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Keeping the Faith: The Rights of Parishioners in Church Reorganizations

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KEEPING THE FAITH: THE RIGHTS OF PARISHIONERS IN CHURCH REORGANIZATIONS

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Abstract: Faced with significant potential liability to victims of sexual abuse at the hands of church personnel, four archdioceses and dioceses of the Roman Catholic Church have filed for Chapter 11 bankruptcy protection. The bankruptcy proceedings present a multitude of novel issues, including valuation of tort claims against the church and determination of the property available to pay those claims. While each issue has the potential to affect parishioners of the church, the issue of property ownership may have a particularly strong effect. Under both canon law and state incorporation statutes, an archdiocese or diocese owns all assets of its churches. Unless the diocese holds this property in trust for the benefit of its parishes, a claim against the diocese or archdiocese may be satisfied with any property located within any of its parishes, even if that property has no other connection to the claim. Such property may be the only means for tort claimants to receive a substantial recovery for their claims, but is also the only means for parishioners to fully practice their faith. This Article considers whether parishioners have a procedural right to represent their interests in a bankruptcy and concludes that parishioners have an interest in bankruptcy proceedings, but that their interest is not sufficient to allow them automatic participation in the bankruptcy proceedings. Rather, the courts will need to determine on a case-by-case basis whether the diocese or archdiocese adequately represents the interests of parishioners within the bankruptcy proceedings in order to determine the ability of parishioners to intervene.

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INTRODUCTION

On July 6, 2004, the Portland, Oregon Archdiocese of the Roman Catholic Church filed for Chapter 11 bankruptcy protection.[1] Nearly four months later, the archdiocese of Tucson, Arizona did the same.[2]

1. Voluntary Petition, *In re* Roman Catholic Archbishop of Portland, No. 04-37154 (Bankr. D. Or. July 6, 2004) [hereinafter Portland Petition].

2. Voluntary Petition, *In re* Roman Catholic Church of the Diocese of Tucson, No. 04-04721 (Bankr. D. Ariz. Sept. 20, 2004) [hereinafter Tucson Petition].

Spokane, Washington's diocese followed suit shortly thereafter.[3] The most recent filing involved the Diocese of Davenport, Iowa.[4] Each diocese[5] faces significant potential liability to victims of sexual abuse at the hands of church personnel.[6]

Although the structure of a church bankruptcy proceeding resembles that of other bankruptcy proceedings, the interests of those affected by the bankruptcy can present unusual challenges. Chapter 11 bankruptcy reorganization seeks to ensure a resolution which is fair and efficient to all interested parties, allowing the debtor to reorganize while paying

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3. Voluntary Petition, *In re* Catholic Bishop of Spokane, No. 04-08822 (Bankr. E.D. Wash. Dec. 6, 2004) [hereinafter Spokane Petition].

4. Voluntary Petition, *In re* Diocese of Davenport, No. 06-02229 (Bankr. S.D. Iowa Oct. 10, 2006) [hereinafter Davenport Petition].

5. Although there are distinctions between the two, for purposes of this Article, "diocese" will be used to refer to either a diocese or an archdiocese.

6. Disclosure Statement Regarding Plan of Reorganization Dated, September 20, 2004, at 1, *In re Diocese of Tucson*, No. 04-04721 (Sept. 20, 2004) [hereinafter Tucson Disclosure Statement]; Disclosure Statement Regarding Debtor's Plan of Reorganization at 5–8, *In re Archbishop of Portland*, No. 04-37154 (Nov. 15, 2005) [hereinafter Portland Disclosure Statement]; Disclosure Statement Regarding Plan of Reorganization Dated October 10, 2005, at 3, *In re Bishop of Spokane*, No. 04-08822 (Oct. 10, 2005); Davenport Petition, *supra* note 4, at 4 (listing 20 largest creditors).

Before the filing of bankruptcy, more than 200 claims of abuse had been filed against the Portland Archdiocese. Debtor's Motion for an Order (1) Fixing a Bar Date for Filing Tort Proofs of Claim, and (2) Approving a Tort Proof of Claim Form, Bar Date Notices, Actual Notice Procedure, and Media Notice Program at 5, *In re Archbishop of Portland*, No. 04-37154 (Aug. 18, 2004).

In the Portland Archdiocese bankruptcy, two lists of the twenty largest unsecured creditor claims were filed—one list of the twenty largest non-tort claimants, and one list of the twenty largest tort claimants. Portland Petition, *supra* note 1, at 7–16. The non-tort claimants' claims total $22,424,529 (the majority of which are claims against the church by its own bank for money lent to the church), *id.* at 7–10; the tort claimants' claims total $341,425,000 (all listed as unliquidated, disputed claims), *id.* at 13–16. Many of these claims of sexual abuse victims were paid before the filing of bankruptcy. *NewsHour with Jim Lehrer: Bankrupt Dioceses* (PBS television broadcast Jan. 25, 2005) (transcript available at http://www.pbs.org/newshour/bb/religion/jan-june05/diocese_1-25.html) (noting that fifty of 180 claims remained unpaid on the petition date).

With regard to the Spokane Diocese, one alleged victim's attorney questioned the need for bankruptcy, stating that "[t]here have been no trials that have assessed any damages against the Church. So what's the need for bankruptcy? How is the Church bankrupt, other than spiritually and morally?" *Id.* (remarks of Don Brockett). Despite those initial reservations, at least some tort victims have agreed to use the bankruptcy system as a means of resolving disputes with the Church—seventy-five of the victims entered into a proposed settlement agreement providing for a $46 million payment to the victims and an apology. Sarah Kershaw, *Rare Kind of Scandal Accord in Spokane Diocese*, N.Y. TIMES, Feb. 2, 2006, at A15.

A study released in 2004 indicated that the Catholic Church had spent $572 million on the sexual abuse scandals. *NewsHour with Jim Lehrer: Church in Crisis* (PBS television broadcast Feb. 27, 2004) (transcript available at http://www.pbs.org/newshour/bb/religion/jan-june04/church_02-27.html).

claims to its creditors.[7] Although the goal of a successful reorganization often conflicts with the goal of maximum payout to creditors, such conflicts have been dealt with by the courts for many years.[8] Church bankruptcies, however, affect parishioners, who differ from the individuals and entities involved in most other Chapter 11 bankruptcies.[9] Although similar to shareholders in that they have some (albeit extremely limited) control over the debtor[10] as well as some long-term stake in the debtor, they differ in that they do not "own" the debtor nor do they have a clear financial interest in it. Likewise, although they share attributes with customers of a traditional company, they do not have the contractual relationship a customer traditionally has with a business. Finally, although many parishioners work to further the church mission, most are not paid employees of the church.[11]

Typical bankruptcies may not include parishioners, but church bankruptcies strongly affect parishioners' interests, and bankruptcy cases can and should take these interests into account. For instance, if the churches, schools, and other assets of the church are sold to pay creditors, the parishioners may be left unable to fully practice their faith. Although one can have belief without buildings, for many Catholics, the ability to fully practice their faith may require the ability to send their children to religious schools, to gather for services in a building dedicated to that purpose, or to have funds available to support church projects.[12] Allowing parishioners to intervene in a bankruptcy

7. *See* N.L.R.B. v. Bildisco & Bildisco, 465 U.S. 513, 517 n.1 (1984).

8. *See* Jonathan C. Lipson, *When Churches Fail: The Diocesan Debtor Dilemmas*, 79 S. CAL. L. REV. 363, 365 (2006).

9. *Id.* (noting "struggle between two sets of comparatively innocent parties"—victims and parishioners).

10. Like shareholders in a company, parishioners in a church frequently have the right to vote for some church-related parishioner positions.

11. *See* Lipson, *supra* note 8, at 382, 399 (discussing concepts of shareholders and creditors in conjunction with parishioners in church bankruptcies).

12. Memorandum in Support of Motion to Intervene at 2, Tort Claimants' Comm. v. Roman Catholic Archbishop of Portland (*In re* Roman Catholic Archbishop of Portland), Adv. Proc. No. 04-03292 (Bankr. D. Or. Feb. 3, 2005) [hereinafter Portland Memorandum in Support of Motion to Intervene] ("Those in the parish communities . . . use these parish properties for religious worship, the baptism of their children, the education of their youth, the marriage of their young people and the burial of their loved ones . . . . These places are integral to the exercise of religious practices that benefit others."); *see also* James A. Hayes, Jr., *A Legal Frontier of Church-State Relations in Portland Diocese Chapter 11 Case*, 1 No. 9 Andrews Bankr. Litig. Rep. 3 ("If these assets are liquidated to satisfy the claims of abuse claimants, parishioners literally may be left without a house in which to worship."); Lipson, *supra* note 8, at 370 (characterizing this dilemma as an "untenable choice[]").

proceeding provides them with an opportunity to assert those interests in an attempt to prevent distribution of those assets needed to practice their faith. On the other hand, sale of those assets would allow significantly larger recoveries to those injured at the hands of Catholic clergy.[13] The courts must therefore determine how parishioners fit into a bankruptcy proceeding.

This Article addresses whether parishioners either have a right or should be permitted to intervene in the bankruptcy proceedings of the Roman Catholic dioceses. Different faiths, and even different churches within the same faith, organize their churches differently which may give rise to different rights in bankruptcy proceedings; this Article considers only the structure of three of the Roman Catholic Churches currently in bankruptcy.[14] It is important to note that the First Amendment's religion clauses may dictate that parishioners be granted a role (or at least have their interests represented) within the bankruptcy proceedings.[15] However, this Article considers only whether the

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Of course, even if the various parishes, schools, and other properties are not deemed property of the estate subject to liquidation to pay claims of creditors, the sale of some property may still be necessary to support the costs of the bankruptcy proceeding itself. *See, e.g.*, Joint Motion for Entry of Order Approving Stipulation Regarding: (1) Disposition of Proceeds of Sale of Real Property Located at 707 N. Cedar, Spokane, Washington, and (2) Deadline for Catholic Charities, Inc. to Commence Action Regarding Interest in Sale Proceeds, *In re* The Catholic Bishop of Spokane, No. 04-08822 (Bankr. E.D. Wash. July 14, 2006) (seeking approval of agreement between Diocese and Tort Claimants to allow sale of St. Ann's in order to pay for bankruptcy expenses).

13. *See* Jeff Wright, *Asset Fight Has Florence Church in a Fix*, THE REGISTER-GUARD, Feb. 1, 2005, at A1 (noting that "the archdiocese's worth could grow by tenfold or more—up to perhaps $500 million—if parish assets are included").

14. Indeed, the problems facing these archdioceses are not unique to the Catholic church. Ira C. Lupu & Robert W. Tuttle, *Sexual Misconduct and Ecclesiastical Immunity*, 2004 BYU L. REV. 1789. Because the Davenport, Iowa bankruptcy filing occurred in 2006, *see supra* note 4, it has not progressed to the point that the other bankruptcy filings have, and is not discussed in this Article. The author anticipates that it will progress in a similar fashion to the first three bankruptcies, with the benefit of the decisions already made in these three bankruptcy proceedings.

15. Lipson, *supra* note 8, at 365. Professor Lipson states "[I]f a diocese were effectively shut down (because all assets were sold) over the objection of the diocese and parishioners, those parishioners, and perhaps the bishop, may credibly claim that this use of the Bankruptcy Code 'substantially burdens' their exercise of religion." Professor Lipson further notes the ever-present conflict between the Free Exercise Clause and the Establishment Clause, in that use of the Bankruptcy Code may burden religious rights of parishioners by allowing federal law to govern how the church operates, but failure to use the Code may grant an unconstitutional preference to religion either if churches are excluded from certain provisions of the Code that apply to bankruptcies filed by other types of entities, or if certain religions are exempt from requirements that would force them to deviate from their foundational principles, while other churches are subject to those same requirements. *Id.* at 366.

Bankruptcy Code itself must or may allow parishioners a voice in the proceedings separately from any reliance on constitutional provisions.

This Article argues that where parishioners' interests will not or may not be adequately represented by their diocese in a bankruptcy case or adversarial proceeding, courts must allow parishioners to intervene to protect their interests. Part I discusses the status of the first three Catholic Church bankruptcy proceedings—Portland, Spokane, and Tucson.[16] Part II discusses the structure of the Roman Catholic Church in the United States, including both the canon law organization and the state law organization of the Church. Part III introduces the bankruptcy system's rules of both mandatory and permissive intervention. Part IV considers how parishioners fit into the bankruptcy system when their diocese files for bankruptcy protection and examines the conflicting roles presented to church leaders acting as debtors-in-possession in representing the interests of both parishioners and creditors in a bankruptcy proceeding. This Article concludes that the Bankruptcy Code and Federal Rules of Bankruptcy and Federal Rules of Civil Procedure permit intervention by parishioners in bankruptcy proceedings when the church-debtor is unwilling or unable to represent the interests of its parishioners.

I. THE BANKRUPTCY PROCEEDINGS

In Portland,[17] Spokane,[18] and Tucson,[19] numerous individuals claiming to have been sexually molested by church personnel have filed civil suits against the church and its personnel. The potential liability facing each diocese, as well as the costs of defending the abuse cases, have led these dioceses to declare bankruptcy. A bankruptcy case involves reaching a resolution between the debtor and its creditors. Within a bankruptcy case there may be numerous adversary proceedings to resolve individual issues. In each of the three cases discussed below, there are various adversary proceedings involving property ownership issues.

16. For a detailed analysis of the proceedings of each of these three bankruptcies, see Lipson, *supra* note 8, at 372–77.

17. *See infra* notes 20–30.

18. *See infra* notes 31–36.

19. *See infra* notes 37–43.

