Nonprofit and Religious-Related Bankruptcies

Paul R. Hage, Moderator
Jaffe Raitt Heuer & Weiss; Southfield, Mich.

Scott K. Brown
Lewis Roca Rothgerber LLP; Phoenix

Evan C. Hollander
Arnold & Porter LLP; New York

Hon. Lee M. Jackwig
U.S. Bankruptcy Court (S.D. Iowa); Des Moines

American Bankruptcy Institute
35th Annual Midwestern Bankruptcy Institute
October 15-16, 2015

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Materials by:

Scott K. Brown
Louis Roca Rothgerber, LLC
201 East Washington, Suite 1200
Phoenix, AZ 85004
sbrown@LRRLaw.com

Paul R. Hage
Jaffe Raitt Heuer & Weiss, P.C.
27777 Franklin, Suite 2500
Southfield, MI 48034
phage@jaffelaw.com

Evan C. Hollander
Arnold & Porter LLP
399 Park Ave.,
New York, NY 10022
Evan.Hollander@aporter.com

Honorable Lee M. Jackwig
United States Bankruptcy Court
Southern District of Iowa
U.S. Courthouse Annex
110 E. Court Ave. Suite 443
Des Moines, IA 50309

Drew Clark
Law Clerk to the Honorable Lee M. Jackwig
United States Bankruptcy Court
Southern District of Iowa
U.S. Courthouse Annex
110 E. Court Ave. Suite 443
Des Moines, IA 50309
atc@iasb.uscourts.gov

3189007.1

A. Introduction.

a. Non-profit sector is a significant contributor to the American economy.
   i. Non-profits provide 5.5 percent of the nation's GDP
   ii. Employ 13.7 million people

b. A number of different types of non-profit corporations exist
   i. Not all non-profits are tax exempt
      1. Generally speaking, in order to be tax exempt, a non-profit must meet the criteria described in IRC section 503(c)(3) –
         a. Operated exclusively for religious, charitable, scientific, public safety, literary, or educational purposes or to foster national or international amateur sports competition, or for the prevention of cruelty to children or animals;
         b. No part of the earnings of the corporation may inure to the benefit of a shareholder;
         c. No substantial portion of the activities may be attempting to influence legislation (except as expressly permitted in the statute); and
         d. Does not participate in a political campaign on behalf of (or in opposition to) any candidate for public office.
   ii. Non-profit membership organizations
      1. Members control the corporation and elect the board of directors, but members do not have an economic stake in the enterprise and membership interests may not be transferred for value like shares in a for-profit corporation.
      2. The mission of a non-profit membership organization may either be to (i) advance a charitable or public purpose (e.g. a non-profit hospital system, a non-profit theater, National Public Radio (NPR), or Public Broadcasting Systems (PBS); or (ii) to benefit the members of the non-profit (e.g. a rural electrical cooperative, a local food cooperative, a university club, or professional sports associations, such as the National Football League (NFL), Major League Baseball (MLB) and the Professional Golfers' Association (PGA)).
   iii. Non-member not-for-profit organizations
      1. Boards are self-selecting and self-perpetuating.
      2. The mission of a non-member not-for-profit corporation will always be to advance a charitable or public purpose (e.g. The American Cancer Society, The Red Cross, The Metropolitan Museum of Art).

c. Non-profits seek bankruptcy protection for many of the same reasons that for-profit corporations file
   i. Liability issues (diocese bankruptcies),
   ii. Changing regulatory environment (hospital system bankruptcies),

3189007.1

iii. Declining interest in services provided (cultural organizations).
iv. Additionally, because non-profits are often dependent upon donor contributions, many are extremely vulnerable to economic recession.

d. Unique issues in dealing with non-profit clients.
   i. Non-profits sometimes have less sophisticated leadership.
   ii. Unfortunately, corporate formalities are sometimes less strictly observed.

