the compelling governmental interest issue because unlike the Seventh Circuit, the district court had held that the committee was the government

[191] *See* 28 U.S.C. § 1334(e) (2018) ("The district court in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction (1) of all the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate . . . ."); *see also* Henry J. Sommer & Richard Levin, 3 COLLIER ON BANKRUPTCY ¶ 541.01 (16th ed. 2017) ("The estate, which comes into existence when a petition under section 301, 302, or 303 is filed, consists of all property that will be subject to the jurisdiction of the bankruptcy court.").

[192] *See* § 323(a).

[193] *See* § 544(a)(1) (judicial lien creditor); *id.* § 544(a)(3) (bona fide purchaser of real property).

[194] In support of its conclusion that the creditors' committee exercising the trustee's powers by derivative standing was not the "government," the court cited to *State Bank of Toulon v. Covey (In re Duckworth)*, 776 F.3d 453, 458 (7th Cir. 2014), noting in a parenthetical only that an "individual trustee" in that case attempted to avoid a transfer. Listecki v. Official Comm. of Unsecured Creditors, 780 F.3d at 740. In *In re Duckworth*, the court held that a chapter 7 trustee asserting the rights of a hypothetical lien creditor under § 544(a)(1) is not subject to parol evidence regarding a mistaken date in a security agreement. It held that § 544(a)(1) makes it clear that the trustee's position exercising the rights of a hypothetical judicial lien creditor is "different" than that of a private creditor.

[195] *Id.* at 739. For a criticism of this conclusion, see *infra* text accompanying notes 261–65.

for purposes of RFRA.[196] Because RFRA applied to the committee's action, the district court considered whether the committee's exercise of fraudulent transfer avoiding powers would substantially burden the Archbishop's exercise of religion. It concluded that it would and that the government lacked a compelling interest that could justify such a burden.[197]

Recall that years earlier, the bankruptcy court in the Portland case considered the debtor's argument that RFRA protected it from exercise (derivatively by the committee) of the trustee's power to avoid parishes unrecorded interests in real property under § 544(a)(3). It did not address the contention that the committee exercising these powers would not be the "government" for RFRA purposes because the parties did not raise it. The court in that case reached the same conclusion as the district court in the Cemetery Trust litigation, that the burden on the debtor from avoiding the parishes' property interests would be substantial and the government's interest in enforcement of § 544(a)(3) was not compelling.[198]

As explained above, when the Cemetery Trust litigation reached the Seventh Circuit, the court held that, because the committee was not the "government," RFRA did not apply. Nonetheless, it reached the issue of whether the government's interest was compelling as part of its analysis of whether the First Amendment protected the Archbishop. For purposes of First Amendment protection, and notwithstanding *Smith*, Seventh Circuit precedent required the court to consider whether a neutral law of general application would "substantially burden" free exercise of religion, and if so whether a compelling government interest justified that burden.[199] The court held that, even assuming avoidance of the Cemetery Trust transfer would substantially burden the Archbishop's exercise of religion, bankruptcy law furthers a compelling governmental interest.[200]

The committee had asserted that the compelling governmental interest in enforcement of the fraudulent transfer avoiding power was "protection of creditors."[201] The Seventh Circuit adopted this assertion enthusiastically.

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196 Listecki v. Official Comm. of Unsecured Creditors (*In re* Archdiocese of Milwaukee), 496 B.R. 905, 917 (E.D. Wis. 2012) ("[T]he pursuit of claims on behalf of a bankruptcy estate is a traditional public function."), *rev'd*, 780 F.3d 731 (7th Cir. 2015).

197 *Id.* at 921–22.

198 Comm. of Tort Litigants v. Catholic Diocese of Spokane (*In re* Catholic Bishop of Spokane), 329 B.R. 304, 325 n.5 (Bankr. E.D. Wash. 2005), *aff'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, No. CV-05-0274-JLQ, 2006 U.S. Dist. LEXIS 6025 (E.D. Wash. Jan. 24, 2006), *and rev'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, 364 B.R. 81 (E.D. Wash. 2006); *see also supra* text accompanying notes 154–62.

199 *See Listecki*, 780 F.3d at 745 (citing Vision Church v. Vill. of Long Grove, 468 F.3d 975, 996 (7th Cir. 2006)).

200 *Id.* at 745–46.

201 *Id.* at 745.

"[T]he importance of protecting the interests of creditors is readily apparent."[202] As support for its conclusion, the court offered an assortment of anecdotes about the political and economic significance of bankruptcy law. It cited cases that noted the history of federal bankruptcy law, none of which addressed the federal government's interest in enforcement of the Bankruptcy Code in general or the trustee's fraudulent transfer avoiding powers in particular.[203] The court undermined its conclusion with two references. First, it cited *United States v. Whiting Pools*,[204] in which the Court noted that bankruptcy reorganization furthers a variety of governmental interests apart from protecting creditors, including preservation of the going-concern value of the debtor, jobs for its employees, and a return on investment for shareholders.[205] Second, the Seventh Circuit cited to *United States v. Lee*, in which the Court held that the government's interest in enforcement of social security taxation law is compelling.[206] The Seventh Circuit noted that the social security system "aids those who have reached a certain age or are disabled," whereas, the Bankruptcy Code "aids those who have reached a certain financial condition and who need assistance repaying or recovering a debt."[207] The Seventh Circuit's analogy between the Bankruptcy Code and the social security system supports the conclusion that the government's compelling interest in the Bankruptcy Code is to offer relief to *debtors*, not creditors.

The Seventh Circuit clearly expressed its disagreement with the Eighth Circuit's contrary holding in *In re Young*.[208] Before *In re Young*, courts were divided as to whether the Bankruptcy Code presented a compelling

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202 *Id*. at 747.

203 *See id*. at 745–46; *see also* Cent. Va. Cmty. Coll. v. Katz, 546 U.S. 356, 365–69 (2006) (discussing the history of U.S. bankruptcy laws and support for inclusion of the Bankruptcy Clause in the Constitution to permit the federal government to provide a uniform law for insolvency and discharge); *id.* at 372 (avoidance of preferential transfers has long been a "core aspect" of bankruptcy law); Cohen v. De La Cruz, 523 U.S. 213, 221 (1998) (the Bankruptcy Act prohibited discharge of claims based on fraud); BFP v. Resolution Tr. Corp., 511 U.S. 531, 540–41 (1994) (history of fraudulent transfer laws); Beiger v. IRS, 496 U.S. 53, 58 (1990) (avoidance powers further the "central policy" of "[e]quality of distribution among creditors"); *In re* River W. Plaza-Chi., LLC, 664 F.3d 668, 671 (7th Cir. 2011) ("A central purpose of bankruptcy . . . is to maximize creditor recovery.") (quoting Corp. Assets, Inc. v. Paloian, 368 F.3d 761, 767 (7th Cir. 2004)).

204 462 U.S. 198 (1983).

205 *See Listecki*, 780 F3d. at 746 (citing *Whiting Pools*, 462 U.S. at 203). The two purposes of § 541 are protecting creditors and permitting the debtor to "carry on and rebuild." *Id.* at 747 (citing Andrews v. Riggs Nat'l Bank (*In re* Andrews), 80 F.3d 906, 909 (4th Cir. 1996)).

206 455 U.S. 252, 258–59 (1982).

207 *Listecki*, 780 F.3d at 746.