A. Portland, Oregon

The effect that the filing of a bankruptcy petition may have on parishioners within a diocese can be seen in the Portland bankruptcy case.[20] In that bankruptcy, tort claimants (as the Tort Claimants Committee) sought a declaratory judgment in an adversary proceeding that property belonged to the Archdiocese, rather than to the individual parishes.[21] The Archdiocese had listed many assets as being held in trust for the benefit of its parishes and, therefore, not subject to the bankruptcy.[22] If the court agrees with the Archdiocese, a minimum of assets would remain to distribute to aggrieved creditors including the tort claimants, but parishes would retain churches, schools, and cash to continue functioning.[23] The parishioners of many of the affected parishes organized as the Committee of Parishioners—Western Oregon.[24] This committee then sought to intervene in the Tort Claimants Committee's adversary proceeding,[25] and was granted the right to intervene in March of 2005.[26] However, the court ultimately sided with the Tort Claimants Committee on the substantive issue of property ownership, holding that the assets did not belong to the individual parishes.[27] The court declined

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20. *See* Portland Memorandum in Support of Motion to Intervene, *supra* note 12, at 12 ("Few proceedings have the potential to affect Catholic parishes more than does this one.").

21. Complaint (Declaratory Judgment re Property of the Estate), Tort Claimants Comm. v. Roman Catholic Archbishop of Portland (*In re* Roman Catholic Archbishop of Portland), Adv. Proc. No. 04-03292 (Bankr. D. Or. Aug. 11, 2004) [hereinafter Portland Complaint].

22. Portland Complaint, *supra* note 21, at 3–4 (listing various bank accounts, tangible assets, and realty).

23. The First Amendment implications of allowing a bankruptcy court to interfere in the property decisions of a church have been debated. *See, e.g.*, Patty Gerstenblith, *Civil Court Resolution of Property Disputes Among Religious Organizations*, 39 AM. U. L. REV. 513 (1990); Marianne Perciaccante, *The Courts and Canon Law*, 6 CORNELL J.L. & PUB. POL'Y 171 (1996). This Article does not refresh that debate, but rather assumes that a bankruptcy court may properly determine the meaning of canon law as needed to resolve such debates.

24. Committee of Parishioners—Western Oregon, Frequently Asked Questions, http://www.parishionerscommittee.org/faq.htm (last visited Dec. 27, 2006). The court went on to include all parishioners within the limits of the diocese as parties in the adversary proceeding. Steve Woodward, *Judge Widens Church Assets Case to All Parishioners*, THE OREGONIAN, July 23, 2005, at A1.

25. Motion to Intervene, *Tort Claimants Comm.* (*In re Archbishop of Portland*), Adv. Proc. No. 04-03292 (Feb. 3, 2005).

26. Order Granting Motion to Intervene, *Tort Claimants Comm.* (*In re Archbishop of Portland*), Adv. Proc. No. 04-03292 (March 22, 2005).

27. Memorandum Opinion (Tort Claimant Committee's Third Motion for Partial Summary Judgment) at 31, *Tort Claimants Comm.* (*In re Archbishop of Portland*), Adv. Proc. No. 04-03292 (Dec. 30, 2005).

to decide whether the use of these particular assets would violate the religious rights of the parishioners.[28] The property ownership decision is now on appeal.[29] The Tort Claimants Committee has filed a Disclosure Statement and competing Plan of Reorganization proposing full payment to all tort claimants using some of these assets, as well as future income.[30]

B. Spokane, Washington

Tort claimants in Spokane (as the Committee of Tort Litigants) also filed adversary proceedings to determine ownership of property in the Spokane bankruptcy proceeding.[31] The bankruptcy court granted partial summary judgment in favor of the Committee of Tort Litigants[32] and the diocese appealed.[33] On appeal, the district court reversed and remanded, citing the apparent failure of the bankruptcy court to consider numerous affidavits from parishioners and priests regarding the intent of the parties

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28. *Id.* at 30. The question of property ownership affects not only who receives the property at the end of the bankruptcy litigation, but also whether the property can be used within the bankruptcy litigation. The Committee of Parishioners argued that it should be permitted to use the assets to fund its participation in the bankruptcy, stating that "the Committee of Tort Claimants seeks to impose a Catch-22: it seeks to require the Committee of Parishioners to prevail on this ultimate issue [property ownership] as a precondition to accessing the funds that are essential for the parishes to prevail on the ultimate issue." Memorandum of Law in Support of Precautionary Motion Regarding Use of Parish Donations at 2, *In re* Roman Catholic Archbishop of Portland, No. 04-37154 (Bankr. D. Or. Apr. 4, 2005).

29. Order Granting Motion for Leave to Appeal Docket No. 3197 (Case No. 04-314), Docket Nos. 512, 513, and 514 (Case No. 04-3292), Tort Claimants Comm. v. Roman Catholic Archbishop of Portland (*In re* Roman Catholic Archbishop of Portland), No. 3:06cv00475 (filed Apr. 6, 2006). Notice of Appeal by Certain Defendants of Order Granting Tort Claimants Committee's Second Motion for Partial Summary Judgment, *Tort Claimants Comm.* (*In re Archbishop of Portland*), Adv. Proc. No. 04-03292 (Feb. 27, 2006); *see also* Order Granting Tort Claimants Committee's Third Motion for Partial Summary Judgment, *Tort Claimants Comm.* (*In re Archbishop of Portland*), Adv. Proc. No. 04-03292 (Feb. 17, 2006) (declaring test property to be property of the estate).

30. Tort Claimants Committee's Disclosure Statement, *Tort Claimants Comm.* (*In re Archbishop of Portland*), Adv. Proc. No. 04-03292 (Feb. 13, 2006).

31. Complaint for Declaratory Relief and Substantive Consolidation, Comm. of Tort Litigants v. Catholic Diocese of Spokane (*In re* Catholic Bishop of Spokane), Adv. Proc. No. 05-80038 (Bankr. E.D. Wash. Feb. 4, 2005) [hereinafter Spokane Complaint].

32. Memorandum Decision re: (1) Plaintiff's Motion for Partial Summary Judgment; (2) Various Motions to Dismiss; and (3) The Catholic Diocese of Spokane's Cross-Motion for Summary Judgment at 50, *Comm. of Tort Litigants* (*In re Bishop of Spokane*), Adv. Proc. No. 05-80038 (Aug. 26, 2006) (holding that "[t]he Disputed Real Property constitutes property of the estate").

33. Motion for Leave to Appeal & Notice of Appeal Transmittal to U.S. District Court, *Comm. of Tort Litigants* (*In re Bishop of Spokane*), Adv. Proc. No. 05-80038 (Sept. 20, 2005).

acquiring the property at issue.[34] The district court found "abundant" evidence "that the costs for the construction of Parish churches and schools on the subject properties were provided by the individual Parishes either through cash on hand or through loans obtained by the Parish and solely paid for by the individual Parish and its members."[35] Therefore, the district court held that the bankruptcy court's summary dismissal could not stand because an issue of material fact existed as to the parishioners' interest in church property.[36]

C. Tucson, Arizona

As in the Portland and Spokane bankruptcy proceedings, the tort claimants (as the Committee of Tort Litigants) in the Tucson bankruptcy sought a judgment declaring that the diocese owned the property of the various parishes, and that the property could be used to pay the claims of creditors.[37] The complaint was dismissed, with the court indicating that the complaint "is not appropriate at this time" without offering further explanation of its decision.[38] The Archdiocese of Tucson and its parishes attempted to avoid a costly dispute over insurability by entering into a

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34. Memorandum Opinion and Order Remanding to Bankruptcy Court at 20–21, Comm. of Tort Litigants v. Catholic Diocese of Spokane, No. 05-CV-274-JLQ (E.D. Wash. June 30, 2006). The district court also added in dicta that the bankruptcy court could have used canon law in its determination of the intent of the parties, but did not need to do so due to the overwhelming evidence of intent from the parishioners and priests via the affidavits filed. *Id.* at 20.

35. *Id.* at 19.

36. The district court placed special emphasis on writings created before the litigation began:

> The correspondence and documents regarding the negotiations and conveyance of title to the real property of St. Aloysius Parish appear to be the most illuminating evidence on the issue of the parties' actions and intent when Parish property in the Spokane Diocese was acquired and improved . . . . Attached to the Affidavit of Father Barnett is a letter Bishop Charles A. White of the Spokane Diocese wrote Father Fitzgerald, the Provincial of the Jesuit Order on November 30, 1935 . . . . This letter, written some 70 years before any issue arose as to ownership of Parish properties, clearly and unequivocally sets forth the role of the Bishop and the Diocese of Spokane as it relates to formal title of Parish real properties being placed in the name of the Diocese or the Bishop . . . . : "I would state further that in every case, I hold each parish responsible for its own obligations. Even when the parish properties are held under the title of the diocesan corporation, the Catholic Bishop of Spokane (the title of nearly all our parish properties) this form of tenure does not change the fact that they are parish properties, the diocesan corporation being a mere non-profit holding corporation which holds the various parish properties in trust for the faithful of the respective parishes."

Id. at 8–9.

37. Complaint for Declaratory Relief and Substantive Consolidation, Comm. of Tort Litigants v. Immaculate Conception Parish in Ajo (*In re* Roman Catholic Church of the Diocese of Tucson), Adv. Proc. No. 05-00117 (Bankr. D. Ariz. Mar. 17, 2005) [hereinafter Tucson Complaint].

38. Order, *Comm. of Tort Litigants* (*In re Diocese of Tucson*), Adv. Proc. No., 05-00117 (Mar. 25, 2005).

settlement agreement to determine how insurance proceeds would be paid in the bankruptcy proceeding.[39] The Archdiocese and the parishes agreed that the parishes would contribute two million dollars to the reorganization proceeding and release any claims to insurance proceeds; the tort claimants were not a party to the settlement agreement.[40] That settlement was, however, included in the diocesan Plan of Reorganization[41] which was, in turn, accepted by the tort claimants as a class[42] and confirmed by the court.[43]

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39. Debtor's Motion for Approval of Settlement Agreement with Parishes at 4, *In re* Roman Catholic Church of the Diocese of Tucson, No. 04-04721 (Bankr. D. Ariz. July 11, 2005). Some of the tort claimants expressed anger over the allocation of the settlement money in the Plan of Reorganization:

> By way of analogy, the Court is asked to conjure a man and his three sons (a gang) who have planned and executed 12 armed bank robberies—these are dangerous serious criminals. The police catch the father, and the prosecutors bring him to trial, where he is convicted but by fast talking only returns some of the loot. And the argument of the sons, who were full participants in the bank robberies, is that they will contribute some small change to the victims in exchange for release of all liability to the people they have injured. No prosecutor on earth would agree to it. So it is with the "gang of parishes." They either were actively engaged in the wrongdoing, or worse, did nothing about it and covered it up for decades, leaving the victims to go through hell on earth because of what they had done or failed to do.

Objection by 6 Class 10 Tort Claimants to Confirmation of Debtor's Third Amended and Restated Plan of Reorganization at 6, *Comm. of Tort Litigants* (*In re Diocese of Tucson*), Adv. Proc. No. 05-00117 (July 3, 2005). Of course, the analogy is weakened because not all of the settling parishes were involved in the torts of the other parishes and their employees.

The Tucson Diocese's plan of reorganization proposes to create a Settlement Trust, out of which all tort claims would be paid. Debtor's Third Amended and Restated Plan of Reorganization at 41–43, 49–50, *In re Diocese of Tucson*, No. 04-04721 (Sept. 21, 2005) [hereinafter Tucson Plan of Reorganization]. This trust would then pay the settled claim amounts of tort claimants. *Id.* at 42–43. The tort claimants could, however, opt out of the Settlement Trust and enter the Litigation Trust also created by the Plan. *Id.* at 49–50. All those in the Litigation Trust would litigate claims against the church and, at the end of the litigation, be paid the lesser of: any judgment in the case, $425,000, or a pro rata share of the Litigation Trust based on the final judgment amounts at trial. *Id.* The trusts will be funded by a combination of cash on hand, cash received from insurance, and proceeds of other actions. *Id.* at 52 (definition of "Fund").

40. Debtor's Motion for Approval of Settlement Agreement with Parishes at 4, *In re Diocese of Tucson*, No. 04-04721 (July 11, 2005).

41. Lipson, *supra* note 8, at 376 (citing Sheryl Kornman, *Diocese to Pay $10M Upfront as Plan OK'd*, TUCSON CITIZEN, July 12, 2005, at 4B).

42. Ballot Report and Certification of Acceptances and Rejections of Chapter 11 Plan for Debtor's Third Amended and Restated Plan of Reorganization Dated May 25, 2005 at 5–6, *In re Diocese of Tucson*, No. 04-04721 (July 8, 2005).

43. Order Confirming the Third Amended and Restated Plan of Reorganization Dated May 25, 2005, Proposed by the Roman Catholic Church of the Diocese of Tucson, *In re Diocese of Tucson*, No. 04-04721 (Aug. 1, 2005); *see also* Lipson, *supra* note 8, at 367, 434–35 (indicating that creditor's approval of the plan of reorganization may minimize Establishment Clause concerns).

II. THE STRUCTURE OF THE ROMAN CATHOLIC DIOCESES AND ARCHDIOCESES

In both its state law structure and its canon law structure, the Roman Catholic Church operates under the notion of individual parishes collecting together as one diocese, with the bishop serving as the administrator of the diocese and all assets located within it.[44] When those assets become part of a bankruptcy proceeding, however, their ownership becomes critically important to the diocese, its creditors, and all those who serve and are served by the diocese. To the extent that these parties are interested in the proceedings and any potential sale or distribution of assets, they need a mechanism for sharing their concerns with the court.

This Part considers the organization of the Roman Catholic Church in the United States under both canon law and state law. First, this Part considers the internal structure of the Roman Catholic Church. Next, this Part reviews the options for recognition of the diocese as an entity by the state in which it lies. Finally, this Part considers the potential conflict that may exist between the need to structure an entity under state law to limit liability, and the need to structure the Roman Catholic Church internally to ensure the hierarchical structure mandated by the doctrine of the Church.