B. Commencement of the Case.

a. Section 109 of the Bankruptcy Code provides that "only a person that resides in or has a domicile, a place of business, or property in the United States … may be debtor under [title 11]."
   i. The Bankruptcy Code defines "person" in section 101(41) to include any individual, partnership or corporation.
      1. Thus, not-for-profit corporations qualifying as a corporation (as that term is defined in section 101(9)) under applicable state law are eligible to file under both chapter 7 and chapter 11 of the Bankruptcy Code.
      2. Many trusts, which do not themselves conduct business, are excluded from the definition of "corporation" because they are not a "business trust." *See e.g., In re Affiliated Food Stores, Inc.,* 134 B.R. 215 (Bankr. N.D. Texas 1991); *In re Hunt,* 160 B.R. 131 (9th Cir. BAP 1993); *In re St. Augustine Trust,* 109 B.R. 494 (Bankr. M.D. Fla. 1990).

b. Section 303(a) of the Bankruptcy Code expressly prohibits the commencement of an involuntary case against a "farmer, family farmer, or *a corporation that is not a moneyed business, or commercial corporation*."
   i. Section 101 does not define the phrase "corporation that is not a moneyed business, or commercial corporation."
      1. Legislative history is somewhat helpful: "schools, churches, charitable organizations and foundations, likewise are exempt from involuntary bankruptcy." *See* H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 321 (1977); S. Rep. No. 95-595, 95th Cong. 2d Sess. 33 (1978).
      2. The name of an organization does not define it character. "In evaluating whether an alleged debtor is a non-profit entity that is not a moneyed business within the meaning of 11 U.S.C. § 303(a), the entity's corporate charter and status under state law is probative, but not determinative. . . . [I]t is also appropriate and necessary for the court to consider the nature and extent of the activities in which the entity has actually engaged." *In re Memorial Medical Center, Inc.,* 337 B.R. 388, 391 (Bankr. D.N.M. 2005); *see also In re Capitol Hill Healthcare Group,* 242 B.R. 199, 202 (Bankr. D. D.C. 1999).

3. Further, just because an organization has "for profit" characteristics, does not mean it is subject to Section 303(a). In *In re Grace Christian Ministries, Inc.*, 287 B.R, 352, 356 (Bankr. W.D. Pa. 2002), the corporation was organized as non-profit entity with the stated purpose of worshipping God in accordance with principles of particular religious faith. But the organization no longer had any ministers and the day care center it operated charged a fee for its child care services. Nevertheless, the court found that it did not cease to be a non-profit entity for purposes of § 303(a). For example, excess fees that the corporation collected, over and above the cost of providing day care, were used to make restitution to congregation members defrauded by former pastor. Further, mere fact that corporation charges, and is paid, a fee for its services does not mean that it is a "moneyed, business, or commercial corporation,"; whether or not corporation so qualifies will, at the very least, depend on what it does with any surplus revenue.

C. Fiduciary Duties of Officers of Non-Profit Corporations.

a. Like the duties of officers and directors of for-profit corporations, the duties of officers and directors of non-profit corporations are a matter of applicable State law.

b. Fiduciary duties of non-profit officers and directors generally parallel the duties of for profit directors and officers.
   i. <u>Duty of Loyalty</u> -- Prohibits transactions between the corporation and interested directors and officers - express "safe harbor" provision where the interested director has made good faith disclosure of material facts as to the conflicting interests and the transaction is authorized by a vote of the disinterested members.
   ii. <u>Duty of Good Faith and Care</u> -- Directors and officers must discharge duties in good faith and with the care that an ordinarily prudent person in a like position would exercise under similar circumstances. Directors may rely on statements and reports prepared or presented by officers or employees believed to be reliable and competent, counsel, accountants and committees (on which the director is not a member).
   iii. <u>Model Nonprofit Corp. Act, § 8.30</u> – A director shall discharge his or her duties as a director, including his or her duties as a member of a committee: (1) in good faith; (2) with the care an ordinarily prudent person in a like position would exercise in similar circumstances; and (3) in a manner the director reasonably believes to be in the best interest of the corporation.

c. Some jurisdictions have found that an implied "duty of obedience" exists in the non-profit context requiring officers and directors to act in furtherance of the non-profit's mission. *See e.g., Manhattan Eye, Ear & Throat Hosp. v. Spitzer,* 715

N.Y.S.2d 575, 593 (Sup. Ct. 1999) ("It is axiomatic that the Board of Directors is charged with the duty to ensure that the mission of the charitable corporation is carried out."); *In re United Healthcare Sys. Inc.,* 1997 U.S. Dist. LEXIS 5090, *15 (D. N.J. March 26, 1997); *Summers v. Cherokee Children & Family Servs.,* 112 S.W.3d 486, 504 (Tenn. Ct. App. 2002).

  i. The purposes for which the organization was established are often described in its articles of incorporation or bylaws. Other documents, such as IRS forms, public communications, solicitation materials, and corporate policies further define the parameters in which the nonprofit corporation is expected to operate.