208 Christians v. Crystal Evangelical Free Church (*In re* Young), 82 F.3d 1407, 1420 (8th Cir. 1996) (holding that "allowing debtors a fresh start and protecting the interests of creditors are not compelling governmental interests under RFRA"), *vacated*, 521 U.S. 1114 (1997).

governmental interest that could justify a substantial burden imposed on a debtor's free exercise of religion.[209] In *In re Young*, a Chapter 7 bankruptcy trustee for an individual debtor brought a fraudulent transfer action against a church transferee for tithes the debtor had made to his church in the year before he filed for bankruptcy.[210] The church transferee asserted that RFRA protected it from avoidance.[211] The Eighth Circuit held in favor of the church. RFRA protected the church from application of the trustee's avoiding powers because exercise of the trustee's power would substantially impair exercise of religion, and the trustee had not established that avoidance of the tithes furthered a compelling government interest.[212] The Eighth Circuit stated its view: "[W]e cannot see how the recognition of what is in effect a free exercise exception to the avoidance of fraudulent transfers can undermine the integrity of the bankruptcy system as a whole; its effect will necessarily be limited to the debtor's creditors, who will as a result have fewer assets available."[213]

The Seventh Circuit dismissed the Eighth Circuit's analysis in *In re Young* as "cursory" and criticized it for failing to consider "the importance of the [Bankruptcy] Code in Supreme Court precedent, our nation's history, or the effect it has on debtors and creditors."[214] It adopted the conclusion of the dissenting opinion in *In re Young* that enforcement of the Bankruptcy Code as a whole "furthers the compelling governmental interest in . . .

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[209] *See* Morris v. Midway S. Baptist Church (*In re* Newman), 183 B.R. 239, 251–52 (Bankr. D. Kan. 1995) (holding that the government's interest in avoiding tithes to the debtor's church as fraudulent transfers was compelling); *In re* Navarro, 83 B.R. 348, 353 (Bankr. E.D. Pa. 1988) (holding that protection of legitimate interests of creditors is a compelling governmental interest). *But see In re* Tessier, 190 B.R. 396, 405 (Bankr. D. Mont. 1995) (holding that the exercise of avoiding powers to expand the estate for creditors is not a compelling interest).

[210] 82 F.3d at 1410. The trustee argued that the tithes were transfers made "for less than reasonably equivalent value" while the debtor was insolvent, and were thus avoidable under § 548 as constructively fraudulent. *Id.* at 1414.

[211] *Id.* at 1417.

[212] *Id.* at 1420.

[213] *Id.* In 1998, Congress amended the Bankruptcy Code expressly to exclude certain pre-petition charitable and religious contributions by debtors to religious organization from fraudulent transfer avoidance in the donor's bankruptcy case. *See* 11 U.S.C. § 548(a)(2) (1998) (current version at 11 U.S.C. § 548(a)(2) (2018)). The 1998 amendments also preclude a court from considering a debtor's qualifying charitable contributions for purposes of calculating his means to pay creditors. 11 U.S.C. § 707(b)(1) (1998) (current version at 11 U.S.C. § 707(b)(1) (2018)). The amendments treat qualifying charitable contributions as "reasonably necessary" expenses for purposes of determining the "disposable income" available to pay creditors. 11 U.S.C. § 1325(b)(2)–(3) (2018).

[214] Listecki v. Official Comm. of Unsecured Creditors, 780 F.3d 731, 747 (7th Cir. 2015). The court described as "without explanation" the Eighth Circuit's conclusion that the government's interest in creditor protection in the Bankruptcy Code is distinguishable from the government's interest in national security or public safety and therefore not compelling. *Id.*

protecting the interests of creditors by maximizing the debtor's estate."[215] Moreover, it held that the Bankruptcy Code is "narrowly tailored to achieve that interest."[216]

The court's conclusion rests on an absurdly sweeping generalization about the purpose of bankruptcy law. The Bankruptcy Code does not serve a single governmental purpose for which the government's interest in enforcement without exception is always compelling. Rather, the Bankruptcy Code endeavors to achieve a balance among a host of sometimes conflicting governmental goals, including but not limited to maximizing payout to unsecured creditors.[217] For example, the trustee's power to avoid fraudulent transfers, the avoiding power at issue in the Cemetery Trust litigation, does not invalidate every wealth-depleting transfer that reduces unsecured creditors' expected payment. Rather, whether the trustee can avoid a transfer as fraudulent depends on a complicated balance between the interests of the transferor's creditors and the interests of the transferee.[218]

In November 2015, after the committee's victory before the Seventh Circuit in the Cemetery Trust litigation, the parties reached a settlement and confirmed a consensual plan.[219] The plan provided for a $21 million fund to

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[215] *Id.* at 746 (alteration in original) (quoting Christians v. Crystal Evangelical Free Church (*In re* Young), 82 F.3d 1407, 1422 (8th Cir. 1996) (Bogue, J., dissenting)), *vacated*, 521 U.S. 1114 (1997).

[216] *Id.* at 749. The court must look "beyond broadly formulated interests justifying the general applicability of government mandates and scrutinize[] the asserted harm of granting specific exemptions to particular religious claimants." *Id.* at 748 (alteration in original) (quoting Gonzales v. Centro Espirita Beneficente Uniao do Vegetal, 546 U.S. 418, 431 (2006)).

[217] *See, e.g.*, United States v. Whiting Pools, 462 U.S. 198, 203 (1983) (observing that "[b]y permitting reorganization, congress anticipated that the business would continue to provide jobs, to satisfy creditors' claims, and to produce a return for its owners."); H.R. REP. NO. 95-595, p. 220 (1977); *see also* Henry J. Sommer & Richard Levin, 3 COLLIER ON BANKRUPTCY ¶ 1100.01 (16th ed. 2017) (noting that "any approach to corporate reorganization must strike a balance between the need of a corporate debtor in financial hardship to be made economically sound and the desire to preserve creditors' and stakeholders' existing legal rights to the greatest extent possible").

[218] Fraudulent transfer law takes into account the bona fides of the transferee, protecting the transferee from avoidance in circumstances when the transferee participated in the transfer for value and in good faith. *See* § 548(c) (stating that a transferee of an avoidable fraudulent transfer who takes for value and in good faith has a lien on the transferred property to the extent of value he gave for the property); BFP v. Resolution Tr. Corp., 511 U.S. 531, 536, 545 (1994) (stating that a transferee who acquires property at a non-collusive, regularly conducted foreclosure sale gives "reasonably equivalent value" and is protected from fraudulent transfer avoidance under § 548(a)(1)(B)(i) even though the foreclosure sale price is below the fair market value for the property).

[219] *See generally* Second Amended Chapter 11 Plan of Reorganization Dated September 25, 2015, Proposed by the Archdiocese of Milwaukee, *In re* Archdiocese of Milwaukee, No. 11-20059-svk (Bankr. E.D. Wis. Sept. 25, 2015) [hereinafter Second Amended Chapter 11 Plan].

compensate sexual abuse claimants, five times more than the debtor had proposed in a plan it filed in February 2014.[220] The Cemetery Trust committed to loan the debtor $3 million and contribute $8 million to the claims settlement fund.[221] Insurers provided $11 million. Total professional fees paid by the estate were approximately $27 million.[222] The bankruptcy court confirmed the consensual plan after concluding that the debtor's plan was in creditors' best interests compared to liquidation.[223] Notwithstanding a favorable outcome for sexual abuse claimants on the Archbishop's religious liberty protection before the Seventh Circuit, the odds that the sexual abuse creditors' committee could avoid the $55 million Cemetery Trust transfer under § 544(b) and Wisconsin law were far from certain.