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44. In a decision regarding the Archdiocese of Boston, the Vatican indicated it believes that the diocese holds all assets for the benefit of parishes located within a diocese. Michael Paulson, *Vatican Stops Diocese in Taking Parish Assets*, BOSTON GLOBE, Aug. 11, 2005, at A1. At the time of the Vatican's decision, the issue of property ownership and trust was being considered in the Spokane Bankruptcy and, indeed, was decided by the court within weeks of the Vatican's statements. *See* Memorandum Decision re: (1) Plaintiff's Motion for Partial Summary Judgment; (2) Various Motions to Dismiss; and (3) The Catholic Diocese of Spokane's Cross-Motion for Summary Judgment, Comm. of Tort Litigants v. Catholic Diocese of Spokane (*In re* Catholic Bishop of Spokane), Adv. Proc. No. 05-80038 (Bankr. E.D. Wash. Aug. 26, 2005) [hereinafter Spokane Memorandum Decision]. The Spokane bankruptcy court held that the property belonged to the diocese, rather than to individual parishes. *Id.* at 50 ("[A]n express trust is created whereby the Bishop, a natural person, holds legal title to the Disputed Real Property in trust for the benefit of the debtor diocese which holds the beneficial interest. The Disputed Real Property constitutes property of the estate."). This decision has been appealed to the U.S. District Court. Notice of Appeal of Orders of Court Entered Aug. 26, 2005 and Docketed as Nos. 321, 322, 323, 324, *Comm. of Tort Litigants* (*In re Bishop of Spokane*), Adv. Proc. No. 05-80038 (Sept. 6, 2005).

A. Canon Law Organization[45]

The Roman Catholic Church is organized hierarchically. At the very top of the hierarchy is the Pope, the highest bishop of the Catholic Church.[46] The Church is then divided into dioceses and archdioceses, each led by a bishop or archbishop.[47] Within an individual diocese lie several parishes, which serve as the primary point of contact with the church structure for most parishioners.[48]

Canon law[49] is the internal legal doctrine of the Roman Catholic Church. It governs all members of the Church,[50] and developed from church documents, Councils, and papal dictates.[51] Canon law defines the structure of the Church and divides the Church into dioceses, each under the care of a bishop.[52] The bishop is the sole representative of the diocese.[53] Generally, the diocesan division is territorial.[54] Although there

45. The author recognizes that a number of constitutional issues regarding religious organizations arise in this context, including the relationship between canon law and state law. For purposes of this Article, the author assumes that canon law may be considered in determining certain aspects of property ownership, such as donative intent when evaluating a claim that property is held in trust. For an interesting article on the conflict between state laws and church autonomy in the sexual abuse cases, see Perry Dane, *"Omalous" Autonomy*, 2004 BYU L. REV. 1715.

46. 1983 CODE C.331.

47. 1983 CODE C.336, 381, 393. Generally, dioceses are led by a bishop and archdioceses are led by an archbishop, but there are exceptions to this rule.

48. 1983 CODE C.374, § 1.

49. The current Code of Canon Law became effective on January 25, 1983, during the papacy of Pope John Paul II, after a long process of divining the Code. Ioannes Paulus PP. II, Apostolic Constitution, Sacrae Disciplinae Leges, *in* CODE OF CANON LAW xi–xvi (Canon Law Soc'y of Am. trans., Latin-English ed. 1983).

50. 1983 CODE C.11, 12.

51. *See* John A. Alesandro, *General Introduction* to THE CODE OF CANON LAW: A TEXT AND COMMENTARY 1, 1–8 (James A. Coriden, Thomas J. Green, & Donald E. Heintschel eds., Paulist Press 1985); *see also* THE OXFORD DICTIONARY OF WORLD RELIGIONS 194 (John Bowker ed. 1997).

52. 1983 CODE C.369 ("A diocese is a portion of the people of God which is entrusted for pastoral care to a bishop with the cooperation of the presbyterate, so that, adhering to its pastor and gathered by him in the Holy Spirit through the gospel and the Eucharist, it constitutes a particular church in which the one, holy, catholic and apostolic Church of Christ is truly present and operative."). The Code of Canon Law also provides for "territorial prelature[s] or territorial abbac[ies]," "apostolic vicariate[s] or apostolic prefecture[s]," and "apostolic administration" in situations where people are not within a diocese. *See* 1983 CODE C.370, 371.

53. 1983 CODE C.393.

54. 1983 CODE C.372.

is just one Church, each diocese operates as a separate "juridic person,"[55] which is then further separated into individual parishes.[56] In many ways, this further division into parish juridic persons mirrors a collection of sister corporations controlled by the same parent.[57]

Although the bishop is responsible for the care of his diocese, he is not its only officer. Each diocese must also have a finance council to oversee the budget of the diocese,[58] and a finance officer "to administer the goods of the diocese."[59] Each diocese also has a pastoral council charged with making recommendations about "pastoral works in the diocese."[60]

The structure of an individual parish within a diocese mirrors the structure of the diocese as a whole. "A legitimately erected parish possesses juridic personality by the law itself."[61] Parishioners generally fall within an individual parish's jurisdiction based on the location of the parishioners.[62] Within each parish, a pastor is appointed by the bishop to run the affairs of that parish.[63] As with the bishop and the diocese, "[i]n all juridic affairs the pastor represents the parish according to the norm of law."[64] This representation includes responsibility for parish property.[65] Like the diocese itself, each parish must have a finance

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55. Canon law defines "juridic persons" as "subjects in canon law of obligations and rights which correspond to their nature." 1983 CODE C.113, § 2. The Canons expand on that definition, noting that juridic persons are established by law or decree to further "works of piety, of the apostolate, or of charity, whether spiritual or temporal." 1983 CODE C.114. As long as the juridic person continues to operate, its existence is continual unless revoked. 1983 CODE C.120, § 1.

56. 1983 CODE C.373, 374.

57. Tucson Disclosure Statement, *supra* note 6, at 15 ("According to Canon Law, a 'juridic person' is the equivalent of a corporation in civil law."); *id.* at 18 ("A juridic person is an artificial person, distinct from all natural persons or material goods, constituted by competent ecclesiastical authority for an apostolic purpose, with a capacity for continuous existence and with canonical rights and duties like those of a natural person (e.g., to own property, enter into contracts, sue or be sued)."); *see also* Lipson, *supra* note 8, at 399 (analogizing Catholic Church to parent corporation).

58. 1983 CODE C.492, 493.

59. 1983 CODE C.494.

60. 1983 CODE C.511.

61. 1983 CODE C.515, § 3; *see also* Tucson Disclosure Statement, *supra* note 6, at 19.

62. 1983 CODE C.518.

63. 1983 CODE C.515, § 1; *see also* Tucson Disclosure Statement, *supra* note 6, at 19. Exceptions can be made to provide that a parish be run by someone other than a pastor in exceptional circumstances. *See* 1983 CODE C.517, 520.

64. 1983 CODE C.532.

65. *Id.* (referring to 1983 CODE C.1281–1288).

council.[66] To the extent that the bishop deems it necessary, a pastoral council may be created to assist the pastor with parish activities.[67]

Although the individual parishes operate as microcosms of the overall diocese, the diocese itself controls many of the actions of each parish, particularly with regard to financial matters. Each parish has a finance council whose duty is merely to "aid the pastor in the administration of parish goods" according to "norms issued by the diocesan bishop."[68] Each diocese also controls the sale or disposition of goods within the parish by setting standards for when approval of the bishop and the diocesan finance counsel is required for leasing and disposition of church property.[69] Although the Roman Catholic Church has internal governance mechanisms, in order to enjoy the benefits of state law incorporation, a diocese must also incorporate according to state law rules.

B. State Law Organization

Various state law mechanisms exist for structuring a church,[70] but many churches establish a corporate structure in order to enjoy the benefits of incorporation.[71] A primary benefit is that governance of the

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66. 1983 CODE c.537.

67. 1983 CODE c.536.

68. 1983 CODE c.537. The parish finance council's function is limited compared to the diocese's finance council. The parish finance council's role is more akin to that of the diocese's finance officer.

69. 1983 CODE c.1292, 1297. Indeed, permission of the Pope may be required for particular dispositions. 1983 CODE c.1292, § 2. Further, the Pope is "the supreme administrator and steward of all ecclesiastical goods." 1983 CODE c.1273.

70. Patty Gerstenblith, *Associational Structures of Religious Organizations*, 1995 BYU L. REV. 439, 441 (listing "the charitable trust, the unincorporated association, the corporation sole, religious corporations, and not-for-profit corporations" as possible organizational structures available to churches, depending upon state of organization).

71. *See id.* at 444–65 (discussing the relative advantages and disadvantages of the various forms of corporation organization and the disadvantages of failure to incorporate); Jill S. Manny, *Governance Issues for Non-Profit Religious Organizations*, 40 CATH. LAW. 1, 1–2 (2000) ("The most popular and perhaps the best way to effectively reduce risk is to separately incorporate the parishes, the dioceses, and the various organizations that support the parishes and dioceses, such as fund-raising entities. If properly structured, the incorporation of each organization will limit the liability of the individual parishes and diocese by reducing their exposure to the actions and negligence of parish employees, volunteers, and associated parties.").

For further discussion of state law incorporation, see generally 1 WILLIAM MEADE FLETCHER ET AL., FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS §§ 5–14 (perm. ed., rev. vol. 1999).

business is separate from the ownership of the business—directors and officers run the corporation, while shareholders own the corporation and enjoy the ultimate benefits of the corporation's profitability. This structure allows the shareholders to limit their risk. Shareholders invest in the company, but in most circumstances are only liable for that initial investment. Wrongdoing by those running the company is not personally attributable to the individual shareholders.[72] Each of the Portland, Tucson, and Spokane dioceses incorporated as a corporation sole,[73] a form which lacks traditional shareholders and traditional internal corporate structures.

The corporation sole allows a church to incorporate the position of its primary leader.[74] In the dioceses of the Roman Catholic Church, that leader is the bishop. Thus, the corporation sole allows incorporation of the bishop's position. By incorporating the position of bishop, the church maintains a constant state of incorporation; when a new bishop replaces a deceased, retiring, or removed bishop, the new bishop becomes the corporation.[75] All assets of the diocese rest in the hands of the bishop.[76]

In each of the Catholic Church bankruptcies, the diocese was incorporated under state law. The individual parishes, however, were not. The legal organization of the parishes and their dioceses therefore raise significant issues regarding the ownership of parish property.[77] As

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72. *But see infra* note 221 (noting the potential problem of piercing the corporate veil).

73. Portland Disclosure Statement, *supra* note 6, at 15–16; Debtor's Plan of Reorganization at 1, *In re* The Roman Catholic Church of the Diocese of Tucson, No. 04-04721, (Bankr. D. Ariz. Sept. 20, 2004) [hereinafter Tucson Debtor's Plan of Reorganization]; Spokane Petition, *supra* note 3. For brevity's sake, this Article focuses on the issues with regard to the Portland, Tucson, and Spokane dioceses. However, property issues arise for churches which are not Roman Catholic, and for churches which are not organized as a corporation sole. *See, e.g.*, Elizabeth Austin, *Exodus. Numbers. Judges. As Conservative Parishes Leave the Liberal Episcopal Church, Who Shall Inherit the Real Estate?*, LEG. AFF., May/June 2004, at 65 (noting that courts need to determine the ownership rights of property involved in the Episcopalian church disagreements). Bankruptcy also affects churches that are not Roman Catholic. *See, e.g.*, Kim Nilsen, *Christian School Shutters; Bank Takes Control*, TRIANGLE BUS. J., June 20, 2003, *available at* http://triangle.bizjournals.com/triangle/stories/2003/06/23/story8.html (discussing bankruptcy of Love Christian Center Church).

74. Hayes, *supra* note 12, at 4; Gerstenblith, *Associational Structures*, *supra* note 70, at 454.

75. Hayes, *supra* note 12, at 4; Gerstenblith, *Associational Structures*, *supra* note 70, at 455.

76. Gerstenblith, *Associational Structures*, *supra* note 70, at 455. *Roundtable Discussion: Religious Organizations Filing for Bankruptcy*, 13 AM. BANKR. INST. L. REV. 25, 39 (Spring 2005) [hereinafter Roundtable Discussion].

77. *See* Portland Complaint, *supra* note 21; Tucson Complaint, *supra* note 37; Spokane Complaint, *supra* note 31 (each seeking declaratory judgment that property is of the estate).

noted in one of the bankruptcies, "[t]he closest analogous entity to a Parish commonly recognized under [state] law is an unincorporated association."[78] By analogy to businesses organized under state law, churches are organized as one large corporation (the diocese), with several subsidiaries, each operating as an unincorporated entity (the parish). The "parent" corporation holds legal title to all property of the unincorporated entities.[79]

Although each diocese may have chosen its state law structure for different reasons, it seems likely that many incorporated to control liability while still maintaining control of the ecclesiastic functions of the church:

> [T]he Archbishop desired that archdiocesan corporations be structured civilly to protect against internal or external threat to their Catholic autonomy. . . . [T]o preserve Catholic autonomy, we sought a means to ensure that all archdiocesan corporations understood, accepted, and advanced the doctrinal and moral teaching of the Catholic Church in their governance, management, administration, and activity.[80]

This corporate structure reflects the Canon Law structure of the church, in that it focuses on the diocese, rather than on individual parishes within the diocese. In so doing, however, it appears that the churches did not fully consider the possibility that such a corporate structure would jeopardize the assets of individual parishes due to the actions of other parishes.[81]

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78. Tucson Disclosure Statement, *supra* note 6, at 19.

79. *See* Tucson Disclosure Statement, *supra* note 6, at 19.

80. Reverend Edward L. Buelt & Charles Goldberg, *Canon Law & Civil Law Interface: Diocesan Corporations*, 36 CATH. LAW. 69, 70 (1993) (discussing incorporation of the Archdiocese of Denver). The authors provide some indication that such a structure was designed to allow the archbishop to control situations such as the sexual abuse cases, noting that "in the event that an employee's activities were contrary to the magisterium of the Church, [the Archbishop] wanted the ability to intervene promptly." *Id.* at 77. The corporate structure itself also provided notice to parishioners that the assets of an individual parish could be used by the diocese. *Id.* at 78 ("He also wanted the faithful made aware that, under the Code of Canon Law, he could utilize funds of a related nonprofit corporation for the benefit of the Archdiocese of Denver if necessary.").

81. *See Roundtable Discussion*, *supra* note 76, at 39–41.