d. In some jurisdictions, directors of non-profit public benefit corporations are specifically required to, among other things, consider the interests of employees, suppliers and beneficiaries of the general or specific public purpose of the corporation when discharging their duties, and in the sales context, are specifically authorized to consider the "resources, intent and conduct (past, stated and potential) of any person seeking to acquire control of the corporation. (e.g. New York Benefit Corporations -- Article 17 of the New York Business Corporation Law § § 1701 - 1709). Moreover, these standards of conduct may be enforceable in an action against directors and officers (e.g. New York Business Corporation Law, § 720(a)(1)(C)).

e. Protective statutes:
  i. Many states either narrowly or broadly immunize directors of nonprofit corporations who serve without compensation.
    1. <u>Michigan Non-Profit Corporations Act – MCL § 450.2209</u> (narrow) – Permits a non-profit to limit, in its articles, the liabilities of its volunteer officers and directors.
      a. Non-profit corporations may limit the liability of volunteer directors and officers for monetary damages for a breach of fiduciary duty.
        i. This limitation on liability is subject to certain exclusions, including a breach of the duty of loyalty, actions not in good faith or involving intentional misconduct or unlawful acts.
      b. Tax-exempt charitable corporations may assume the liability of volunteer directors to third parties for acts or omissions if the liability was incurred in good faith performance of the director's duties.
      c. A non-profit corporation may assume the liability for all acts or omissions of a volunteer director, volunteer officer or other volunteer provided that the volunteer was acting in good faith and within the scope of his or her authority.

    2. <u>Minnesota Non-Profit Corporations Act, § 317A.257</u> (broad) - Subject to certain exceptions set forth in the statute, an unpaid

director of a nonprofit corporation that is exempt from state income tax is not personally liable for his or her acts or omissions while serving as a director of the corporation if:

a. The director acted in good faith,
b. The director acted within the scope of his or her responsibilities, and
c. The act or omission did not constitute willful or reckless misconduct.

ii. In addition to varying levels of protection afforded by state law, federal law also protects non-profit volunteers from liability for actions done while serving the corporation.

1. Volunteer Protection Act, 42 U.S.C. § 14505 - Shields a non-profit director from tort liability if:
   a. The director was acting within the scope of his or her responsibilities,
   b. The director was properly licensed to engage in the activity (if required by applicable state or federal law),
   c. The harm was not caused by willful or criminal misconduct, gross negligence, reckless misconduct, or a conscious, flagrant indifference to the rights or safety of the individual harmed, and
   d. The harm was not caused by the volunteer while operating a motor vehicle or other vehicle for which the state requires an operator's license and insurance to operate the vehicle.

f. Despite these additional protections, all non-profits should still obtain director's and officer's insurance.

D. Property of the Estate.

a. Section 541 broadly defines property of the estate to include, among other things:
   i. (a)(1): "[e]xcept as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case";
   ii. (a)(5): "[a]ny interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date– (A) by bequest, devise, or inheritance;"
   iii. (a)(7): "[a]ny interest in property that the estate acquires after the commencement of the case."
   iv. (c)(2) provides the following exception: "A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title.
   v. (d) makes this clarification: "[p]roperty in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest … becomes property of the estate under subsection (a)(1) or (2) of

3189007.1

this section 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."

b. Restricted/endowment funds and charitable trust.
   i. The Bankruptcy Code defines property of the estate, but "[p]roperty interests are created and defined by state law." *Barnhill v. Johnson*, 503 U.S. 393, (1992) ("'property' and 'interests in property' are creatures of state law."); *Butner v. U.S.*, 440 U.S. 48, 55 (1979). Generally, whether restricted/endowment funds and/or charitable trusts are property of the estate turns on state law. *In re Steven Smith Home for the Aged, Inc.,* 80 B.R. 678 (Bankr. E.D.Pa.1987) (debtor's right to proceeds from charitable trust defined by state law).
   ii. Diocese cases:
      1. *In re Roman Catholic Archbishop of Portland in Oregon*, 345 B.R. 686 (Bankr. D. Oregon 2006) (perpetual endowment fund was not property of the estate because it was a valid charitable trust under Oregon law).
      2. *In re Catholic Diocese of Wilmington, Inc.*, 432 B.R. 135 (Bankr. D. Del. 2010) (pooled funds held by the diocese were property of the estate because (with one exception) the participants in the pool did not have written trust agreements with the diocese and they were unable to trace the supposed "trust" funds; conversely, the property of one entity that had an express written trust agreement with the debtor was not property of the estate).
      3. *In re Archdiocese of Milwaukee*, 483 B.R. 855, 857 (Bankr. E.D. Wis. 2012) (pooled investments were not property of the estate because the funds were not commingled and could be traced).
   iii. Lesson from the Diocese cases? "When working to ensure the integrity and separateness of the funds of each participant in a mutual investment vehicle, the wisest course of action is to have in place express trust agreements and segregated accounts in which the pooled funds are never commingled with funds held and used for other purposes." Thomas M. Horan, *'Property of the Estate in Church Bankruptcies: Archdiocese of Milwaukee,'* XLIV Am.Bankr.Inst.J, 1, 44-45, March 2013.