3. Competing Plans and Cram Down

The Saint Paul and Minneapolis case was the first to involve a competing creditors' plan and cram down confirmation under § 1129(b). All previous cases, except San Diego (which was dismissed after settlement), have concluded with confirmation of a consensual plan.[224] While the substantive consolidation litigation was pending in the Saint Paul and Minneapolis case, the Archdiocese filed its first plan of reorganization in May 2016.[225] The parties failed to reach a settlement, and after the expiration of the period in which the debtor has the exclusive right to file a plan in August 2016, the committee of sexual abuse claimants filed a competing plan.[226]

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220 *Id.* at 25–26; *see also* Annysa Johnson, *Archdiocese of Milwaukee Settles Sexual Abuse Claims for $21 Million*, J. SENTINEL (Aug. 4, 2015), http://archive.jsonline.com/news/religion/archdiocese-settles-sexual-abuse-claims-for-21-million-b99542352z1-320651132.html/.

221 *See* Second Amended Chapter 11 Plan, *supra* note 219, at 23; *see also* Rich Kirchen, *Judge OK's Final Archdiocese of Milwaukee Chapter 11 Plan with $21M to Abuse Victims*, MILWAUKEE BUS. J. (Nov. 9, 2015), http://www.bizjournals.com/milwaukee/news/2015/11/09/judge-oks-final-archdiocese-of-milwaukeechapter-11.html.

222 *See* Fourth Amended Disclosure Statement for the Second Amended Chapter 11 Plan of Reorganization Dated September 25, 2015, Proposed by the Archdiocese of Milwaukee at 44, *In re* Archdiocese of Milwaukee, No. 11-20059-svk (Bankr. E.D. Wis. Sept. 25, 2015) [hereinafter Fourth Amended Disclosure Statement].

223 Order Confirming Second Amended Chapter 11 Plan of Reorganization Dated September 25, 2015, Proposed by the Archdiocese of Milwaukee at 8, *In re* Archdiocese of Milwaukee, No. 11-20059-svk (Bankr. E.D. Wis. Nov. 13, 2015). The Disclosure Statement explained that the Plan satisfied the best interest test as to sexual abuse claimants because in a hypothetical Chapter 7 liquidation, unsecured creditors would receive no distribution unless the trustee achieved a significant recovery from the Cemetery Trust in fraudulent transfer avoidance litigation. *See* Fourth Amended Disclosure Statement, *supra* note 222, at 89–96.

224 *See infra* Appendix B: Outcomes of Cases.

225 *See* Chapter 11 Plan of Reorganization of the Archdiocese of Saint Paul & Minneapolis, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. May 26, 2016).

226 *See* Chapter 11 Plan of Reorganization of the Official Committee of Unsecured

The debtor had settled with eleven of thirteen of its insurers, subject to court approval of its plan.[227] The debtor's plan provided for a $500,000 counseling fund for sexual abuse claimants and creation of an independent trust to administer and pay sexual abuse claims.[228] The trust included about $100 million to be contributed by archdiocesan insurers and $30 million by parishes, parish insurers, and the Archdiocese.[229] It provided for discharge of all tort claims against the Archdiocese and a channeling injunction that channeled any pre-petition claims against the Archdiocese, the parishes, and settling insurers, exclusively against the trust.[230]

The committee's competing plan similarly created a trust for payment of sexual abuse claims, but the Archdiocese was required to contribute at least $99 million.[231] The committee would control the trust which would succeed to the debtor in possession's transfer avoidance actions against parishes and its rights against its insurers, nullifying debtor's conditional settlements and queueing up years of litigation.[232] It did not provide for immediate discharge of the debtor or the parishes or for a channeling injunction.[233] Ninety-four percent of the members of the class of sexual abuse claimants voted to reject the debtor's plan.[234]

Creditors of the Archdiocese of Saint Paul & Minneapolis, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. Aug. 22, 2016); *see also* Joint Chapter 11 Plan of Reorganization of the Archdiocese of Saint Paul & Minneapolis, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. June 28, 2018) [hereinafter Joint Chapter 11 Plan]. The debtor in a Chapter 11 case has the exclusive right to file a plan of reorganization during the first 120 days after commencement of the case. *See* 11 U.S.C. § 1121(b) (2018). If the debtor files a plan during this exclusive period, the debtor has until 180 days after commencement of the case to obtain creditor consent. *Id.* § 1121(c)(3).

227 First Amended Disclosure Statement for First Amended Chapter 11 Plan of Reorganization of the Archdiocese of Saint Paul & Minneapolis at 12, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. Nov. 15, 2016). Under the plan, the debtor contributed all of its rights against two of the insurers to the trust and nine in cash. *Id*. The Committee conceded that six of the eleven settlements were reasonable and objected to the remaining five. *Id.* at 13.

228 *Id.* at 57.

229 *Id.* at 2–3, 11.

230 *Id.* at 100–101; *see also* First Amended Chapter 11 Plan of Reorganization of the Archdiocese of Saint Paul & Minneapolis at 16–17, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. Nov. 15, 2016) [hereinafter First Amended Chapter 11 Plan].

231 Disclosure Statement for Chapter 11 Plan of Reorganization of the Official Committee of Unsecured Creditors of the Archdiocese of Saint Paul & Minneapolis at 2, 56–57, C-2, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. Aug. 22, 2016).

232 *Id.* at 23.

233 *Id.* at 33, 35.

234 *See* Legal Objection to Confirmation of the Debtor's Second Amended Chapter 11 Plan of Reorganization at 6, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. July 1, 2017).

The committee objected to confirmation of the debtor's plan on grounds that the bankruptcy court lacked jurisdiction to impose a channeling injunction protecting parishes (non-debtors) over the objection of the class of sexual abuse creditors whose claims would be affected.[235] The debtor argued in favor of confirmation of its plan, asserting that without a channeling injunction including claims against parishes and insurers, no reorganization would be possible.[236]

Both sides recognized a split in the circuits on the question of whether or under what circumstances a bankruptcy court can impose a channeling injunction without the consent of affected creditors.[237] The bankruptcy court held that it had jurisdiction to order a channeling injunction to protect non-debtors.[238] However, the debtor's plan could not be confirmed absent "significant acceptance" by the creditors whose claims would be subject to the channeling injunction.[239] Because more than ninety percent of the members of the class of sexual abuse claimants voted to reject the debtor's plan, the requisite "significant acceptance" was lacking.[240]

The bankruptcy court held that the committee's plan was "replete with uncertainties and contingencies that will frustrate the debtor's effort to

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[235] *Id.* at 6 (noting that if the court were to confirm the debtor's plan including the channeling injunction protecting non-debtors it would be "the first bankruptcy court in the country to do anything of the kind"). The committee also argued that absent consent of the parties, the bankruptcy court lacked jurisdiction in effect to enter a final judgment on sexual abuse claimants' state law claims against non-debtors because such matters were not "core proceedings arising under title 11 or arising in a case under title 11." *Id.* at 11–12.