III. INTERVENTION IN BANKRUPTCY PROCEEDINGS

The Bankruptcy Code expressly gives many parties the right to be part of a bankruptcy proceeding.[82] For parties not expressly given a right to intervene, the courts are left to determine how traditional principles of legal standing[83] and the Bankruptcy Code provisions work together to ensure fair representation of all necessary parties. Parishioners are not automatically granted a right to intervene in a bankruptcy proceeding. Thus, the courts must consider the special relationship of parishioners to their church to determine if and when those parishioners should be allowed to join bankruptcy proceedings.

Two primary policies conflict when courts determine whether to allow a third party to intervene in a bankruptcy proceeding. On the one hand, a fair and complete adjudication dictates allowing anyone who may be impacted by a bankruptcy proceeding to participate.[84] On the other hand, judicial efficiency leans in favor of limiting proceedings, which are already inherently filled with multiple interests, to those most affected by the bankruptcy.[85] Ultimately, the court must exercise its

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82. 11 U.S.C. § 1109(b) (2000) (providing that "the debtor, the trustee, a creditors' committee, an equity security holders' committee, a creditor, an equity security holder, or any indenture trustee may raise and may appear and be heard on any issue in a case under this chapter").

83. In addition to the statutes governing participation in bankruptcy proceedings, the U.S. Supreme Court has set forth a three-part test for determining whether a party has standing to be heard in any proceeding. Those requirements are that: (1) the participant be harmed, (2) the harm is the result of the challenged actions, and (3) that the requested relief will likely redress such harm. Valley Forge Christian Coll. v. Ams. United for Separation of Church and State, Inc., 454 U.S. 464, 472 (1982). These requirements combine to require that the potential intervenor have a "'personal stake in the outcome' of a case." *In re* Lewis, 273 B.R. 739, 742 (Bankr. N.D. Ga. 2001) (citing Baker v. Carr, 369 U.S. 186, 204 (1962)). They further limit the bankruptcy court's ability to grant a right to intervene, even when the statutory requirements are met. *In re* Delta Underground Storage Co., 165 B.R. 596, 598 (Bankr. S.D. Miss. 1994). The Bankruptcy Code's intervention provisions do not alter constitutional law principles of standing. *In re* James Wilson Assocs., 965 F.2d 160, 169 (7th Cir. 1992). The *Lewis* court, however, noted the difficulties of applying this standard in a bankruptcy context:

> Unlike a traditional two-party lawsuit, determining whether a party has standing in a bankruptcy proceeding is a somewhat esoteric question. A bankruptcy proceeding is not about just the interests of a plaintiff and a defendant whereby one party alleges an injury caused by conduct of another party. A bankruptcy proceeding involves the rights and obligations of a debtor, creditors, and trustee, among others. Moreover, bankruptcy involves the administration of an estate's property and necessarily affects other parties' rights and interests vis-à-vis that property.

In re Lewis, 273 B.R. at 742.

84. *See* Official Unsecured Creditors' Comm. v. Michaels (*In re* Marin Motor Oil, Inc.), 689 F.2d 445, 457 (3d Cir. 1982) (discussing 11 U.S.C. § 1109(b) and its relationship to due process).

85. *In re* First Humanics Corp., 124 B.R. 87, 90–91 (Bankr. W.D. Mo. 1991) (citations omitted); *In re* River Bend-Oxford Assocs., 114 B.R. 111, 114–15 (Bankr. D. Md. 1990) (permitting partners

discretion in determining whether to allow a non-named party to intervene.[86]

A. Mandatory Versus Permissive Intervention

The Bankruptcy Code (Code)[87] and the Federal Rules of Bankruptcy Procedure (FRBP) include a variety of sections regarding intervention in a bankruptcy proceeding. Section 1109 of the Code states that a party-in-interest *must* be allowed to intervene in any bankruptcy case;[88] FRBP 2018 *permits* intervention for any interested party with cause to intervene.[89] Rule 24 of the Federal Rules of Civil Procedure (FRCP) is incorporated by reference into FRBP 7024 and provides for mandatory intervention:[90]

> (1) when a statute of the United States confers an unconditional right to intervene; or
>
> (2) when the applicant claims an interest relating to the property or transaction which is the subject of the action and the applicant is so situated that the disposition of the action may as a practical matter impair or impede the applicant's ability to protect that interest, unless the applicant's interest is adequately represented by existing parties[;][91]

and for permissive intervention:

> (1) when a statute of the United States confers a conditional right to intervene; or

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of a partnership that was itself a limited partner of the debtor to file a plan of reorganization due to unrepresented financial interests in the bankruptcy).

86. *In re* Addison Cmty. Hosp. Auth., 175 B.R. 646, 651 (Bankr. E.D. Mich. 1994) (citing Benny v. England, 791 F.2d 712 (9th Cir. 1986)); *In re* City of Bridgeport, 128 B.R. 686, 687 (Bankr. D. Conn. 1991); Rollert Co. v. Charter Crude Oil Co., 50 B.R. 57, 64 (Bankr. W.D. Tex. 1985).

87. 11 U.S.C. §§ 101–1527.

88. 11 U.S.C. § 1109(b) ("A party in interest, including the debtor, the trustee, a creditors' committee, an equity security holders' committee, a creditor, an equity security holder, or any indenture trustee, may raise and may appear and be heard on any issue in a case under this chapter.").

89. FED. R. BANKR. P. 2018(a) ("In a case under the Code, after hearing on such notice as the court directs and for cause shown, the court may permit any interested entity to intervene generally or with respect to any specified matter."). Though FRBP 2018 includes other intervention provisions, those provisions apply specifically to the State Attorney General, labor unions, and Chapter 9 cases, and thus would not be applicable herein.

90. FED. R. BANKR. P. 7024 ("Rule 24 F.R.Civ.P. applies in adversary proceedings.").

91. FED. R. CIV. P. 24(a).

(2) when an applicant's claim or defense and the main action have a question of law or fact in common.[92]

The Advisory Committee Notes for FRBPs 7024 and 2018 indicate that FRBP 7024 governs adversary proceedings and FRBP 2018 governs "cases."[93] In analyzing a potential intervenor's rights, it is critical to determine two things—first, is the potential intervenor seeking to intervene in an adversary proceeding or a bankruptcy case; second, is the potential intervenor arguing that intervention is mandatory or permissive?

The interplay of section 1109, FRBP 7024 and FRBP 2018 can be seen in Figure 1.

Figure 1: Mandatory and Permissive Intervention in Bankruptcy Cases and Adversary Proceedings

	Type of Proceeding	
Type of Intervention	Bankruptcy Case	Adversary Proceeding
Mandatory Intervention	Party-in-interest under section 1109	Unrepresented and significant interest in property under FRBP 7024 (referencing FRCP 24(a))
Permissive Intervention	Interested entity with cause under FRBP 2018	Common question under FRBP 7024 (referencing FRCP 24(b))

The language of section 1109 mentions only bankruptcy *cases*, with no mention of whether adversary proceedings are also included within

92. FED. R. CIV. P. 24(b).

93. FED. R. BANKR. P. 2018, advisory committee's note ("This rule does not apply in adversary proceedings. For intervention in adversary proceedings, see Rule 7024."); FED. R. BANKR. P. 7024, advisory committee's note ("A person may seek to intervene in the case under the Code or in an adversary proceeding relating to the case under the Code. Intervention in a case under the Code is governed by Rule 2018 and intervention in an adversary proceeding is governed by this rule.").

its reach. Courts have interpreted this language differently, with some applying section 1109's mandatory intervention rules in adversary proceedings, and others limiting section 1109 to cases alone.[94] Those courts that broaden section 1109's scope to include adversary proceedings sometimes cite FRCP 24's statement that mandates intervention when required by another statute.[95] To find that section 1109, which expressly provides a right to be heard in a "case," also applies to adversary proceedings, defies the separation which is expressly provided for in the Advisory Notes to each of FRBPs 2018 and 7024. However, the Code provisions trump the FRBP provisions (and, even more so, the Advisory Committee Notes to the FRBPs) in the case of a conflict.[96] Because a "case" is not defined in the Code, there does not seem to be a conflict in the literal language of the provisions. Furthermore, even if section 1109 does not apply to adversary proceedings, the factors for determining "party-in-interest" status under section 1109 mirror the considerations for mandatory intervention under FRCP 24(a)(2) in that both consider whether the putative intervenor has a substantial interest in the case sufficient to require intervention.[97]

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94. *Compare* Official Unsecured Creditors' Comm. v. Michaels (*In re* Marin Motor Oil, Inc.) 689 F.2d 445 (3d Cir. 1982) *and* Gleason v. Commonwealth Cont'l Health Care, 147 B.R. 813 (Bankr. S.D. Fla. 1992) *with* 4 WILLIAM L. NORTON, JR. & WILLIAM L. NORTON III, NORTON BANKRUPTCY LAW AND PRACTICE 2d § 80:2 (2006) (citing Fuel Oil Supply & Terminaling v. Gulf Oil Corp., 762 F.2d 1283 (5th Cir. 1985)) *and* 4A Bankr. Service Law. Edition (West) § 42:377 (July 2005) (citing *In re* 995 Fifth Ave. Assocs., L.P., 157 B.R. 942 (Bankr. S.D.N.Y. 1993) (no mandatory intervention right in adversary proceedings)). *See also* Vermejo Park Corp. v. Kaiser Coal Corp. (*In re* Kaiser Steel Corp.), 998 F.2d 783, 790 (10th Cir. 1993) ("Intervention in a bankruptcy case and intervention in an adversary proceeding conducted in the bankruptcy case must be sought separately."); Kenneth N. Klee & K. John Shaffer, *Creditors' Committees Under Chapter 11 of the Bankruptcy Code*, 44 S. CAL. L. REV. 995, 1046–47 (1993).

95. *See, e.g.*, *Gleason*, 147 B.R. at 815.

96. *See* FED. R. BANKR. P. 1001, advisory committee's notes (noting that FRBPs are designed to be consistent with the Code); Russell A. Eisenberg & Frances Gecker, *Due Process and Bankruptcy: A Contradiction in Terms?*, 10 BANKR. DEV. J. 47, 51 (1993/1994). For an extensive analysis of this issue, see Jennifer M. D'Angelo, Comment, *If You Can't Beat Them, Join Them: Inclusive Joinder and the Filtering of Article III Status into Bankruptcy Courts*, 22 EMORY BANKR. DEV. J. 603 (2006).

97. The Third Circuit has considered intervention by a creditor's committee, a group specifically listed as a party-in-interest under section 1109. *In re* Marin Motor Oil, Inc., 689 F.2d 445. Ultimately, that court held that section 1109 creates an absolute right of intervention in adversary proceedings as well as cases, focusing on very practical considerations: "[m]ost litigated matters in a bankruptcy case are adversary proceedings." *Id.* at 450. To bar the creditor's committee "would drastically restrict the rights of parties to appear and be heard." *Id.* Further, the court dismissed the argument that such an interpretation of section 1109 would unduly burden adversary proceedings, finding that "relatively few individuals would have enough interest in the outcome of an adversary proceeding to seek to intervene." *Id.* at 453. *In re Marin* is often cited for this liberal interpretation

B. Bankruptcy Cases Versus Adversary Proceedings

In order to determine the appropriate Code provision or Rule of Procedure to use in determining a party's ability to intervene, it is first necessary to determine whether the proceeding is an adversary proceeding. Bankruptcies begin with the filing (either by the debtor or by its creditors) of a bankruptcy petition[98] under one of five chapters[99] of the Code. Chapter 11 deals with reorganization and prescribes the means by which the debtor's assets may be distributed among its creditors.[100] Each of the church bankruptcies discussed herein was filed by the archdiocese, diocese, or bishop under Chapter 11.[101] Either the debtor (known as the "debtor-in-possession")[102] or a trustee assigned by the Bankruptcy Court runs the Chapter 11 bankruptcy.[103] The debtor-in-possession or trustee is responsible for continuing operations of the business (if applicable), creating a plan for the reorganization of the debtor,[104] and executing that plan once confirmed.[105] A great deal of negotiation and compromise goes into a successful Chapter 11 proceeding. Creditors who wish to be paid in a bankruptcy proceeding generally file a proof of claim indicating their right to payment.[106] Once approved, the claim is paid under the distribution scheme dictated by the Code.[107] This process, beginning with the filing of a petition and

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of section 1109. *See, e.g.*, Term Loan Holder Comm. v. Ozer Group, L.L.C. (*In re* Caldor Corp.) 303 F.3d 161, 164–65 (2d Cir. 2002); Phar-Mor, Inc. v. Coopers & Lybrand, 22 F.3d 1228, 1230 (3d Cir. 1994); *In re* Amatex Corp., 755 F.2d 1034, 1040 (3d Cir. 1985). But the *In re Marin* decision pertained only to the definition of a "case," not of a "party-in-interest." *See In re Marin*, 689 F.2d at 450.

98. 11 U.S.C. §§ 301(a), 303(b) (2000).

99. *Id.* at §§ 701–784 (ch. 7), §§ 901–946 (ch. 9), §§ 1101–1174 (ch 11), §§ 1201–1231 (ch. 12), §§ 1301–1330 (ch. 13).

100. *Id.* §§ 1101–1174 (ch. 11).

101. Portland Petition, *supra* note 1, at 1; Tucson Petition, *supra* note 2, at 1; Spokane Petition, *supra* note 3, at 1.

102. 11 U.S.C. § 1101(1).

103. *Id.* § 1106.

104. *Id.* § 1106(a)(5).

105. *Id.* § 1106(a)(1) (referencing *id.* § 704(2), (5), (7)–(9)).

106. *Id.* § 501; *see also* S. REP. NO. 95-989, at 61 (1978), *as reprinted in* 1978 U.S.C.C.A.N. 5787, 5847 (legislative history of 1978 Act stating "[i]n general, however, unless a claim is listed in a . . . chapter 11 case and allowed as a result of the list, a proof of claim will be a prerequisite to allowance for unsecured claims").

107. In Chapter 7 of the Code, the distribution scheme is outlined for all cases. 11 U.S.C. § 726. In the remaining chapters, the distribution scheme is submitted for approval as part of a plan. *Id.* §§ 941, 1123, 1222, 1322.

continuing through payment of claims in bankruptcy, is a "bankruptcy case."