E. Sale of Assets.

a. Some states have laws that limit the ability of a non-profit to sell assets.
   i. For example, some states have "conversion" laws regulating the sale of non-profit hospitals to for-profit enterprises. *See* Maizel & Lane, *The Sale of Nonprofit Hospitals through Bankruptcy: What BAPCPA Wrought,* ABI JOURNAL, 30-JUNE Am.Bankr.Inst.J. 12 (2011).
   ii. Additionally, many states allow the state attorney general or some other governmental agency to exercise oversight over the sale of non-profit entities.
   iii. These requirements often led to disputes about whether federal bankruptcy

law preempts the authority of the state. *See e.g., In re Bankruptcy Appeal of Allegheny Health, Education and Research Foundation, Appeal of Order Staying/Enjoining Orphans Court Proceedings,* 252 B.R. 309 (W.D. Pa. 1999) (holding that attorney general's oversight role continued postposition and was exempt from the automatic stay as a "police or regulatory power").

b. BAPCPA incorporated a number of amendments that impact the ability of a non-profit to sell assets in bankruptcy. These revisions were incorporated primarily at the request of state attorneys general to preserve the state's oversight role. *See* H.R. Rep. No. 109-31, pt. 1, at 145 (2005).

   i. <u>Section 541(f)</u> – Notwithstanding any other provision of this title, property that is held by a debtor that is a corporation described in section 501(c)(3) of the Internal Revenue Code of 1986 and exempt from tax under section 501(a) of such Code may be transferred to an entity that is not such a corporation, but only under the same conditions as would apply if the debtor had not filed a case under this title.

   ii. <u>Section 363(d)(1)</u> – The trustee may use, sell, or lease property under subsection (b) or (c) of this section—

      (1) in the case of a debtor that is a corporation or trust that is not a moneyed business, commercial corporation, or trust, only in accordance with non-bankruptcy law applicable to the transfer of property by a debtor that is such a corporation or trust; and

   iii. <u>Section 1129(a)</u> - The court shall confirm a plan only if all of the following requirements are met:

      (16) All transfers of property under the plan shall be made in accordance with any applicable provisions of non-bankruptcy law that govern the transfer of property by a corporation or trust that is not a moneyed, business, or commercial corporation or trust.

c. Post-BAPCPA, the attorney general is clearly an important party in interest with standing in any non-profit bankruptcy case, especially those involving the sale of assets.

F. Limitations on Conversion/Liquidation.

a. Limitations on Conversion –

   i. Section 1112 provides for the conversion or dismissal of a chapter 11 case to a case under chapter 7 upon demonstration of "cause".

      1. However, section 1112(c) prohibits the *court* from converting a case under chapter 11 to a case under chapter 7 if the debtor is a "*non-moneyed, non-business or non-commercial corporation, **unless the debtor requests such conversion.***"

         a. <u>Question</u>: Can a chapter 11 trustee for a non-profit debtor

3189007.1

request a conversion to chapter 7?

2. While conversion is not possible, it would appear that it is possible for creditors to confirm a liquidating plan in chapter 11 if the exclusivity period has expired.

ii. There is no similar restriction on the dismissal of the bankruptcy case of a non-profit entity. *See e.g., In re S.A.B.T.C. Townhouse Ass'n, Inc.,* 152 B.R. 1005, 1011 (Bankr. M.D. Fla. 1993) (because debtor was not a "moneyed, business, or commercial corporation," and because debtor did not consent to conversion, chapter 11 case had to be dismissed upon showing that debtor could not confirm a plan.).

b. Limitations on Liquidation –

i. Some states require attorney general approval for liquidation/dissolution of a non-profit.

ii. In Michigan, the Dissolution of Charitable Purpose Corporation Act, MCL § 450.251 provides that charitable purpose organizations shall not be dissolved without obtaining approval from the attorney general.