[236] Omnibus Response to Legal Objections to the Debtor's Second Amended Chapter 11 Plan of Reorganization at 5, 17–18, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. Aug. 4, 2017) (citing *In re* 710 Long Ridge Rd. Operating Co., No. 13-13653, 2014 WL 886433, at *15–16 (Bankr. D.N.J. Mar. 5, 2014) (holding that, because reorganization would otherwise be impossible, approving injunctions was necessary to protect the debtor's key employees notwithstanding claimants' rejection of the plan)) ("Put simply, a channeling injunction represents the best and only vehicle for a fair and just global resolution of claims in this case.").

[237] *See* Order Denying Confirmation of Debtor's Plan Dated and Filed on December 19, 2016 at 4–13, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. Dec. 28, 2017) [hereinafter Order Denying Confirmation of Plan] (describing state of the law among the circuits). The parties agreed that the applicable standard for an injunction protecting non-debtors was set out by the bankruptcy court in *In re Master Mortg. Inv. Fund*, 168 B.R. 930 (Bankr. W.D. Mo. 1994). The court should consider five factors: (1) an identity of interest between the debtor and the third party, e.g. indemnity, such that a suit against the non-debtor is, in essence, a suit against the debtor or implicating estate assets; (2) the non-debtor has contributed "substantial assets" to the reorganization; (3) the injunction is essential to reorganization; (4) a "substantial majority" of the impacted class of creditors agrees to such injunction; and (5) the plan provides a mechanism for the payment of "all, or substantially all," of the claims of the impacted class. *Id.* at 934–35.

[238] *See* Order Denying Confirmation of Plan, *supra* note 237, at 13–14.

[239] *Id.* at 16.

[240] *Id.*

reorganize," and created a long list of issues for litigation and court resolution as part of the confirmation process.[241] Perhaps the most daunting open issue was a determination of the assets to be included as in property of the estate and the value of those assets. The bankruptcy court dubbed the committee's plan a "plan of future litigation" and a "boon for lawyers" with no chance of achieving timely payment to creditors and successful reorganization of the debtor.[242]

In a joint memorandum denying confirmation of both plans, the bankruptcy judge expressed his frustration with both parties who failed to agree on a plan after three years.[243] Resolution of the case, the judge wrote, will require an agreement. The parties and their lawyers "must put aside their desire to win and decide to put together a resolution that is fair to all the *people* involved."[244] In June 2018, the parties reached agreement on a consensual plan that would provide $210 million for 450 sexual abuse claimants.[245]

V. THE LEGACY OF THE CATHOLIC BANKRUPTCY CASES

A. *Organization Under Canon Law*

In some respects, the Catholic bankruptcies are not unusual among bankruptcy cases of non-profit organizations.[246] The absence of profit-seeking stockholders or any market analog to evaluate the effectiveness of managerial decisions relative to the competition increases risk of loss from incompetence or fraud.[247] All non-profit organizations are prone to mismanagement notwithstanding the sincerity of their religious beliefs or

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241 Order Denying Confirmation of the Committee of Unsecured Creditors' Plan Dated and Filed on December 19, 2016 at 23, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. Dec. 28, 2017) [hereinafter Order Denying Confirmation].

242 *Id.* at 25.

243 Joint Memorandum to Orders Denying Confirmation of Plans Filed by the Debtor and the Creditors Committee at 1, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. Dec. 28, 2017) [hereinafter Joint Memorandum].

244 *Id.* at 3 (emphasis in original). The court noted that sexual abuse claimants' lawyers may be a source of plan funding. Assuming 33% contingency fees, attorneys' fees for sexual abuse claimants' lawyers would range between $30 and $40 million dollars, a "pretty hefty sum for completing proofs of claim." *Id.* at 3–4.

245 *See infra* Appendix B: Outcomes of Cases.

246 *See* Foohey, *supra* note 11, at 278 (noting that about ninety religious organizations file petitions under Chapter 11 each year).

247 ***See*** Comm. on Budget & Fin., *Diocesan Internal Controls: A Framework*, U.S. CONF. OF CATH. BISHOPS, http://www.usccb.org/about/financial-reporting/diocesan-internal-controls-framework.cfm (last visited May 10, 2019) (providing guidelines to alert bishops to weaknesses in internal controls, risk of embezzlement, and fraudulent financial reporting). The USCCB has recognized this risk. *Id.*

mission.[248]

Catholic organizations are different from other non-profit organizations in two respects. First the Catholic bankruptcies have revealed a heightened vulnerability to mismanagement because of the hierarchical structure of Catholic organizations under canon law. Relative to congregational religious organizations, canon law assigns unilateral authority in the bishop to assign and supervise priests assigned to parishes. But, the bishop is neither accountable to the pastor or parishioners in the parishes where the priests serve, nor privy to day to day parish operations. The separation between authority and the consequences of the exercise of authority increases the risk of mismanagement, cover up, and resulting tort exposure for Catholic organizations relative to that of non-hierarchical non-profit organizations.

Second, centralized authority in the bishop of title to parish property, or centralized supervisory authority in the bishop over separately incorporated parishes and indirectly over their decentralized property interests, likely increases the expected value of sexual abuse claims against Catholic dioceses relative to similar claims against non-hierarchical religious organizations. Professor Douglas Laycock noted the impact of the Catholic hierarchical organizational structure on the magnitude of its tort liability. "A scandal like [the clergy sexual abuse scandal] becomes utterly destructive of Catholicism in the United States and not of Protestantism in the United States without regard to differences in the culpability of the conduct."[249]

The hierarchical structure of Catholic organizations under canon law created a paradox in their bankruptcy cases because it departs from the ordinary democratic corporate governance structure that underlies efficient loss allocation under organizational law and bankruptcy law. The Catholic bankruptcy cases opened to public view the fact that Catholic parishes and the individual Catholics who support them financially are not analogous to shareholders of the diocese, or even ordinary autonomous donors to a non-hierarchical religious organization. Catholics do not control the management of their parishes or their diocese, other than as advisors to the pastor.[250] They can exercise the power of the purse by withholding

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[248] *See* John B. Duncan et al., *Internal Control Systems in U.S. Churches: An Examination of the Effects of Church Size and Denomination on Systems of Internal Control*, 12 ACCT. AUDITING & ACCOUNTABILITY J. 142, 142–43 (1999).

[249] *Roundtable Discussion: Religious Organizations Filing for Bankruptcy*, 13 AM. BANKR. INST. L. REV. 25, 40 (2005) [HEREINAFTER *ROUNDTABLE DISCUSSION*]; *SEE ALSO Transcript of the Dedication Ceremony for the Conrad B. Duberstein Bankruptcy Courthouse*, 13 AM. BANKR. INST. L. REV. 1 (2005). During the roundtable discussion, Douglas Laycock asserted that "the choice of religious structure is a constitutionally protected choice." *See Roundtable Discussion*, *supra* at 40.

[250] *See* 1983 CODE C.537 (requiring each parish to have a parish finance council regulated by "universal law" as well as "by norms issued by the diocesan bishop" which serves to "assist the pastor in the administration of the goods of the parish").

contributions. However, use of this tool to discipline ineffective management is difficult to square with canon law that requires Catholics to support the Church.[251] Catholics can protest bad management by leaving the Church and there is evidence that Catholics have done so in response to the sex abuse scandal.[252] But abrogation of faith as a monitoring tool is costly relative to a shareholder's ability to sell shares in a mismanaged firm.