Adversary proceedings are a special type of proceeding within a bankruptcy case. An adversary proceeding is, essentially, a trial within the bankruptcy,[108] and usually begins with a complaint. It involves the same procedural rules as litigation in other federal courts, including complaints, answers, counter- and cross-claims, and discovery.[109] Not every matter in a bankruptcy case qualifies as an adversary proceeding; the Code expressly dictates those matters which may be adversary.[110] The property ownership disputes in the Portland, Tucson, and Spokane bankruptcies are adversary proceedings because they involve proceedings to determine the interests of parties in property that may be part of the estate.[111]

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108. 6 NORTON & NORTON, *supra* note 94, § 138:4.

109. *See generally* FED. R. BANKR. P. 7001–7087.

110. FRBP 7001 identifies proceedings in bankruptcy that qualify as adversary proceedings, including proceedings:

- to recover assets of the debtor or the estate, with some exceptions;
- to establish the existence, priority, or amount of a lien, except for liens on exempt property;
- to approve the sale of property jointly owned by the estate;
- to determine or oppose a discharge;
- to reverse confirmation of a reorganization plan;
- to determine the propriety of "injuncti[ve] or . . . equitable relief" outside of a plan of reorganization;
- to subordinate a claim outside of the plan of reorganization; and
- to transfer an action pending in another jurisdiction to the bankruptcy case's district.

The realm of non-adversary proceedings is not as clearly defined as that of adversary proceedings, but in the author's experience includes the following:

- bankruptcy administration, including whether to file for bankruptcy and in which chapter, hiring of bankruptcy professionals, opposition to appointment of a trustee, conversion of the bankruptcy into another chapter of the Bankruptcy Code, and establishment of committees;
- proceedings regarding property of the estate that are not adversary proceedings, including adequate protection of creditors, termination of the automatic stay, disposition of property of the estate, borrowing by the estate, continuation or termination of executory contracts;
- claims, including priority and payment on claims; and
- the plan of reorganization.

111. FED. R. BANKR. P. 7001; Portland Complaint, *supra* note 21; Tucson Complaint, *supra* note 37; Spokane Complaint, *supra* note 31 (each complaint seeking declaratory judgment that property is of the estate).

C. *Permissive and Mandatory Intervention in Bankruptcy Cases*

Both the permissive and mandatory intervention standards in bankruptcy cases indicate that a third party may or must be permitted to intervene in cases when that party has an interest in the case. For a parishioner, there are two possible means of intervention in a bankruptcy case. The first, section 1109 of the Code, provides for mandatory intervention. The other, FRBP 2018, provides for permissive intervention. Both share a common standard for the court to consider—whether the parishioners are sufficiently interested in the outcome of the case to justify intervention of yet another party into a bankruptcy case. Code section 1109 provides that "[a] *party-in-interest*, including[112] the debtor, the trustee, a creditors' committee, an equity security holders' committee, a creditor, an equity security holder, or any indenture trustee, may raise and may appear and be heard on any issue in a case under this chapter."[113] Thus, if a potential intervenor can establish that it is a "party-in-interest" it *must* be permitted to intervene in the bankruptcy case pursuant to section 1109.[114] If a party cannot establish that it is a "party-in-interest" its only other avenue for intervention it to establish that it *should* be permitted to intervene in the case under FRBP 2018.[115]

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112. The Code expressly provides that variations of "include" do not restrict the list to those mentioned. 11 U.S.C. § 102(3).

113. *Id.* § 1109(b) (emphasis added).

114. *But see* Kowal v. Malkemus (*In re* Thompson) 965 F.2d 1136, 1141–42 (1st Cir. 1992) (indicating that even section 1109 does not provide an absolute right to intervene in every matter, leaving some discretion to the courts to determine whether intervention is necessary).

115. The Code generally provides substantive provisions, while the FRBPs and FRCPs provide procedural guides. Although the "may" and "must" provisions of FRBP 2018 and section 1109 indicate that these provisions are separate, at least one court has held that FRBP 2018 simply provides the mechanism for implementing section 1109 of the Code. Hasso v. Mozsgai (*In re* La Sierra Fin. Servs., Inc.) 290 B.R. 718, 728 (B.A.P. 9th Cir. 2002). If so, there is no distinction between a "party-in-interest" and an "interested party," and the "causation" required under FRBP 2018 would simply be the interest that is sufficient to create "party-in-interest" status. *See Hasso* (*In re La Sierra Fin. Servs.*), 290 B.R. at 728. Combining these terms, however, creates some interpretative problems. FRBP 2018 governs permissive intervention. But one of the requirements of FRBP 2018, interest of the party, leads to mandatory intervention under section 1109. If "party-in-interest" and "interested party" are equivalents, and FRBP 2018 just provides the implementation procedures for section 1109, it seems unnecessary for FRBP 2018 to add the causation requirement or to permit judicial discretion regarding intervention. One court has explained the intersection of section 1109 and FRBP 2018 as follows: "Rule 2018(a) provides for intervention by entities not otherwise having a right to participate in the bankruptcy case under section 1109 or other provisions." *In re* Addison Cmty. Hosp. Auth., 175 B.R. 646, 650 (Bankr. E.D. Mich. 1994) (citations omitted).

Although section 1109 and other sections of the Code provide rights for a party-in-interest, the Code itself does not define what constitutes a party-in-interest.[116] Parishioners are not listed as parties-in-interest. However, the list in section 1109 is not exclusive,[117] and the term "party-in-interest" is never defined within the Code. Case law dictates that the phrase "party-in-interest" must be construed liberally,[118] ensuring that those with a sufficient interest in the proceeding are given an opportunity to participate.[119] In a business reorganization, a multitude of parties may have an interest in the proceeding:

> The workout[120] will be cause for many parties who have some relationship to or depend on the debtor's business to be concerned and watchful as the workout unfolds. Employees, retirees, shareholders, lessees, mass tort claimants, franchisees, franchisers, labor unions, government authorities, customers, distributors, and others will react to the possible termination, sale, modification, or relocation of the debtor's business. While many of these interested parties may not appear to be major players in the workout—lacking numbers, organization, or clout—they may take on great importance as new directions develop during the workout. The major players should not be indifferent to the effect of the workout on these diverse parties. The legitimate concerns of such parties should be addressed; they will be needed to vote for, support, and perhaps implement a reorganization plan.[121]

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116. This vagueness is somewhat surprising, given the importance of party-in-interest status. Being a party-in-interest allows a party to play a significant advisory role in the bankruptcy proceeding. *See In re* Pub. Serv. Co. of N.H. (Pub. Serv. I), 88 B.R. 546, 551 (Bankr. D.N.H. 1988) (listing some of the actions that a party-in-interest may take in a bankruptcy proceeding). For example, parties in interest may request relief from or extension of the automatic stay imposed by the Bankruptcy Court (11 U.S.C. §§ 362(c)(3)(B), 362(d)(1)); seek appointment of a trustee (*id.* §§ 303(g), 1104(a)); or file a competing plan of reorganization (*id.* § 1121(c)).

117. 11 U.S.C. § 102(3); *see also* 5 COLLIER ON BANKRUPTCY ¶ 1109.02[1] (15th ed. 1987).

118. *In re* Wells, 227 B.R. 553, 559 (Bankr. M.D. Fla. 1998).

119. Numerous cases have held that the term "party-in-interest" must be construed broadly to allow those with an interest in the proceedings to participate. *See, e.g.*, *In re Addison*, 175 B.R. at 650; *In re* Farley, Inc., 156 B.R. 203, 208 (N.D. Ill. 1993) (citing Unsecured Creditors Comm. v. Marepcon Fin. Corp. (*In re* Bumper Sales, Inc.) 907 F.2d 1430, 1433 (4th Cir. 1990)); *In re Pub. Serv.*, 88 B.R. at 550; *In re* Citizens Loan & Thrift Co., 7 B.R. 88, 90 (Bankr. N.D. Iowa 1980).

120. A "workout" typically involves negotiating agreements outside of the bankruptcy system to attempt to prevent the debtor from needing to file for bankruptcy protection. It can involve many of the same considerations as a bankruptcy proceeding, including renegotiation of indebtedness amounts and payment schedules. 9 AM. JUR. 2d, *Bankruptcy* § 35 (2006).

121. DONALD LEE ROME, BUSINESS WORKOUTS MANUAL § 1:21 (Nov. 2002).

Although a party can obtain party-in-interest status based on a financial interest in the bankruptcy proceeding,[122] neither the statute nor the majority of case law requires that the interest of a putative party-in-interest be financial.[123] Indeed, many courts recognize other interests that may qualify for party-in-interest status, including "practical stake[s],"[124] "legally protected interest[s],"[125] or interests of "those who will be impacted in any significant way."[126] However, the alleged damage to the potential party-in-interest must be tangible,[127] even if somewhat speculative.[128]

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122. *See In re* Hathaway Ranch P'ship, 116 B.R. 208, 213 (Bankr. C.D. Cal. 1990) (finding that limited partner of the debtor's general partner had sufficient potential for gain or loss based on debtor's bankruptcy to be a party-in-interest); *In re* FRG, Inc., 107 B.R. 461, 467–68 (Bankr. S.D.N.Y. 1989) (finding that a creditor's recovery in a related bankruptcy proceeding could be substantially affected by the bankruptcy at issue, and thus the creditor satisfied requirements for party-in-interest status); *see also* Doral Ctr., Inc. v. Ionosphere Clubs, Inc. (*In re* Ionosphere Clubs, Inc.), 208 B.R. 812, 815 (Bankr. S.D.N.Y. 1997) (granting party-in-interest status to pre-petition owner of right of first refusal on property); *In re* Chandler Airpark Joint Venture I, 163 B.R. 566, 568–69 (Bankr. D. Ariz. 1992) (finding that party granted deed from debtor, despite contingent nature of deed, has financial interest and is thus party-in-interest); Vieland v. First Fed. Sav. Bank, 41 B.R. 134, 139 (Bankr. N.D. Ohio 1984) (granting party-in-interest status to post-petition bidder on property to seek relief from automatic stay preventing sale of property). Where there is no direct financial interest, party-in-interest status has been denied. *See In re* Athos Steel and Aluminum, Inc., 69 B.R. 515, 519 (Bankr. E.D. Pa. 1987) (noting that bankruptcy would "have no direct effect on the objector's pecuniary interests" and the objector was therefore not a party-in-interest). Furthermore, not every financial interest is sufficient to render one a party-in-interest. *See, e.g., In re* Crescent Mfg. Co., 122 B.R. 979, 981 (Bankr. N.D. Ohio 1990) (denying party-in-interest status to post-petition bidder on property of debtor).

123. *See In re Wells*, 227 B.R. at 559 ("Unfortunately, courts have not established a general test to determine what constitutes the requisite stake . . . . '[we] know a sufficient stake when [we] see it.'" (citing Peachtree Lane Assocs., Ltd. v. Granader (*In re* Peachtree Lane Assocs.), 188 B.R. 815, 825, n.8 (N.D. Ill. 1995) and quoting Jacobellis v. Ohio, 378 U.S. 184 (1964) (Stewart, J., concurring))); Portland Memorandum in Support of Motion to Intervene, *supra* note 12, at 4–5.

124. *In re Wells*, 227 B.R. at 559.

125. *Id.* However, in *Wells*, the court went on to find that the party-in-interest had "a direct legal and pecuniary interest" in the bankruptcy proceeding. *Id.* at 560.

126. *In re* Cowan, 235 B.R. 912, 915 (Bankr. W.D. Mo. 1999) (citing *In re* Johns-Manville Corp., 36 B.R. 743, 754 (Bankr. S.D.N.Y. 1984)).

127. *In re Athos Steel*, 69 B.R. at 519–20 (1987) (finding that brother whose reputation might be injured due to association with debtor corporation could not qualify as party-in-interest).

128. In *In re First Interregional Equity Corp.*, the court determined that a trustee in the bankruptcy of a related entity constituted a party-in-interest. 218 B.R. 731, 739 (Bankr. D.N.J. 1997). Even though the extent of the financial effect on the Trustee's estate was not certain, the court found that the possibility of significant financial effect sufficed to warrant intervention. *Id.* at 738–39 & n.5. The Third Circuit has even granted party-in-interest status to future claimants not yet identified in an asbestos-manufacturing company's bankruptcy proceeding despite the uncertainty of their future claims or the impact that the bankruptcy would have on those claims. *In re* Amatex Corp., 755 F.2d 1034, 1042 (3d Cir. 1985).

The confusion over the elements required for party-in-interest status is evident even in a leading treatise on bankruptcy law, which notes that "anyone holding a direct *financial* stake in the outcome of the case should have an opportunity . . . to participate in the adjudication of any issue that may ultimately shape the disposition of his or her interest."[129] In a later section, however, the same treatise notes that section 1109's list of parties-in-interest is not exclusive, and that any individual with a "*significant legal*" interest in the case may qualify.[130] Finally, in discussing the rationale for the statute, the treatise explains that a "person *directly affected* by" the bankruptcy may present arguments.[131] It is certainly possible for a person or entity to be affected by a bankruptcy without a legal or financial interest in the case. The confusion grows when one considers that section 1109's mandatory intervention standard applies to "parties-in-interest," while FRBP 2018's permissive intervention standard applies to "interested parties." If interested parties and parties-in-interest are synonymous, FRBP 2018 is rendered superfluous because the parties would already receive mandatory intervention rights under section 1109. Yet there is no guidance as to how these practically identical terms differ. In order to determine how parishioners might fit into this bankruptcy scheme, some guidance may be obtained by looking at cases involving potential parties-in-interest or interested parties that are neither creditors nor persons with a contractual financial interest in the bankruptcy proceeding, and who reflect some of the same issues as parishioners—specifically, customers and putative property owners.

1. Customers

Customers hold a unique position with regard to a business undergoing bankruptcy proceedings in that the customers' interests in the bankrupt debtor may not be entirely clear. They are a necessary part of any business and typically the primary focus of the business. They may also be creditors of the business, for example if they have paid for a

129. 7 COLLIER ON BANKRUPTCY ¶ 1109.01[1] (Alan N. Resnick & Henry J. Sommer eds., 15th ed. rev. 2005) (emphasis added) (citing Doral Ctr., Inc. v. Ionosphere Clubs, Inc. (*In re* Ionosphere Clubs, Inc.) 208 B.R. 812, 814 (Bankr. S.D.N.Y. 1997)).