1. Even a non-profit who is not a "charitable purpose organization" must submit a letter to the attorney general stating that it is not a charitable purpose organization and, thus, does not need attorney general approval.

G. Plan Confirmation Issues. Although non-profit entities must satisfy the requirements of § 1129 in order to confirm a plan of reorganization, the nature of the business and other factors may make it less difficult to achieve confirmation via "cramdown."

a. Absolute Priority Rule. What is the absolute priority rule? Among other things, it requires that a class of creditors or interest holders that is junior to another class of creditors or interest holders cannot "receive or retain under the plan on account of such junior claim or interest any property." 11 U.S.C. § 1129(b)(2). The absolute priority rule comes into play when determining whether the plan is "fair and equitable," a standard that has to be met if the plan proponent wishes to "cramdown" the plan on a class of creditors that objected to the plan. The question that most often arises in non-profit cases is whether the debtor's principals can remain in place post-confirmation even if unsecured creditors are not being paid in full and vote to reject the plan.

i. The circuit courts do not think nonprofits are subject to the absolute priority rule. *See In re Wabash Valley Power Assoc. Inc.*, 72 F.3d 1305, 1318-19 (7th Cir. 1996) (an equity interest is composed of multiple components - control, the right to share in profits and ownership of corporate assets - and the debtor's principals only held one of these interests (control) and that is not enough to invoke the absolute priority rule); *In re General Teamsters, Warehousemen and Helpers Union, Local 890*, 265 F.3d 869, 873-77 (9th Cir. 2001) (two indicia of equity interest -

control and the right to share in profits - were not present in the case); *see also In re Save Our Springs Alliance Inc.*, 388 B.R. 202, 245 (Bankr. W.D. Tex. 2008), *aff'd,* 2009 WL 8637183 (W.D. Tex. Sept. 29, 2009), *aff'd,* 632 F.3d 168 (5th Cir. 2011) (non-profit corporation has no equity holders).

ii. But one commentator thinks their reasoning is wrong and too narrow. Pamela Foohey*, Chapter 11 Reorganization and the Fair and Equitable Standard: How the Absolute Priority Rule Applies To All Nonprofit Entities,* ST. JOHN'S LAW REVIEW, Vol. 86 (2012) ("Notably missing by and large from these opinions, particularly the Ninth Circuit's opinion, however, is the recognition that the absolute priority rule is only one facet of the fair and equitable standard. In not acknowledging the connection between the absolute priority rule and the fair and equitable standard, these courts have created case law that may be read to provide that a nonprofit's reorganization plan need not allocate going concern value of the debtor nonprofit to creditors until they are paid in full before that value is accessible to prepetition interest holders who resemble a for-profit's owners - or the nonprofit itself - simply because the absolute priority rule, as explicitly codified, is inapplicable.")

b. Feasibility. Feasibility is a major hurdle to confirming a chapter 11 plan and can involve lengthy and expensive litigation, including the use of expert witnesses. Put simply, "feasibility" means "[c]onfirmation of the plan is not likely to be followed by the debtor's liquidation, or the need for further financial reorganization of the debtor or any successor to the debtor under the plan." 11 U.S.C. § 1129(a)(11).

i. Some courts give nonprofits the benefit of the doubt on feasibility. That's because nonprofits generally provided a needed and important benefit to society, or so the argument goes. Put a church out of business? Not if there's a glimmer of hope of reorganization. Shut down a health care business providing services to the indigent? No judge is going to want that on their list of "things to be remembered for." Of course there are limits.

ii. An "operating income" plan? That worked. *See In re Indian National Finals Rodeo Inc.*, 453 B.R. 387, 402-03 (Bankr. D. Mont. 2011) (ticket sales for national finals rodeo event sponsored by debtor had increased consistently for approximately the past six years, especially since debtor moved event to Las Vegas, debtor had long-term agreement with casino to host the rodeo and casino had invested in success of event by accepting a sponsorship thereof in lieu of debt, which was expected to continue in the future, debtor had had no increase in its insurance costs for five years and expected no future increases, debtor had received assurances that its stock costs would not increase, recent decline in event sponsorships could be explained by creditor's collection efforts, such that resolution of creditor's