B. *Contribution by Parishes and Parishioners*

Sexual abuse claimants organized as creditors' committees were no doubt effective in using the tools available to creditors in bankruptcy court as leverage in plan negotiations outside of the courtroom. Their successes were all in preliminary skirmishes. No bankruptcy court has entered an order to avoid a parish's interest in property, to avoid a property transfer to a parish, or to disregard the corporate distinction between a parish and a diocese to which the entities would otherwise be entitled to under state corporation law.

No doubt all parties in the Catholic bankruptcy cases understood that a bankruptcy court order approving a trustee's sale of a Catholic parish church or school would likely set off an explosion of self-immolating litigation. Apart from the daunting practical challenge of appraising and marketing specialized, religious use property given zoning and other limitations on such property for non-religious use, the Bankruptcy Code requires a non-profit debtor to comply with any state law restrictions for sale of property under §

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[251] *See id.* C.222, § 1 (requiring the faithful to "assist with the needs of the Church so that the Church has what is necessary for divine worship, for the works of the apostolate and of charity, and for the decent support of ministers"); *see also* Elizabeth Fernandez, *Catholic Group Strives to Mend Church / Voice of Faithful Wants Active Laity to Address Clergy Scandal*, S.F. GATE (Feb. 3, 2003), http://www.sfgate.com/bayarea/article/Catholic-group-strives-to-mend-church-Voice-of-2636824.php (expressing frustration of the role of the laity as "pray, pay and obey").

[252] *See* Angela K. Dills & Rey Hernandez-Julian, *Negative Publicity and Catholic Schools*, 50 ECON. INQUIRY 143 (2012) (noting that the negative publicity from the sex abuse scandal explains about five percent of the decline in the number of Catholic schools in the last twenty years); Daniel M. Hungerman, *Substitution and Stigma: Evidence on Religious Markets from the Catholic Sex Abuse Scandal*, 5 AM. ECON. J. 227 (2013) (noting that the scandal led to the departure of two million Catholics, generating an estimated three billion dollars in donations to other religious groups).

363(b)[253] and as a condition to confirmation of a plan of reorganization.[254] It is not clear how a bankruptcy court could order a liquidation sale of religious property if it were subject to state law transfer restrictions.

Nor is it clear how courts would rule on a religious liberty defense raised by a Catholic bishop in opposition to a bankruptcy court-ordered sale of a parish church or school. The bankruptcy cases so far have explored only the theoretical surface of RFRA or First Amendment protection from transfer avoidance litigation. Apart from the concern expressed by the bankruptcy court in Portland over a substantial burden on free exercise of religion upon loss of *all* facilities for worship and education, the bankruptcy cases have left unresolved bankruptcy and religious liberty issues triggered by a court-ordered liquidation of parish property used for worship or religious education.

The focus of litigation in the Catholic bankruptcy cases on parish property as property of a diocesan debtor's estate should not obscure the importance of future contributions of Catholic faithful as a plan-funding source. Canon law obligates Catholics to support the Church.[255] It gives the bishop authority to tax parishes for ordinary support of the diocese, but

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[253] 11 U.S.C. § 363(d)(1) (2018) (permitting a trustee to "use, sell, or lease property [out of the ordinary course]" only in accordance with applicable non-bankruptcy law that governs the transfer of property by a corporation or trust that is a non-profit organization); *see also id.* § 541(f) (2018) (property held by a federal tax exempt debtor may be transferred to a non-tax exempt debtor only by complying with all "conditions as would apply" if the debtor had not filed for bankruptcy). *See generally* Henry J. Sommer & Richard Levin, 3 COLLIER ON BANKRUPTCY ¶ 363.04 (16th ed. 2017). New York law, for example, prohibits transfer of substantially all the assets of a non-profit organization unless, among other requirements, the terms of the transfer are "fair and reasonable to the corporation" and "the purposes of the corporation or the interests of the members will be promoted" by the transaction. N.Y. NOT-FOR-PROFIT CORP. LAW § 511(d) (2018); *see also In re* HHH Choices Health Plan, LLC, 554 B.R. 697 (Bankr. S.D.N.Y. 2016) (considering all the circumstances and approving proposed sale of substantially all the assets of a non-profit debtor under § 363(d)(1)).

[254] 11 U.S.C. § 1129(a)(16) (2018) ("All transfers of property under the plan shall be made in accordance with any applicable provisions of nonbankruptcy law that govern the transfer of property by a corporation or trust that is not a moneyed, business, or commercial corporation or trust.").

[255] *See* 1983 CODE C.222, § 1 (providing that the faithful are "obliged to assist with the needs of the Church so that the Church has what is necessary for divine worship, for the works of the apostolate and of charity, and for the decent support of ministers"); *id.* C.1262 ("The faithful are to give support to the Church by responding to appeals . . . ."); *id.* C.1261, § 1 (providing that the faithful are "free to give temporal goods for the benefit of the Church"). Commentators explain these provisions as directed at secular law that limits the freedom of the Church to receive donations or of the faithful to donate. NEW COMMENTARY ON CANON LAW, *supra* note 19, at 1461 (providing that C.1261, § 1 is understood to be "directed at those, within or outside the Church, who would seek to deny or discourage such an exercise of religious liberty," and asserting that bishops have a right to financial support of the faithful against interference by civil authority); *see also* C.1260 ("The Church has an innate right to require from the Christian faithful those things which are necessary for the purposes proper to it.").

imposes no obligation on the bishop to do so.[256] Assessment by dioceses of parishes is common, however it appears that parishes comply voluntarily with such assessments.[257] Although Catholic bishops certainly expect Catholic faithful to provide financial support for their dioceses through parish assessments, this expectation of support is neither the diocese's *property* under secular law, nor as a basis for funding a feasible, confirmable plan.[258]

The question of whether a bankruptcy court could *compel* parishes or individual members of the Catholic faithful to fund their diocese's plan of reorganization arose in the Saint Paul and Minneapolis case. The sexual abuse creditor's committee's plan provided that the diocese would transfer to a trust established to pay sexual abuse claimants the diocese's rights to collect past-due assessments owed to the diocese by the parishes.[259] The parishes objected to confirmation of the committee's plan, arguing, among other things, that the Archbishop's power to assess parishes is not a secular

[256] *See* C.1263. To impose a tax, the bishop must first consult with the diocesan finance council and presbyteral council. *Id.* The bishop also has authority to order parishes to take up a special collection "for specific parochial, diocesan, national, or universal projects." C.1266; *see also* NEW COMMENTARY ON CANON LAW, *supra* note 19, at 1465 ("A diocesan bishop who chooses not to use the coercive instrument of taxation in order to meet the needs of the diocese, but who prefers to rely on free-will offerings in response to fund–raising appeals, is free to do so."); Robert L. Kealy, *Taxation, Assessments and Extraordinary Collections*, *in* CHURCH FINANCE HANDBOOK 77, 79 (Kevin E. McKenna et al. eds., 1999). The bishop may impose an extraordinary tax on parishes and on individual parishioners for needs out of the ordinary course "in case of grave necessity." C.1263; *see also* Matthew J. Barrett, *The Theological Case for Progressive Taxation as Applied to Diocesan Taxes or Assessments Under Canon Law in the United States* 63 JURIST 312, 335 (2003) (noting that a few bishops have used this authority to tax parishioners to raise revenue to fund an employee pension plan or for housing for retired priests); THE CANON LAW SOC'Y OF GR. BRIT. & IR., *supra* note 44, at 713 (noting that some bishops have imposed extraordinary taxes to pay diocesan legal fees in sexual abuse litigation).