130. *Id.* ¶ 1109.02[1] (emphasis added) (collecting cases).

131. *See id.* ¶ 1109.04[2][b] (emphasis added) (citing *In re* Boomgarden, 780 F.2d 657 (7th Cir. 1985); Official Unsecured Creditors' Comm. v. Michaels (*In re* Marin Motor Oil, Inc.), 689 F.2d 445 (3d Cir. 1982)).

product that has not yet been delivered. But when a customer does not have a specific claim against the company, and is thus not a creditor of the debtor, what rights does it have in bankruptcy? The role of customers in one public utility's bankruptcy provides a close, though imperfect, analogy to the interests of parishioners in a church bankruptcy.

The New Hampshire Bankruptcy Court faced this issue in the context of permissive intervention in *In re Public Service Co. of New Hampshire* (*Public Service I*),[132] in which environmental groups[133] moved to intervene in a public utility company bankruptcy based on their members' status as customers. In addition to the customers, *Public Service I* involved a number of other parties seeking to intervene, including attorneys general as consumer representatives, a business association, and citizen groups.[134] The court first considered the effect of FRBP 2018, particularly its requirement that the party demonstrate "cause" to participate in the proceeding.[135] Quoting *Collier on Bankruptcy*, the court held that cause requires the party to possess "an economic or similar interest" in the bankruptcy proceeding.[136] For the New Hampshire attorney general, the result was simple because the Code mandated the state as a party in interest.[137] For all other parties, the court refused to find an ability to intervene generally, while recognizing that in individual matters within the bankruptcy proceeding, parties may be interested and able to intervene.[138] The Court then continued by determining that two entities—the New Hampshire Office of the Consumer Advocate (Consumer Advocate) and the Business and Industry Association (BIA)—would be granted limited party-in-interest status in matters where they could assist the court with "their respective

132. 88 B.R. 546 (Bankr. D.N.H. 1988).

133. *See In re* Pub. Serv. Co. of N.H. (Pub. Serv. II), 90 B.R. 575, 579 (Bankr. N. H. 1988) (related proceeding identifying the groups as environmental groups).

134. *In re Pub. Serv.* (*Pub. Serv. I*), 88 B.R. at 548–49. A total of three customer ratepayer groups moved to intervene: The Citizens Within the 10 Mile Radius, Inc., the Seacoast Anti-Pollution League, and the Campaign for Ratepayers' Rights.

135. *Id.* at 551–52.

136. *Id.* at 551 (quoting 8 COLLIER ON BANKRUPTCY, *supra* note 118 ¶ 2018.03[3]).

137. *Id.* at 555 (citing 11 USC 1129(a)(6)). Though not dispositive of the case, the court noted that New Hampshire also had an economic interest in the case as a creditor, *id.* at 555 n. 3, and due to its role as public utility regulator, was a party-in-interest "in every practical sense." *Id.* at 555.

138. *Id.* at 555 ("[T]he path of wisdom *is* to defer deciding these matters until they can be presented in more specific contexts").

viewpoints and special expertise."[139] These entities had routinely assisted the New Hampshire Public Utility Commission by bringing forth viewpoints of utility customers;[140] as a result, the knowledge those entities acquired could be useful to the bankruptcy court.[141] Although stopping short of granting general party-in-interest status, the Court permitted "limited intervention rights under FRBP 2018(a) in order that they may provide the court with advice and information regarding the effect on the rates of their particular constituencies of proposals otherwise before the court in these proceedings."[142] While the court allowed some parties to intervene, either generally or in a limited manner, it failed to further define the concept of a "party-in-interest" under Section 1109 or FRBP 2018.

The contrast between the court's treatment of the customer ratepayers and its treatment of the Consumer Advocate and BIA is instructive. The court, in examining the customer ratepayers' right to intervene, implied that those ratepayers did not have a strong enough interest, financial or otherwise, to be allowed to intervene themselves, at least not generally. The Consumer Advocate and the BIA, both of whom represented the interests of various ratepayers, but did not appear to have a direct financial stake themselves, were allowed limited intervention rights. By

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139. *Id.* at 557. Compare this result with that in *In re Addison Community Hospital Authority*, in which the court declined the request of a citizen's group to intervene in proceedings regarding the plan of reorganization. 175 B.R. 646, 650 (Bankr. E.D. Mich. 1994). In denying the request, the court found the citizen's group to be "merely interested" in the bankruptcy proceedings without a "direct legal interest" in the proceedings. *Id.* at 650. The court seemed particularly concerned with judicial efficiency, noting that it would not want to allow all citizens in the area to participate in the proceedings. *Id.* at 650 ("By allowing a large number of non-creditors to be heard in this action, the Court would be granting a blanket invitation to all parties in the area serviced by Addison. This would hamper, and unduly delay, the debt adjustment process.").

140. *In re Pub. Serv.* 88 B.B. at 555. Compare this result with that in *In re* Ionosphere Clubs, Inc., 101 B.R. 844 (Bankr. S.D.N.Y. 1989). In *Ionosphere*, the court denied a right to intervene for a general consumers' rights organization in an airline bankruptcy. It distinguished the *Public Service* case because in *Ionosphere* the consumer advocacy group was general, rather than organized to represent these particular consumers and, thus, lacked the expertise factor. *Id.* at 851. According to the *Ionosphere* court, "The real party in interest is the party that has the legal right which is sought to be enforced or is the party entitled to bring suit." *Id.* at 849. The court was concerned over the possibility of a group claiming to represent consumers (as opposed to the consumers themselves) interfering in a bankruptcy proceeding and that "[o]verly lenient standards may potentially overburden the reorganization process by allowing numerous parties to interject themselves into the case on every issue, thereby thwarting the goal of a speedy and efficient reorganization." *Id.* at 849, 850 (citing Roslyn Sav. Bank v. Comcoach Corp. (*In re* Comcoach Corp.), 698 F.2d 571, 574 (2d Cir. 1983) and *In re Pub. Serv.*, 88 B.R. at 554).

141. *In re Pub. Serv.*, 88 B.R. at 557.

142. *Id.*

implication, therefore, the court found that a direct financial interest is neither absolutely necessary, nor by itself sufficient, to create an automatic right to participate in a bankruptcy proceeding.

The same court had another opportunity to define party-in-interest in a later opinion in the same bankruptcy, *In re Public Service Co. of New Hampshire* (*Public Service II*).[143] As had happened earlier, a state attorney general (this time, from Massachusetts), and a variety of citizen organizations sought to intervene. The proceeding involved a proposal by the debtor to reorganize the ownership structure of the company.[144] Though the court recognized that the parties seeking to intervene may have had a variety of noneconomic motives for intervention,[145] it also noted that each had economic concerns as well.[146] In the end, the court concluded that the parties could intervene in the case without the need to determine whether a financial concern was necessary for intervention.[147] However, though the court conceded that the parties had brought forth financial considerations, the court did not indicate whether the parties seeking intervention (or even the parties represented by them) would themselves be financially affected. Rather the court merely noted that whether "this action if approved [will] lead to the possibility of a diminution in the value of the assets of this estate" is a financial question.[148] Interestingly, in *Public Service II*, the court seemed to favor a broad standard, consistent with its prior opinion, that the court may hear from any party that may be able to help in the proceeding.[149] The court did not temper that broad standard in light of any potential financial interests.

The two *Public Service* decisions provide little guidance on what to do with customers; the cases clearly establish that general intervention is not appropriate, but fail to indicate whether potential financial impact on customers is either necessary or sufficient to provide a right to intervene in a limited way in specific matters.

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143. 90 B.R. 575 (Bankr. N. H. 1988).

144. *Id.* at 576.

145. *Id.* at 579.

146. *Id.* at 580.

147. *Id.* at 580.

148. *Id.* at 580.

149. *Id.* at 579 ("The reorganization court I believe has sufficient discretion to 'hear' any entity at any hearing to the extent that the entity may be able to provide an aid to the court in understanding the matter before it.").

In many ways, parishioners are similar to customers in the bankruptcy scheme. Like customers, they are not necessarily owed anything by the debtor—the primary impact may be in the future. Just as customers may be able to do business with other companies—if there are other companies—with no financial downside, parishioners are permitted to exercise their faith regardless of contribution (or lack thereof) to the church. But there are also differences between parishioners and business customers. Unlike customers, parishioners often do not have the ability to simply choose another business ("church") to attend and, if desired, to contribute to (at least not absent a change in religious faith). In addition, unlike utility companies which are heavily regulated by the government, churches—and particularly their relationships with their "customers"—are subject to minimal state intervention. Thus, while utility customers' interests may be protected in other ways, parishioners may not be so fortunate.[150] Parishioners' concerns in their church's bankruptcy proceedings extend beyond mere finances. Though cases like *Public Service I* and *II* indicate that parishioners should not be permitted to intervene generally in all bankruptcy proceedings of their churches, there may be particular situations where the effect on parishioners justifies limited intervention. Such limited intervention would allow parishioners to present their interests in proceedings which directly affect those interests without overburdening the bankruptcy courts with additional parties and arguments when not necessary to ensure protection of those interests.

2. *Potential Property Owners*[151]

Bankruptcy proceedings deal with property rights,[152] and naturally anyone with a potential right to the property at issue will seek to protect that right in the bankruptcy proceeding. However, merely having an

150. This is an issue of adequate representation in the bankruptcy, rather than of whether the customer or parishioner is interested in the proceedings. Interestingly, unlike FRCP 24, FRBP 2018 does not include a requirement that the interested party's interests not be represented in the bankruptcy.

151. In an adversary proceeding, FRCP 24(a)(2) provides that property ownership may create a mandatory right of intervention. With a bankruptcy case, property ownership itself is not being used to create a right to intervene, but rather to establish either "party-in-interest" status that will allow for mandatory intervention under section 1109 or "interested party" status under FRBP 2018.

152. Tenn. Student Assistance Corp. v. Hood, 541 U.S. 440, 447 (2004) (finding that discharge of a debt by a bankruptcy court is an in rem proceeding).

interest in the property, or being financially impacted as a result of the property distribution, may not suffice to establish party-in-interest status.

Two cases from the New York bankruptcy courts analyze intervention by parties claiming rights in property of the bankruptcy estate. The Bankruptcy Court for the Southern District of New York refused to permit intervention in the bankruptcy proceeding of a shopping store tenant where the putative intervenor was "merely 'concerned' with the results of the proceeding."[153] The putative intervenor, a clothing store, attempted to intervene when the debtor-tenant sought to assign its lease to another clothing store in violation of the shopping-center-mix provisions of its lease.[154] The court denied the putative intervenor's motion to intervene because the shopping-center-mix provisions were intended to protect the landlord, not other tenants.[155] Thus, the putative intervenor had no legally protectable interest to claim.[156] In so holding, the court noted that creditors of creditors do not have a right to intervene in bankruptcy cases because, while the bankruptcy may affect them financially, the relationship is too tenuous to create a right to intervene.[157]

Three years later, the Bankruptcy Court for the Eastern District of New York permitted intervention by a party claiming ownership of property.[158] The debtor, a professional sports photographer, sued the National Basketball Association (NBA) for the return of photographs shot by the debtor. He then reopened his bankruptcy case to determine the effect of the photographs on the bankruptcy proceeding.[159] The NBA sought to participate in the bankruptcy proceeding.[160] The court permitted the NBA to intervene, finding that it had "an actual, direct

153. *In re* Martin Paint Stores, 199 B.R. 258, 264 (Bankr. S.D.N.Y. 1996) (citing *In re* Goldman, 82 B.R. 894, 896 (Bankr. S.D. Ohio 1988)).

154. *Id.* at 260–61.

155. *Id.* at 264.

156. *Id.* at 265.

157. *Id.* at 264. Not all courts agree, however, that one who is a creditor of a creditor cannot be a party-in-interest. *See In re* Cowan, 235 B.R. 912 (Bankr. W.D. Mo. 1999). In *Cowan*, the debtor had filed a prior bankruptcy, and the court acknowledged that the creditors of the original bankruptcy were, in essence, now creditors of the bankruptcy trustee from the original bankruptcy. *Id.* at 915. Even though the creditors could now be classified as creditors-of-creditors in the debtor's subsequent bankruptcy proceeding, the court permitted intervention to allow the creditors to allege that the debtor had filed a second bankruptcy in bad faith. *Id.* at 915, 918.

158. *In re* Koch, 229 B.R. 78, 82 (Bankr. E.D.N.Y. 1999).

159. *Id.* at 79.

160. *Id.* at 81.

interest in this bankruptcy case inasmuch as it claims to be the owner of property which the Debtor claims belongs to his bankruptcy estate."[161]

In both of these cases, the potential intervenor sought to protect a financial interest. But financial interest alone is not necessarily sufficient to create party-in-interest status in the bankruptcy proceeding as is an ownership interest in property allegedly belonging to the bankruptcy estate.

3. *Conclusions on Party-in-Interest Status*

When determining whether an unnamed party is a party-in-interest under section 1109 or an interested party under FRBP 2018, a court should consider whether the party will be financially or legally affected by the proceeding, but may also consider whether the party's participation is necessary to protect its interests and the effect of intervention on judicial efficiency.[162] Because of the vast universe of potential issues in one bankruptcy case, it is impossible to conclude that a parishioner would always qualify (or not qualify) for intervention under section 1109 and FRBP 2018.

D. *Permissive and Mandatory Intervention in Adversary Proceedings*

FRBP 7024 applies FRCP 24 to adversary proceedings which, in turn, includes both mandatory and permissive intervention provisions.[163] Intervention is mandatory when dictated by statute or when the intervenor's interest in property may be "impair[ed] or impede[d]" by the resolution of the matter.[164] Intervention is permissive when dictated by statute or when the intervenor shares a "claim or defense" in common

161. *Id.* at 82.