3189007.1

claim through debtor's bankruptcy could be expected to result in increased sponsorships, and there was no evidence that debtor's proposed cutbacks in event expenses were not possible).

iii. A "donation-funded plan"? No. *In re Save Our Springs (S.O.S.) Alliance Inc.*, 632 F.3d 168, 172-73 (5th Cir. 2011) (bankruptcy court did not clearly err in finding that Chapter 11 plan proposed by debtor, a nonprofit charitable organization, was not feasible and could not be confirmed, where plan relied on speculative contributions by debtor's donors and where, even if the $20,000 in nonbinding pledges that debtor was able to secure all resulted in corresponding monetary contributions to debtor's reorganization, there was still a $40,000 shortfall in necessary donations).

iv. Considering a church reorganization?
   1. Age and health of the leader of the congregation. Is there a succession plan in place?
   2. Denomination of the church. If it is nondenominational, how long has it been in existence? If donations are decreasing, why?
   3. Supplemental income other than voluntary donations, like school income.

c. Best Interests of Creditors Test. Section 1129(a)(7) requires that each holder of a claim accept the plan or "receive or retain under the plan on account of such claim or interest property of a value … that is not less than the amount that such holder would so receive or retain if the debtor were liquidated under chapter 7 of this title."

   i. This test generally is not a difficult hurdle to clear for plan confirmation. It may be even easier in a nonprofit bankruptcy case as pointed out by Kavita Gupta, "Confirmation Issues Facing a Nonprofit Debtor," XXI ABI Journal 3, April 2010:
      1. The Bankruptcy Code (section 1112(c)) and state law may preclude or restrict the forced sale of a nonprofit's assets, leading to the argument that the test should not apply in the first place.
      2. The costs associated with various compliance requirements in selling or transferring assets of a nonprofit could depress the value of a forced liquidation of a nonprofit.
      3. Nonprofit assets by their very nature could yield lower values, i.e. unique property like a church or synagogue, zoning restrictions, "goodwill," and so forth.

H. The Diocese Cases.

a. Claims process.
   i. Generally.
      1. State law determines the existence of a claim, but federal law determines when the claim arises for bankruptcy purposes. *In re Roman Catholic Archbishop of Portland in Oregon*, No. 04-37154-ELPLL, 2005 WL 148775, 2 (Bankr. D. Or. Jan. 10, 2005).

2. In most mass tort bankruptcies, there are generally three categories of claimants. Daniel J. Callaghan, *Constituencies and Objectives in Mass Tort Claim Cases*, 071008 ABI-CLE 301 (ABI Northeast Bankruptcy Conference July 10-12, 2008).
    a. Individuals who have initiated litigation.
    b. Individuals who have asserted claims but have not yet instituted litigation.
    c. Individuals who are unaware of their potential claims at the time of the bankruptcy filing.

ii. Due to the sensitive nature of tort survivors' claims, confidentiality has been a major concern in the diocese cases.
1. Some courts have appointed a third party to act as the debtor's claims agent in order to provide an additional level of confidentiality for tort survivors. *See, e.g.*, *In the Matter of Diocese of Davenport*, No. 06-02229-lmj11 (S.D. Iowa, filed Oct. 10, 2006).
    a. Claims agent receives proofs of claim from tort survivors and files redacted proof of claim that protects the identity of the claimant.
    b. Agent may only release confidential information to certain individuals specified by the court pursuant to confidentiality protocols.
2. Confidentiality protocols.
    a. Approved by court to protect tort survivors.
    b. Those authorized to receive confidential information sign a sworn statement that they will comply with the protocols. *See In re Catholic Bishop of Spokane*, No. 04-08822-PCW11 (Bankr. E.D. Wash., filed Dec. 6, 2004).
3. Courts not utilizing a claims agent have directed that proofs of claim be mailed to a specific individual at the bankruptcy court. *See, e.g.*, *Catholic Bishop of Northern Alaska*, No. 08-00110-DMD (Bankr. D. Alaska, filed Mar. 1, 2008).

iii. Generally, courts have allowed a longer period for tort survivors to file claims in diocese cases. Time periods have ranged from 179 days (Wilmington, DE) to 459 days (Spokane, WA) after the petition date.

iv. In order to ensure that tort survivors are made aware of the Debtor's bankruptcy and the time in which claims may be filed, courts approve specific notice procedures, which include direct mail and notice by publication.
1. Direct mail.
    a. Generally sent to known claimants who have either filed claims or have made accusations against specific individuals.
    b. In San Diego, direct mail notice was also sent to alumni of high schools in the Diocese territory (to the extent lists of such individuals existed) and to individuals on the mailing list of a

diocesan publication. *In re The Roman Catholic Bishop of San Diego*, No. 07-00939-LA11 (Bankr. S.D. Cal., filed Feb. 27, 2007).