[257] *See, e.g.*, DIOCESE OF PHOENIX, BISHOP'S ASSESSMENT POLICY (2016) (imposing a penalty for late payments); DIOCESE OF SAULT SAINTE MARIE, POLICY NO. 2: DIOCESAN ADMINISTRATION EXPENSE (2016) (noting that the assessment "is payable at the end of each month"); *The Process and Use of Parish Assessments*, CATH. DIOCESE OF CLEVELAND, https://www.dioceseofcleveland.org/offices/finance/report-to-the-community/the-process-and-use-of-parish-assessments (last visited May 10, 2019) (noting "[e]ach parish is expected to remit their assessment to the Diocese in a timely fashion over the course of the fiscal year").

[258] *See* § 1129(a)(11); *see also In re* Roman Catholic Archbishop of Portland in Or., No. 04-37154, 2007 Bankr. LEXIS 1180, at *24 (Bankr. D. Or. Apr. 13, 2007) ("Feasibility has been defined as whether the things which are to be done after confirmation can be done as a practical matter under the facts." (quoting *In re* Jorgensen, 66 B.R. 104, 108 (B.A.P. 9th Cir. 1986)). A plan funded primarily by future donations raises a concern about its feasibility. *See, e.g.*, Save Our Springs (S.O.S.) All., Inc. v. WSI (II)-COS, LLC (*In re* Save Our Spring (S.O.S.) All., Inc.), 632 F.3d 168, 172–73 (5th Cir. 2011) (holding that a plan funded exclusively by donations was not feasible); *In re* Indian Nat'l Finals Rodeo Inc., 453 B.R. 387, 402 (Bankr. D. Mont. 2011).

[259] Joint Chapter 11 Plan, *supra* note 226, at 56; *see also* First Amended Chapter 11 Plan, *supra* note 230, § 5.2(e)(3).

legal right, not property of the estate, and not an appropriate source of funding for a feasible plan.[260]

The bankruptcy court agreed with the parishes. It concluded that a bishop's authority to assess parishes is not a legal right and therefore is not property of the debtor's estate under § 541.[261] In a memorandum accompanying the order dismissing both plans and relegating the parties to resume negotiation, however, the court admonished parishes that they "must consider the possibility of contributing something" to compensate sexual abuse claimants as part of a consensual plan. "The fact that the abuse may not be the legal responsibility of the parishes. . . is hardly the point, any more than their work to help the hungry and homeless are motivated by legal responsibilities."[262]

C. *Religious Liberty for Debtors*

Courts that have considered Catholic debtors' religious liberty defenses to the application of bankruptcy law have overwhelmingly rejected them. A recurring judicial reaction to debtors' arguments was that having chosen bankruptcy, Catholic dioceses and institutes must leave their religious status at the courthouse door. In the Spokane case, the bankruptcy court observed, "Bankruptcy debtors who voluntarily choose to participate in that statutory scheme, even those of a religious nature, should not be able to 'pick and choose' among Code sections."[263] In the Portland case, the bankruptcy court suggested that a party for whom application of § 541 would impose a substantial burden on religious expression does not need to assert the First Amendment to protect itself. It can simply forgo the benefits of a bankruptcy proceeding.[264] In the Cemetery Trust litigation in the Milwaukee case, the Seventh Circuit noted that the Archdiocese knew of and voluntarily undertook the costs associated with filing for bankruptcy, including loss of control over property of the estate.[265] The court went so far as to assert that

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[260] Objection of the Official Committee of Parish Creditors to Confirmation of the Chapter 11 Plan of the Official Committee of Unsecured Creditors at 1–3, 5, *In re* Archdiocese of Saint Paul & Minneapolis, No. 15-30125 (Bankr. D. Minn. June 7, 2017).

[261] Order Denying Confirmation, *supra* note 241, at 19.

[262] Joint Memorandum, *supra* note 243, at 3.

[263] Comm. of Tort Litigants v. Catholic Diocese of Spokane (*In re* Catholic Bishop of Spokane), 329 B.R. 304, 324 n.5 (Bankr. E.D. Wash. 2005), *aff'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, No. CV-05-0274-JLQ, 2006 U.S. Dist. LEXIS 6025 (E.D. Wash. Jan. 24, 2006), *and rev'd in part sub nom.* Comm. of Tort Litigants v. Catholic Diocese of Spokane, 364 B.R. 81 (E.D. Wash. 2006).

[264] Tort Claimants Comm. v. Roman Catholic Archbishop of Portland in Or. (*In re* Roman Catholic Archbishop of Portland in Or.), 335 B.R. 842, 853 n.9 (Bankr. D. Or. 2005) (stating that if the First Amendment protected the debtor from application of the bankruptcy code, the proper remedy "might well be dismissal of the case").

[265] Listecki v. Official Comm. of Unsecured Creditors, 780 F.3d 731, 747 (7th Cir. 2015).

the Archdiocese's choice to file for Chapter 11 relief was evidence of the government's "significant interest" in the enforcement of bankruptcy laws.[266]

We are left with a thin and confusing record that offers little guidance on key issues. The Seventh Circuit in *Listecki* made it clear that it decided only that the Archbishop was not entitled to protection from the committee's fraudulent transfer litigation under either the First Amendment or RFRA. It did not decide whether the transfer from the Archdiocese to the Cemetery Trust was avoidable, because that issue was not before it.[267] As discussed above, its narrow conclusion relied on fundamental misunderstandings of bankruptcy law.[268]

When the question of whether the bankruptcy trustee is a governmental actor has arisen in other contexts, courts have treated the trustee as a government actor. For example, courts have consistently held that the *Barton* doctrine protects bankruptcy trustees from suit in district court for actions taken in exercise of their authority over property of the estate.[269] The *Barton* doctrine generally prohibits suit against a court-appointed receiver in a federal district court without permission of the court who appointed him.[270] The Seventh Circuit in *In re Linton*[271] held that the *Barton* doctrine applies to suits against a bankruptcy trustee because the trustee "is a statutory successor to the equity receiver . . . working in effect for the court that appointed or approved him, administering property that has come under the court's control by virtue of the Bankruptcy Code."[272] The Seventh Circuit in *Listecki* did not consider its own precedent in *In re Linton.*

After the Seventh Circuit decided *Listecki*, the Third Circuit held, in *In re J & S Properties*,[273] without discussing *Listecki*, that a bankruptcy trustee acting as agent for the estate is a governmental actor.[274] The court considered whether a bankruptcy trustee was entitled to qualified immunity from

266 *Id.*

267 *Id.* at 736.

268 *See* discussion *supra* Part IV.D.1–2.

269 *See, e.g.*, Blixseth v. Brown (*In re* Yellowstone Mountain Club, LLC), 841 F.3d 1090, 1094 (9th Cir. 2016); Muratore v. Darr, 375 F.3d 140, 147 (1st Cir. 2004); Carter v. Rodgers, 220 F.3d 1249, 1253 (11th Cir. 2000); *In re* Linton, 136 F.3d 544, 545 (7th Cir. 1998); Lebovits v. Scheffel (*In re* Lehal Realty Assocs.), 101 F.3d 272, 276 (2d Cir. 1996); Allard v. Weitzman (*In re* Delorean Motor Co.), 991 F.2d 1236, 1240–41 (6th Cir. 1993).