162. *In re* Addison Cmty. Hosp. Auth., 175 B.R. 646, 651 (Bankr. E.D. Miss. 1994) (citing *In re* City of Bridgeport, 128 B.R. 686, 687 (Bankr. D. Conn. 1991)) (also weighing an additional factor: a party's need to intervene in order to ensure that the case does not set precedent that may adversely affect that party in future cases); *In re* Ionosphere Clubs, Inc., 101 B.R. 844, 853 (Bankr. S.D.N.Y. 1989); *In re* Pub. Serv. Co. of N.H., 88 B.R. 546, 551 (Bankr. D.N.H. 1988)); *see also In re* First Interregional Equity Corp., 218 B.R. 731, 736 (Bankr. D.N.J. 1997) (citing *In re* Torrez, 132 B.R. 924, 936 (Bankr. E.D. Cal. 1991)); *In re City of Bridgeport*, 128 B.R. at 687–88; *In re Ionosphere*, 101 B.R. at 853.

163. Cindy Vreeland, *Public Interest Groups, Public Law Litigation, and Federal Rule 24(a)*, 57 U. CHI. L. REV. 279, 282 (1990).

164. FED. R. CIV. P. 24(a)(2).

with one involved in the adversary proceeding.[165] In short, even without an express statute granting intervention to a particular party, intervention is proper when the intervenor has an interest in the property at issue which stands to be harmed or an issue in common with the proceeding in which the party seeks to intervene.

An express right to intervene in an adversary proceeding may be conferred by statute.[166] However, the Code never mentions parishioners. Thus, to the extent that parishioners seek to intervene as of right in an adversary proceeding, FRCP 24 implies that they can do so only when they have an unrepresented property interest.[167] Mandatory intervention has been interpreted to require a showing of an interest that is "direct, substantial, and legally protectable."[168]

E. Necessity of a Substantial and Unrepresented Interest in the Bankruptcy Case

Regardless of whether a parishioner seeks mandatory or permissive intervention, or whether the proceeding is an adversary proceeding or a case, the parishioner must establish an "interest" in the case.[169] Under

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165. FED. R. CIV. P. 24. The common claim or defense provides an interesting contrast to the intervention provisions of FRBP 2018 and section 1109. In those other intervention provisions, a party with a common interest is not permitted to intervene if the parties currently involved in the proceeding can adequately represent that interest. FRCP 24's permissive intervention provision, however, is designed with judicial efficiency in mind. 32B AM. JUR. 2D *Federal Courts* § 2153 (2005). The intervenor may be permitted to intervene precisely because of its common interest. *Id.* But that common interest must be rooted in a "claim or defense," implying that the potential intervenor must also be involved in separate litigation. Unless the parishioners are also involved in litigation that would invoke a common claim or defense, such a provision will not be of use. In determining whether a party should be permitted to participate, the court must ensure that such participation will not create an excessive burden on the proceedings themselves, such that the intervention is not justified. FED. R. CIV. P. 24(b)(2).

166. *See* FED. R. CIV. P. 24.

167. This language arises out of FRCP 24's mandatory intervention provisions, which allow intervention when another statute so requires (this only applies in the church bankruptcy context if section 1109 is construed to require intervention for parishioners as parties-in-interest in adversary proceedings) or "when the applicant claims an interest relating to the property or transaction which is the subject of the action and the applicant is so situated that the disposition of the action may as a practical matter impair or impede the applicant's ability to protect that interest, unless the applicant's interest is adequately represented by existing parties." FED. R. CIV. P. 24(a)(2).

168. *In re* Kaiser Steel Corp., 998 F.2d 783, 790 (10th Cir. 1993) (quoting United States v. Perry County Bd. of Educ., 567 F.2d 277, 279 (5th Cir. 1978)).

169. *See* 11 U.S.C. § 1109 (2000) (requiring demonstration of party-in-interest status for intervention); FED. R. BANKR. P. 2018 (requiring demonstration of interested party status for intervention); FED. R. CIV. P. 24 (requiring showing of interest in property to allow intervention

FRBP 2018, the parishioner would also need to establish "cause" to intervene; under FRCP 24, the parishioner must demonstrate that the intervention is needed to protect his or her interests in the property at issue. And, because parishioners are not expressly listed as a party-in-interest under Section 1109, mandatory intervention is only available when they establish an interest mandating a right to participate. Thus, regardless of which rule a court uses, it appears that a parishioner's best chance for intervention lies in establishing a significant and unprotected interest in the decision to be rendered in the proceedings.

The parishioners do have an "interest" in the bankruptcy cases of their churches. Their interest in practicing their faith is significant—indeed, constitutionally protected.[170] The parishioners may also have prospective financial interests if donations are required to keep the church functioning after distributions are made to creditors. These are significant interests that should support intervention. An interest alone, however is not sufficient for intervention; that interest must also be unprotected.

The Spokane bankruptcy case provides insight on how claims for parishioner intervention might be handled.[171] In that matter, the Tort Claimants' Committee[172] sought an order that it was entitled to intervene in any adversary proceedings related to the bankruptcy case. The Bankruptcy Court did not allow mandatory intervention, noting that the Tort Claimants' Committee could protect its interests in other ways, including objecting to proposed settlements of the adversary

absent statute mandating intervention). For discussion of FRCP 24's permissive intervention provisions, see *supra* Part III.D.

170. U.S. CONST. amend. I; *see also* 42 U.S.C. § 2000bb-1(c) (2000) (granting individuals standing to sue the federal government for burdening the free exercise of religion).

171. Only the Portland bankruptcy court has expressly considered the issue of parishioner intervention. Although the Portland bankruptcy court's opinion does not provide much detail on the issue, the briefs filed by the parties consider it in more detail. Portland Memorandum in Support of Motion to Intervene, *supra* note 12; Tort Claimants Committee's Response to Motions to Intervene at 3, Tort Claimants' Comm. v. Roman Catholic Archbishop of Portland (*In re* Roman Catholic Archbishop of Portland), Adv. Proc. No. 04-03292 (Bankr. D. Or. Feb. 28, 2005) ("[T]he Parish Committee can never be anything other than a voice for Debtor's interests. Its intervention can add nothing to these proceedings.").

172. The Tort Claimants' Committee differs from the Tort Litigants' Committee. The latter committee includes those potential tort claimants who also have pending litigation in the bankruptcy proceedings. Memorandum at 3, Tort Claimants' Comm. v. Catholic Diocese of Spokane (*In re* Catholic Bishop of Spokane), B.A.P. Nos. EW-05-1273-NBS & EW-05-1276-NBS (B.A.P. 9th Cir. Sept. 6, 2006) (unpublished opinion on file with author) [hereinafter Spokane Memorandum Opinion].

proceedings.[173] The Bankruptcy Appellate Panel (BAP)[174] reversed, holding that the Tort Claimants' Committee's interests were not adequately represented and, thus, intervention would be permitted.[175] The BAP noted that the adversary proceedings could have a significant impact on what property would be part of the estate eligible for distribution to creditors, and that the Tort Claimants' Committee membership could be harmed as a result.[176]

Perhaps the most enlightening section of the BAP's opinion, and an indication of how the Ninth Circuit might react to a petition to intervene by parishioners, comes in the discussion of whether the Tort Litigants' Committee could or would adequately represent the interests of the Tort Claimants' Committee. The Spokane Diocese argued that the Tort Litigants and the Tort Claimants shared a common interest—to maximize the estate for the benefit of the creditors. But the BAP was not convinced, requiring a very strong showing of adequate representation to deny intervention:

> In this Circuit, "in determining whether an applicant's interest is adequately represented by existing parties, we consider: (1) whether the interest of a present party is such that it will *undoubtedly* make all of the intervenor's arguments; (2) whether the present party is capable and willing to make such arguments; and (3) whether the would-be intervenor would offer any necessary elements to the proceedings that other parties would neglect." . . . The proposed intervenor need only show that the representation "may be" inadequate.[177]

The court noted that the two committees both sought to maximize the estate, but disagreed on how the property of the estate should be distributed once maximized.[178] Similarly, parishioners and their bishop

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173. *Id.* at 4, 9.

174. Bankruptcy Appellate Panels, or "BAP"s, are established by 28 U.S.C. § 158 to hear bankruptcy appeals with the consent of the parties involved in the appeal. Ordinarily, appeals from the bankruptcy courts would be heard by the District Court. 28 U.S.C. § 158 (2000).

175. Spokane Memorandum Opinion, *supra* note 172, at 14.

176. Spokane Memorandum Opinion, *supra* note 172, at 9–10.

177. Spokane Memorandum Opinion, *supra* note 172, at 10–11 (emphasis added) (internal citations omitted).

178. Spokane Memorandum Opinion, *supra* note 172, at 13. The court also cited "[t]he record . . . [of] animosity, mistrust and ill will among certain members of the [Tort Claimant's Committee] and the [Tort Litigants Committee]" in determining that the Tort Litigants' Committee might not adequately represent the interests of the Tort Claimants' Committee. Presumably, this would not be an issue between parishioners and their diocese. *Id.* at 12.

share a common interest—maximization of the trust property. The parties may differ, however, when the bishop assumes additional duties as a debtor-in-possession.[179] In that case, the sole party to the case who shared the parishioners' interests may no longer be able to protect those interests.

As the courts continue to consider the various property-related issues in the church bankruptcy proceedings, they must simultaneously weigh the need for parishioners to intervene in those proceedings against the need to ensure an efficient bankruptcy process. Parishioners are interested parties when their churches file for bankruptcy protection. Yet, allowing them to intervene in the bankruptcy proceedings may increase the costs of the bankruptcy or delay the process. The courts are left to determine an equitable solution that will best protect everyone's interests.

IV. PARISHIONER INTERVENTION IN BANKRUPTCY PROCEEDINGS

Parishioners should be allowed to intervene in both bankruptcy cases and adversary proceedings when they have a substantial interest in the property that the diocese cannot adequately represent. Parishioners do not need to intervene in proceedings where the only issue is ownership of church property and the diocese has already argued that the property belongs to the parishes. Parishioners have a substantial interest in ownership of church property; the property of the church ensures parishioners a means to practice their faith.[180] Further, parishioners may have a financial interest if additional funds are required of them in order to continue their parish's existence. In the typical case, the diocese adequately represents these interests. However, parishioners must be allowed to intervene in proceedings that determine how church property is distributed where the diocese, acting as debtor-in-possession, fails to represent parishioners' interests.

179. See *infra* Part IV.B.

180. Portland Memorandum in Support of Motion to Intervene, *supra* note 12, at 2 ("Those in the parish communities . . . use these parish properties for religious worship, the baptism of their children, the education of their youth, the marriage of their young people and the burial of their loved ones . . . . These places are integral to the exercise of religious practices that benefit others.").

A. Intervention When the Diocese Seeks To Protect Its Parishioners' Interests by Arguing that Property Is Held in Trust

When the diocese shares the viewpoint of its parishioners and, thus, seeks to protect their interests, parishioners do not need to intervene in the church's bankruptcy proceedings. Specifically, where the diocese argues that it holds property in trust for its parishioners, the parishioners interests are adequately protected. The intent of the donor may be determinative of trust status. Although a variety of trust forms exist, the two most common means of establishing trusts, "express trusts" and "resulting trusts," both rely on a determination of donative intent.[181] An express trust is formed when the settlor of the trust expressly indicates an intent that the transferred property be held in trust for the benefit of another.[182] Although frequently written, an express trust may be created orally or even by the settlor's conduct.[183] With a resulting trust, the intent that the transferred property be held in trust is presumed for the settlor of the trust.[184]

The Portland bankruptcy highlights the complexity of analyzing the trust status of property belonging to the church.[185] Church funds, whether for the Archdiocese or an individual parish, come largely from donations.[186] Some funds are donated or raised with a specific purpose in

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181. *See* RESTATEMENT (THIRD) OF TRUSTS § 2 (2003) ("A trust . . . is a fiduciary relationship with respect to property, arising from a manifestation of intention to create that relationship and subjecting the person who holds title to the property to duties to deal with it for the benefit of charity or for one or more persons, at least one of whom is not the sole trustee."). For a further discussion of trust issues regarding bankrupt churches, see Daniel J. Marcinak, *Separation of Church and Estate: On Excluding Parish Assets from the Bankruptcy Estate of a Diocese Organized as a Corporation Sole*, 55 CATH. U. L. REV. 583 (2006).

182. 90 C.J.S. Trusts § 8 (2002) ("Express trusts are those which are created by the direct and positive acts of the parties, by some writing, or deed, or will, or by words either expressly or impliedly evincing an intention to create a trust." (footnotes omitted)); *see also* Portland Memorandum in Support of Motion to Intervene, *supra* note 12, at 6; Spokane Memorandum Decision, *supra* note 44, at 38 (noting that the Spokane Archdiocese's articles of incorporation expressly stated that the Archdiocese held "property in trust for . . . the Roman Catholic Church" and using that statement as an indication that, while an express trust existed, the parishes were not the beneficiaries of that trust relationship); Gerstenblith, *Civil Court*, *supra* note 23, at 552.

183. RESTATEMENT (THIRD) OF TRUSTS § 13 cmt. b; GEORGE GLEASON BOGERT, TRUSTS AND TRUSTEES § 45 (2d ed. rev. 1984).

184. RESTATEMENT (THIRD) OF TRUSTS § 7 cmt. a ("A resulting trust arises from an intention that is legally attributed to a transferor based on the nature of the transaction, rather than from manifested intent."); *see also* Spokane Memorandum Decision, *supra* note 44, at 39–42 (discussing, but rejecting, equitable notion of constructive trust).

185. *See supra* Part I.A (discussing ownership issues raised in Portland bankruptcy).