2. Notice by publication.
    a. Often accomplished pursuant to a court-approved media notice program.
    b. Generally includes national and regional publications, diocesan publications, and website postings.
    c. Some courts have approved notices specifically listing diocese schools that may have been affected as well as individuals against whom credible claims have been made.
    d. Other methods have included radio advertisements and letters read to parishes by priests at mass.
    e. In Tucson, the media plan was estimated to cost $60,000. *In re The Roman Catholic Church of the Diocese of Tucson*, No. 4:04-bk-04721-BMW (Bankr. D. Ariz., filed Sept. 20, 2004).
3. In areas where some tort survivors may not speak English, notice has been issued in additional languages, including Spanish (Tucson), Vietnamese (San Diego), and Hmong (Milwaukee).

v. Future claims representatives are necessary in mass sexual abuse tort claims because, due to the nature of child sexual abuse, claimants might not realize that they have a claim before the bar date. However, those claimants that are aware of their claim are subject to the bar date.
    1. *In re Roman Catholic Archbishop of Portland in Oregon*, No. 04-37154-ELPLL, 2005 WL 148775, at 2* (Bankr. D. Or. Jan. 10, 2005) (court determined that future claims representative should represent those who knew they were subjected to sexual contact as children, but had yet to discover the causal connection to their injury, because such claims were tolled under state statute of limitations).
    2. *John Doe 150 v. Archdiocese of Portland in Oregon*, 469 F. App'x 641 (9th Cir. 2012) (disallowing late filed claim because a reasonable person in the claimant's circumstances would have realized the harm that he had suffered by the claims deadline).

b. Mediation/Arbitration.
    i. Many Debtors have incorporated mediation/arbitration of tort claims into their plan in order to more quickly resolve claims of tort survivors.
        1. Plans relying on mediation/arbitration often provide that all tort survivor claims will be paid out of a Settlement Trust unless the claimant elects to litigate the claim.
        2. Many cases have utilized a tiered system to determine the amount each tort survivor is to be paid. In such a system, the court-appointed Special Arbitrator is given strict criteria for each tier, with considerations such as the age of the victim at the time of the abuse and the notoriety of the alleged abuser. *See, e.g.*, *In re The Roman*

Catholic Church of the Diocese of Tucson, No. 4:04-bk-04721-BMW (Bankr. D. Ariz., filed Sept. 20, 2004)

3. Examples.
    a. In Tucson, claimants placed in tiers receiving greater damages were required to prove more elements of their claim, such as abuse by a responsible person and bringing the claim within the statute of limitations.
    b. In Alaska, those claimants choosing to litigate their claims would receive a pro rata share of the net funds in the Litigation Trust only after all litigation claims had been allowed or disallowed.
    c. In Milwaukee, claims were not submitted to arbitration and Debtor developed a targeted claims objection process to determine which claims Debtor believed were unenforceable. Such process was designed to minimize the costs to the Estate.

ii. When a claimant agrees to binding arbitration as part of a debtor's chapter 11 plan, courts should be reluctant to review the arbitrator's decisions.

1. *Gomes v. Roman Catholic Church of the Diocese of Tucson (In re Roman Catholic Church of the Diocese of Tucson)*, No AZ-07-1409- 2008 WL 8448067 (9th Cir. BAP Oct. 17, 2008) (binding arbitration of tort survivor's claim was not appealable; however, had appellant objected to the chapter 11 plan and the procedure set forth for settling claims, such objection would have allowed an appeal of plan confirmation).
2. Possible grounds for appealing decision of Special Arbitrator .
    a. Federal Arbitration Act.
        i. Award procured by corruption, fraud, or undue means.
        ii. Evident partiality or corruption of arbitrator.
        iii. Arbitrators guilty of misconduct in refusing to postpone hearing, or in refusing to hear evidence pertinent and material to the controversy, or of any other misbehavior by which the rights of any party have been prejudiced.
        iv. Arbitrator exceeded the powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.
    b. Nonstatutory grounds.
        i. Award exhibits manifest disregard of the law.
        ii. Award is arbitrary and capricious.
        iii. Enforcement of the award is contrary to public policy.