270 Barton v. Barbour, 104 U.S. 126, 129 (1881) (stating that plaintiffs must obtain the permission of the bankruptcy court before suing certain officers acting in their official capacities).

271 136 F.3d 544 (7th Cir. 1998).

272 *Id.* at 545.

273 Phoenician Mediterranean Villa, LLC v. Swope (*In re* J & S Props., LLC), 872 F.3d 138 (3d Cir. 2017).

274 *Id.* at 143.

liability under § 1983 for actions taken as bankruptcy trustee to preserve property of the estate.[275] Applying the test for qualified immunity set forth in *Harlow v. Fitzgerald*,[276] the Third Circuit held that the trustee was entitled to immunity.[277] Noting that a trustee has a duty to protect property of the estate, account for it to the court, and perform other adjudicatory and administrative functions, the court held that it was "clear that Chapter 7 Bankruptcy Trustees . . . are government officials."[278]

Because the Seventh Circuit in *Listecki* determined that exercise of the trustee's avoiding powers was not action of the "government," it did not decide whether, *if RFRA applied*, the government's interest in enforcing the trustee's avoiding powers against the Archbishop would be sufficiently compelling to justify a substantial burden on free exercise of religion. Under RFRA, courts must consider whether the government's interest is compelling with reference to the application of a specific law to the "particular claimant whose sincere exercise of religion is being substantially burdened."[279] The Supreme Court has held in cases construing RFRA that whether a substantial burden is justified by a compelling governmental interest turns on "a case-by-case determination of the question, sensitive to the facts of each particular claim."[280] The compelling interest test under RFRA is "not to be made in the abstract" but rather "in the circumstances of [the] case."[281]

The Seventh Circuit's justification for its conclusion that the government's interest in enforcement of bankruptcy law was compelling for

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[275] After a dispute with a tenant, the trustee changed the locks on a building which was the largest asset in the estate, ostensibly to preserve the asset from damage. *Id.* at 140–41. The tenant sued the trustee for wrongful eviction and violation of its Fourth and Fourteenth Amendment rights under § 1983. *Id.* at 141–42.

[276] 457 U.S. 800, 818 (1982).

[277] *In re J & S Props., LLC*, 872 F.3d at 143.

[278] *Id.*; *see also* Curry v. Castillo (*In re* Castillo), 297 F.3d 940, 950–51 (9th Cir. 2002) (noting that the bankruptcy trustee performs "both adjudicatory and administrative functions" and is a congressionally-created "hybrid official").

[279] Gonzales v. Centro Espirita Beneficente Uniao do Vegetal, 546 U.S. 418, 430–431 (2006) (citing 42 U.S.C. § 2000bb-1(b) (2018)).

[280] *Id.* at 431 (quoting Emp't Div. v. Smith, 494 U.S. 872 (1990), *superseded by statute*, Religious Freedom Restoration Act of 1993, Pub. L. No. 103-141, 107 Stat. 1488 (codified at 42 U.S.C §§ 2000bb–2000bb-4 (2018)), *as recognized in* Holt v. Hobbs, 135 S. Ct. 853, 859 (2015)); *see also* Church of the Lukumi Babalu Aye v. City of Hialeah, 508 U.S. 520, 546 (1993) (stating that a compelling interest is one "of the highest order" and is found in "rare cases").

[281] Cal. Democratic Party v. Jones, 530 U.S. 567, 584 (2000); *see also* Burwell v. Hobby Lobby Stores, Inc., 573 U.S. 682, 725 (2014) (stating that the government must demonstrate that its "marginal interest in enforcing the [challenged law] in these cases" is compelling); Brown v. Entm't Merchs. Ass'n, 564 U.S. 786, 804 n.9 (2011) ("[T]he government does not have a compelling interest in each marginal percentage point by which its goals are advanced.").

First Amendment protection falls short of the individualized analysis the Court has required under RFRA. The Seventh Circuit noted that ruling in favor of the Archbishop would create a general free exercise of religion exception to the Bankruptcy Code[282] and a "logistical nightmare" for the courts.[283] It described a classic slippery slope: The court would have to consider every section in the Bankruptcy Code, determine whether that section substantially burdened a party's religious beliefs, and then determine whether the particular section furthered a compelling governmental interest.[284]

In *Gonzales v. O Centro Espirita Beneficente Uniao do Vegetal*,[285] a RFRA case, the Supreme Court characterized this argument as "the classic rejoinder of bureaucrats throughout history: If I make an exception for you, I'll have to make one for everybody, so no exceptions."[286] The Court made it clear in *Gonzales* that RFRA mandates that courts balance *on a case-by-case basis* the governmental interests in consistent enforcement of laws against the imposition in that case on individuals' religious liberty.[287] It held that under RFRA, exceptions from law enforcement to protect free exercise of religion do not invariably open an unmanageable floodgate of requests for exceptions or fatally undermine the government's interest in enforcement.[288] In contrast to the Seventh Circuit's prediction of doom, the Supreme Court in *Gonzales* expressed confidence that courts are capable of deciding in individual cases when the balance tips in favor of protection of religious

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282 Listecki v. Official Comm. of Unsecured Creditors, 780 F.3d 731, 748 (7th Cir. 2015) ("Such an exception would also open up a religious affirmative defense beyond this case to all provisions of the Code, so long as that belief is sincerely held.").

283 *Id.*

284 *Id.*

285 546 U.S. 418 (2006) (holding that government failed under RFRA to demonstrate a compelling interest in enforcement of the Controlled Substances Act (CSA) against a church and its members who used a controlled substance in religious worship).

286 *Id.* at 436.

287 *Id.* at 430 (noting that "RFRA requires the Government to demonstrate that the compelling interest test is satisfied through application of the challenged law 'to the person'—the particular claimant whose sincere exercise of religion is being substantially burdened."); 42 U.S.C. § 2000bb-1(b); *see also* Cutter v. Wilkinson, 544 U.S. 709 (2005) (stating that courts must use a case-by-case analysis to determine whether government's interest in uniform application of law is sufficiently compelling to justify a burden on free exercise of religion under the Religious Land Use and Institutionalized Persons Act of 2000, which applies RFRA standards to federal and state prisoners' requests for religious accommodations); United States v. Christie, 825 F.3d 1048 (9th Cir. 2016) (rejecting slippery-slope reasoning in a case involving a religious group's assertion of a Free Exercise clause exception to the cannabis prohibitions in the CSA).

288 *Gonzales*, 546 U.S. at 431–36; *see also* Wisconsin v. Yoder, 406 U.S. 205, 213, 236 (1972) (recognizing a religious liberty exemption from generally applicable state compulsory education laws for Amish children because the state failed to show an impediment to its "paramount" interest in education by recognizing an exemption for the Amish).

liberty.[289]

It remains to be seen how the Seventh Circuit's opinion in *Listecki*, and the split it created with the Eighth Circuit's holding in *In re Young*, will influence the development of law governing religious liberty defenses to bankruptcy law. Bankruptcy laws do not frequently conflict with religious expression, and the specific circumstances of cases where they do will be critically important. For example, compared to the tithes the Eighth Circuit protected from fraudulent transfer avoidance in *In re Young*,[290] the transfer of $55 million to the Cemetery Trust appeared to be an intentional wealth protective maneuver in anticipation of liability for sexual abuse claims, not a routine act of religious expression. The Seventh Circuit's holding in *Listecki*, although broad in its conclusions, can be limited to its unusual procedural posture and facts. Although its impact on the law governing religious liberty may be limited, the Seventh Circuit's decision resolved an expensive legal issue in the case, shifted the leverage in favor of sexual abuse claimants, and smoothed the way for settlement and confirmation of a consensual plan of reorganization.

VI. CONCLUSION

The use of bankruptcy proceedings by Catholic organizations as a means to resolve mass tort liability for clergy sexual abuse has been remarkably successful.[291] For the Catholic diocesan debtors, the price of bankruptcy relief has been intense public scrutiny of previously private matters, including the external consequences of inter-hierarchical relationships prescribed in canon law. The bankruptcy cases of Catholic dioceses have made it clear that Catholic religious organizations are significant economic actors in the secular world. Decisions made within the Catholic hierarchy of authority under canon law for internal religious purposes have profound external consequences, not only on creditors outside the Church, but also on the faithful within it.

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289 *Gonzalez*, 546 U.S. at 436.

290 Christians v. Crystal Evangelical Free Church (*In re* Young), 82 F.3d 1407, 1420 (8th Cir. 1996), *vacated*, 521 U.S. 1114 (1997).

291 *See infra* Appendix B: Outcomes of Cases.

APPENDIX A: CASE INFORMATION

Name of Debtor	Date Filed	Court	Docket Number	Date Confirmed	Corporate Form of Debtor	Separately Incorporated Parishes?
Archdiocese of Portland	07/06/ 2004	D. Oregon	3:04-bk-37154	04/17/2007	Corporation Sole	No
Diocese of Tucson	09/20/ 2004	D. Arizona	4:04-bk-04721	08/01/2005	Corporation Sole	No
Diocese of Spokane	12/06/ 2004	E.D. Washington	2:04-bk-08822	04/24/2007	Corporation Sole	No
Diocese of Davenport	10/10/ 2006	S.D. Iowa	3:06-bk-02229	05/01/2008	Non-Profit Corp.	Yes
Diocese of San Diego	02/27/ 2007	S.D. California	3:07-bk-00939	Settled 11/ 16/2007	Corporation Sole	No
Diocese of Fairbanks*	03/01/ 2008	D. Alaska	4:08-bk-00110	02/17/2010	Corporation Sole	No
Oregon Province, Society of Jesus	02/17/ 2009	D. Oregon	3:09-bk-30938	07/29/2011	Non-Profit Corp.	No**
Diocese of Wilmington	10/18/ 2009	D. Delaware	1:09-bk-13560	07/28/2011	Non-Profit Corp.	Yes
Archdiocese of Milwaukee	01/04/ 2011	E.D. Wisconsin	2:11-bk-20059	11/13/2015	Non-Profit Corp.	Yes
Christian Brothers of Ireland	04/28/ 2011	S.D. New York	7:11-bk-22820	01/13/2014	Non-Profit Corp.	Yes
Diocese of Gallup	11/12/ 2013	D. New Mexico	1:13-bk-13676	06/23/2016	Corporation Sole	No
Diocese of Stockton	01/15/ 2014	E.D. California	2:14-bk-20371	01/13/2017	Corporation Sole	Yes
Diocese of Helena	01/31/ 2014	D. Montana	2:14-bk-60074	03/05/2015	Corporation Sole	No
Archdiocese of St. Paul and Minneapolis	01/16/ 2015	D. Minnesota	3:15-bk-30125	09/25/2018	Religious Corp.***	Yes
Diocese of Duluth	12/07/ 2015	D. Minnesota	5:15-bk-50792	Pending	Religious Corp.***	Yes
Diocese of New Ulm	03/03/ 2017	D. Minnesota	3:17-bk-30601	Pending	Religious Corp.***	Yes
Diocese of Great Falls- Billings	03/31/ 2017	D. Montana	2:17-bk-60271	08/22/2018	Corporation Sole	No
Crosier Fathers and Brothers	06/01/ 2017	D. Minnesota	4:17-bk-41681	03/26/2018	Non-Profit Corp.	Yes

* The corporate name of the Diocese of Fairbanks is Catholic Bishop of Northern Alaska, or CBNA, which is listed as the official name of the debtor in all bankruptcy court filings.

** Oregon Province is comprised of Jesuit Communities, many of which are not separately incorporated entities.

*** St. Paul and Minneapolis, Duluth, and New Ulm are classified as "Religious Diocesan Corporations" under relevant state statutory regimes recognizing religious corporations.

APPENDIX B: OUTCOMES OF CASES

					Amount in Millions				
Name of Case	**Type**	**Date Filed**	**Date Confirmed**	**Time Filing to Confirmation**	**Settlement Total**	**Insurance Portion**	**Total Prof'l Fees**	**Number of Victims**	**Settlement Per Victim**
Portland	Archdiocese	07/06 /2004	04/17/2007	2.78 Years	$74.4	$52.0	$19.1	173	$430,000
Tucson	Diocese	09/20 /2004	08/01/2005	0.86 Years	$22.2	$14.8	$5.0	45	$493,300
Spokane	Diocese	12/06 /2004	04/24/2007	2.38 Years	$48.0	$20.0	$10.9	150	$320,000
Davenport	Diocese	10/10 /2006	05/01/2008	1.56 Years	$37.0	$19.5	$2.6	162	$228,390
San Diego *	Diocese	02/27 /2007	11/16/2007	0.72 Years	$198.1	$75.65	$5.0	144	$1,375,690
Fairbanks **	Diocese	03/01 /2008	02/17/2010	1.97 Years	$9.8	$1.4	$4.8	290	$33,790
Oregon Province Society of Jesus	Religious Order	02/17 /2009	07/29/2011	2.44 Years	$166.1	$118.0	$8.6	535	$310,460
Wilmington	Diocese	10/18 /2009	07/28/2011	1.78 Years	$77.4	$15.6	$15.8	148	$522,970
Milwaukee	Archdiocese	01/04 /2011	11/13/2015	4.86 Years	$21.0	$10.7	$23.0	350	$60,000
Christian Bros. of Ireland	Religious Order	04/28 /2011	01/13/2014	2.72 Years	$16.5	$3.5	$8.1	400	$41,000
Gallup	Diocese	11/12 /2013	06/23/2016	2.62 Years	$22.0	$18.9	$3.5	57	$385,960
Stockton	Diocese	01/15 /2014	01/13/2017	3.00 Years	$17.1	$3.3	$1.0	30	$570,000
Helena	Diocese	01/31 /2014	03/05/2015	1.09 Years	$21.0	$14.4	$2.0	360	$58,000
St. Paul and Minneapolis	Archdiocese	01/16 /2015	09/25/2018	3.69 Years	$210.3	$166.8	$26.0	450	$467,300
Great Falls-Billings	Diocese	03/31 /2017	08/22/2018	1.39 Years	$20.0	$8.0	$1.5	86	$232,560
Crosier Fathers and Brothers	Religious Order	06/01 /2017	03/26/2018	0.82 Years	$25.5	$19.8	$1.1	43	$593,020
Duluth	Diocese	12/07 /2015	Pending						
New Ulm	Diocese	03/03 /2017	Pending						
	Total:				**$986.4**	**$562.4**	**$138.0**	**3,423**	**Average of $288,168 per victim**

* San Diego was settled and subsequently dismissed by the bankruptcy court on November 16, 2007.

** The corporate name of the Diocese of Fairbanks is Catholic Bishop of Northern Alaska, or CBNA.