iii. The use of mediation to settle tort claims may create issues between parties, such as the debtor and an insurance carrier, which the court must resolve.
   1. In Alaska, debtor's insurance carriers alleged that plan provisions waiving the statute of limitations for certain settling claimants violated the agreements between debtor and the carriers. *In re Catholic Bishop of Northern Alaska*, No. F08-00110-DMD, 2009 WL 8412175 (Bankr. D. Alaska Sept. 11, 2009).
   2. The Alaskan insurance carriers also alleged that the procedure by which the Special Arbitrator was to determine, settle, and allow the settling claims violated the insurance companies' rights under the policies to control the investigation, settlement, and defense of any claim.

c. Channeling Injunction.
   i. Legal basis.
      1. The channeling injunction was developed in the 1980s as part of the asbestos cases in order to promote finality of any settlement reached. Congress ultimately enacted section 524(g) and (h) in order to bring certainty to the channeling injunction process. Daniel J. Callaghan, *Constituencies and Objectives in Mass Tort Claim Cases*, 071008 ABI-CLE 301 (ABI Northeast Bankruptcy Conference July 10-12, 2008).
      2. Many courts approving channeling injunctions have done so based on the bankruptcy court's equitable power and the doctrine of marshaling of assets. Susan G. Boswell, *Dealing with Unknown Claims and Channeling Injunctions in the Diocese of Tucson Case* (ABA National Conference of Bankruptcy Judges Nov. 3, 2005).

   ii. Scope.
      1. Broader channeling injunctions have enjoined future claims against the Debtor, Reorganized Debtor, Parishes, Parish Entities, Catholic Entities, and Settling Insurers. *See In re Catholic Bishop of Spokane*, No. 04-08822-PCW11 (Bankr. E.D. Wash., filed Dec. 6, 2004).
      2. In Spokane, the plan specifically listed entities and individuals against whom subsequent actions were not enjoined.
      3. In Davenport, the plan made clear that actions against the individual perpetrators were not enjoined.

   iii. Although courts have held the channeling injunction should only be used in unusual circumstances, courts have approved such injunctions when the settlement in question forms the basis of a chapter 11 plan and allows the plan to take effect. In such a situation, the entire settlement and hence the plan hinges on the parties being free from the very claims that the injunction would prohibit. Susan G. Boswell, *Dealing with Unknown Claims and Channeling Injunctions in the Diocese of Tucson Case*, 15-16.

iv. Courts have considered a number of factors to determine whether a channeling injunction is appropriate in a given case. *In re Master Mortgage Investment Fund, Inc.*, 168 B.R. 930 (Bankr. W.D. Mo. 1994).
   1. Whether there is an identity of interest between the debtor and the third party, usually an indemnity interest, such that a suit against the nondebtor is essentially a suit against the debtor or will deplete assets of the estate.
   2. Whether the nondebtor has contributed substantial assets to the reorganization.
   3. Whether the injunction is essential to the reorganization, and it is not likely the reorganization will be successful without it.
   4. Whether a substantial majority of the creditors agree to the injunction. Specifically the court should look to whether the impacted classes have overwhelmingly voted to accept the proposed plan treatment.
   5. Whether the plan provides a mechanism for the payment of all, or substantially all, of the claims of the class or classes affected by the injunction.

d. Nonmonetary plan provisions.
   i. In addition to the financial consideration inherent in any bankruptcy, many of the diocese cases incorporated nonmonetary provisions into the plan to address issues regarding sexual abuse.
   ii. Examples.
      1. Publically releasing the names of perpetrators of abuse, including publication on the diocese's website.
      2. Providing information in parish bulletins and diocese publications with contact information for the Victim Assistance Coordinator and encouraging abuse survivors to seek mental health support and counseling.
      3. Supporting a complete elimination of all criminal statutes of limitation for child sexual abuse committed by clergy or others in similar positions of authority.
      4. Making reasonable space available on the diocese website for survivors to tell their stories of abuse, if they so desire.
      5. Issuing a personal letter of apology from the Archbishop or Bishop to any tort survivor or immediate family member who requests such a letter.