186. Portland Memorandum in Support of Motion to Intervene, *supra* note 12, at 1.

mind, such as building a new school or providing for the retirement of clergy. For example, one parish in the Portland Archdiocese raised almost two million dollars in pledges to build a church, of which seven hundred fifty thousand dollars has been received and is frozen as a result of the bankruptcy proceeding—the money cannot be used for the building fund unless the bankruptcy court deems that it will not be used to pay claims in the bankruptcy proceeding.[187] The intent of those donating funds for such a building project is clear: they wanted to build a church.[188] Where donors give funds for a specific purpose, they likely establish a trust relationship both under the law of most states[189] and in canon law.[190] Other funds, however, are not given for a specific purpose, but rather for the general use of the church.[191]

With such general funds, the issues become much more complex. First, were the funds given "in trust" and, second, if they were given "in trust," for what purpose was the trust developed? The Portland Parishioners argue that all donations and funds raised are held in trust for the individual parishes from which they came.[192] But do parishioners *really* give money to the church with the expectation that it will be used exclusively for their own parish?

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187. Wright, *supra* note 13. That parish is not alone; Wright mentions that almost $4 million was put into capital improvement funds throughout the archdiocese. *Id.*; *see also* Tucson Disclosure Statement, *supra* note 6, at 20 (indicating that each individual parish purchased its own land and built its own church with its own funds).

188. Wright, *supra* note 13 (quoting parishioner and chairman of the building fund, stating that "[a]ll we understand is that we gave money for a specific purpose, and now that money may not go to build a church").

189. RESTATEMENT (THIRD) OF TRUSTS § 2.

190. *See* 1983 CODE c.1267 ("Offerings given by the faithful for a certain purpose can be applied only for that same purpose.").

191. In the Tucson bankruptcy, the court documents indicate that donations not tied to specific purposes, such as weekly offertory collections, were held by the Parishes until the Parish had sufficient funds to cover three months' worth of general expenses; any funds greater than that amount would be held by the Diocese. Tucson Disclosure Statement, *supra* note 6, at 21. However, who holds legal title to the funds is not dispositive of equitable ownership of the funds. RESTATEMENT (THIRD) OF TRUSTS § 2. Even if the individual parishes actually hold and control the funds, they may still be considered diocesan property in a bankruptcy and, conversely, funds held by the Diocese may still be held in trust for the individual parishes. *See generally* Tucson Disclosure Statement, *supra* note 6, at 21 (arguing that Diocese holds "Unrestricted Deposits" in trust for parishes).

192. Portland Memorandum in Support of Motion to Intervene, *supra* note 12, at 1. The court in the Spokane bankruptcy also considered, but rejected, the argument that the very statute allowing for the incorporation of the church automatically created a trust relationship between the church and its parishioners. Spokane Memorandum Decision, *supra* note 44, at 35–36.

The parishioners argue that their donative intent when supplying money to their local parishes was that the parishes themselves retain the benefit of the money.[193] However, this donative intent will likely fail to meet the standard of intent required for an express, or even resulting, trust.[194] "The expression of a generally benevolent attitude or of a general donative intent is not the equivalent of a trust intent."[195] However, this rule does not mean that all parishioner donations and all church properties are subject to the claims of bankruptcy creditors.[196] Indeed, there may be two levels of intent to consider. On the level of the individual parishioner, an expression of intent regarding the donations *is* sometimes expressly stated, such as with building drives or other targeted donations.[197] Even if no such intent is evident on the parishioner level, to the extent that property is turned over to the diocese by a parish, the intent *of the parish* may be the relevant consideration. This is particularly true if the parish is considered to be a separate legal entity. Some money may be turned over with the intent that the diocese hold it for the parish's benefit, while other funds may be provided for the

193. For example, multiple affidavits were filed in the Spokane case indicating the parishioners' intention that the donated money be used for the benefit of the individual parishes. *See, e.g.*, Affidavit of Monsignor James Ribble in Response to Summary Judgment (Cathedral of Our Lady of Lourdes Parish) at 3, Comm. of Tort Litigants v. Catholic Diocese of Spokane (*In re* The Catholic Bishop of Spokane), Adv. Proc. No. 05-80038 (Bankr. E.D. Wash. May 27, 2005) ("All money collected in the regular Sunday collection is for the use, maintenance and improvement of Our Lady of Lourdes."); Declaration of Jack O'Brien in Response to Summary Judgment (St. Peter's – Spokane) at 2, *Comm. of Tort Litigants* (*In re Bishop of Spokane*), Adv. Proc. No. 05-80038 (May 27, 2005) ("Further, I have contributed to the Parish on a regular basis and it is my intent that my contributions to the Parish go to the exclusive use of the Parish."); Affidavit of Linda Kobe-Smith in Response to Summary Judgment (St. Ann's Parish, Spokane) at 2, *Comm. of Tort Litigants* (*In re Bishop of Spokane*), Adv. Proc. No. 05-80038 (May 26, 2005) ("All money donated to St. Ann's Parish through the weekly collections was for the direct use [sic] St. Ann's, for its benefit and furtherance of St. Ann's charitable works, at St. Ann's sole discretion, not for use by the Diocese.").

194. Even if such an intent is found, money cannot be in a trust unless it is "traceable." *See* 5 COLLIER ON BANKRUPTCY, *supra* note 129, ¶ 541.11. Assuming, however, that the archdiocese separates gifts given for specific purposes from gifts given for general support of the parish, and that each parish's gifts are accounted for separately, tracing should not present a problem.

195. BOGERT, *supra* note 183, § 46 (internal citations omitted).

196. *But see* Lipson, *supra* note 8, at 407 (arguing that "[i]f the Portland and Spokane cases are any indication, the application of ordinary bankruptcy and state law would likely produce results which parishioners would find troubling"). Lipson also discusses the history of trust law within the churches, concluding that state trust law may prevent property from belonging to the diocese. *Id.* at 393–99.

197. *But see* Spokane Memorandum Decision, *supra* note 44, at 43 (distinguishing the parishioners' intent that the money be used to build the building from the parishioners' intent as to who would own the building).

diocese's own use. The question of whether a trust has been formed requires difficult determinations of intent; this is true whether the question involves the possible formation of a trust when parishioners donate money to the church, or when parishes subsequently turn over that money to a diocese.[198]

As the courts make these determinations, they will need to consider both the magnitude of the parishioner's interests and the parishioner's need to be part of the proceedings in order to adequately represent their interests. As noted above, the interests of the parishioners lie in being able to use that property which is needed to fully practice their faith. The need, however, to intervene to represent those interests is not as clear.

Although there may be situations in which the diocese and its parishes and parishioners disagree over the ownership of property, the parishioners in the Portland case expressly note that they agree with the Archdiocese as to the ownership of the property in question.[199] The parishioners do not claim that property listed by the Archdiocese as titled in the Archdiocese actually belongs to the parishes. Rather, the parishioners merely repeat the claims of the Archdiocese that the Archdiocese's ownership is in trust for the parishes:

> In this proceeding, the Committee of Parishioners will allege that: (1) significant portions of the "Disputed Property" (as defined in the Complaint) are not property of the estate under 11 U.S.C. § 541 because the Archdiocese holds only legal title to, and not an equitable interest in, such property; (2) the members and constituents of the Committee of Parishioners, and their predecessors, donated significant portions of the Disputed Property with intent that the property be dedicated to the religious and charitable purposes of the parish and the parish community, and that such donations and intentions create charitable trusts enforceable under Oregon law; (3) the members and constituents of the Committee of Parishioners are beneficiaries of the charitable trusts mentioned above and possess enforceable rights under Oregon law to enforce the trust.[200]

198. For an extensive analysis of intent and trusts in the context of churches, see Gerstenblith, *Civil Court*, *supra* note 23, at 550–66.

199. Portland Memorandum in Support of Motion to Intervene, *supra* note 12, at 7 ("The Archdiocese agrees that it holds only legal title and not the beneficial interest in the Disputed Properties.").

200. Portland Memorandum in Support of Motion to Intervene, *supra* note 12, at 5.

The Portland Complaint defines "Disputed Property" as "property that Debtor does not consider to be property of the estate or that Debtor contends [is] being held by Debtor for others."[201] When confronting the issue of whether property will remain in the hands of the Church or go to the creditors, the Church and its parishioners will typically agree that, to the extent possible, property should remain with the Church.[202] Although the diocese and the parishioners present a common viewpoint in the current adversary proceeding, the real dispute between the diocese and its parishioners is not whether the property belongs to the estate, but what happens to the property once taken out of the estate. That issue does not need to be resolved yet, if ever, in the bankruptcy court.[203]

B. Intervention When the Diocese's Interests Conflict with Its Parishioners' Interests

Potential for future conflicts between the parishes and the dioceses exists. When conflict arises between these two entities, the diocese may not adequately represent the interests of its parishioners. In that case, the parishioners should be allowed to intervene to protect their interests.

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201. Portland Complaint, *supra* note 21, at 4.

202. The author recognizes that some parishioners, out of concern for the tort victims, may feel differently but, in those circumstances, the parishioners should be adequately represented by the tort claimants in the proceedings. Further, because such parishioners are seeking not to keep money for themselves or their own purposes, they are not protecting their own property interests and would thus not qualify for a significant interest under the intervention requirements.

203. The disputes over property between dioceses and their parishes will frequently involve proceedings that arise after the adversary proceeding. For example, if the debtor diocese seeks a preferential transfer recovery against one of its creditors, a contractor hired to build a new parish, it will use an adversary proceeding to do so. But what becomes of the recovered funds? Are the funds property of the diocesan estate (and, thus, the creditors)? Of the diocese itself? Of the parishioners? Although the diocese and parishioners may disagree as to these matters, the parishioners may not need to intervene in the adversary proceeding itself to protect their rights. The dispute has nothing to do with whether the funds constitute a preferential transfer and can be recovered. Rather the dispute is over who is entitled to the funds *once recovered*. The actual distribution of funds between the diocese, for the benefit of the bankruptcy estate, and the parishioners is not an adversarial proceeding, except to the extent that it affects the ability to confirm a reorganization plan or that the parishioners are already party to the proceeding (such as when the estate seeks to "recover" the assets from the individual parishes or parishioners who, at that point, are parties in the adversarial proceeding and do not need to intervene). The parishioners may need to intervene, but the intervention comes in the bankruptcy case under section 1109 and FRBP 2018, not in the adversary proceeding under FRBP 7024.

1. *Disputes When the Diocese Refuses to Argue that State Law Creates a Trust Relationship*

With regard to property disputes between the diocese and its individual parishes, the parishioners in Portland note that the issue of whether canon or state law applies may arise.[204] If the Archdiocese argues that state law is the source of its trust relationship, it may be estopped in the future from arguing that canon law should be considered. The Archdiocese may not be willing to make this argument, even if it affects the trust status of its parishioners' property, for fear that the precedent will harm it in the future. Although it is not clear that whether canon law or state law is applied will produce different results, if there is a possibility that the parishioners' interests in the property will be better protected under state law, the parishioners should be allowed to intervene to make that argument. To date, however, there has been no refusal by the Archdiocese to make such an argument.[205] Without an indication that the canon law/state law argument will become important to the case or that the argument will not be made by the Archdiocese, it is premature for the parishioners to intervene.

2. *Disputes When the Diocese Is Acting as Debtor-in-Possession*

If during the bankruptcy case, a diocese becomes classified as a debtor-in-possession, its new status may create a conflict between the

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204. Although the parishioners anticipate arguing that state law *may* constitute the basis for the trust relationship between the parishes and the diocese, the parishioners assume that the diocese will not make the same arguments out of concern for the precedential effect of such decisions. Portland Memorandum in Support of Motion to Intervene, *supra* note 12, at 10. Precedential effect is of concern, as the Spokane bankruptcy court noted. Spokane Memorandum Decision, supra note 44, at 19–24. To the extent that a diocese makes an argument regarding property ownership in one case, it may be prevented from making a different argument in a future case. Indeed, the tort claimants in Portland indicated that prior decisions in which the Spokane diocese had claimed ownership rights over parish property should prevent the Portland Archdiocese from arguing otherwise in the bankruptcy proceeding. Portland Memorandum in Support of Motion to Intervene, *supra* note 12, at 10–11. The Spokane court, however, did not find sufficient inconsistency in the two arguments to justify barring the Archdiocese from making such an argument. Spokane Memorandum Decision, *supra* note 44, at 23–24. Had the court found otherwise, the parishioners would likely need to intervene in order to make the argument regarding property ownership because there would be no other party willing and able to make such an argument.

205. Moreover, no court has yet determined that state law will lead to a different result than canon law, which also provides that the assets are held in a trust relationship. *See* Hayes, *supra* note 12, at 5; *see also Roundtable Discussion*, *supra* note 76, at 38 (comments of Mr. Phelan).

legal duties of the diocese and the interests of its parishioners.[206] A debtor-in-possession in Chapter 11 takes on most of the duties of a trustee in Chapter 11,[207] including the duties to care for the property of the estate,[208] object to claims as needed,[209] file documents and reports,[210] and put together a plan of reorganization.[211] The debtor-in-possession has fiduciary duties as a result of its position.[212] Although there is substantial disagreement among the courts as to what this fiduciary duty entails, it is clear that the duty is owed, at least in part, to creditors and that it requires some protection of the assets of the bankruptcy estate for the benefit of those creditors.[213]

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206. Though by definition a "debtor-in-possession" refers to the debtor, 11 U.S.C. § 1101(1) (2000), the two are quite distinct. *See* Theresa J. Pulley Radwan, *Limitations on Assumption and Assignment of Executory Contracts by "Applicable Law"*, 31 N.M. L. REV. 299, 304–10 (2001). One of the key distinctions between a pre-bankruptcy debtor and a debtor-in-possession in bankruptcy are the unique duties of the debtor-in-possession. A debtor, whether in possession or not, must provide information to the court and appear at hearings as required by the Bankruptcy Code. 11 U.S.C. § 521. Section 521 of the Code was substantially revised in 2005 to include additional duties, primarily involving additional documentation to be provided by the debtor. A debtor-in-possession also takes on duties under § 1107. For a discussion of how the conflicting duties of bishop and debtor-in-possession may lead to questions regarding appointment of a trustee, see Lipson, *supra* note 8, at 400–02.

207. 11 U.S.C. § 1107(a).

208. *Id.* § 704(2), made applicable to Chapter 11 by *id.* § 1106(a)(1).

209. *Id.* § 704(5), made applicable to Chapter 11 by *id.* § 1106(a)(1).

210. *Id.* § 704(7)–(9), made applicable to Chapter 11 by *id.* § 1106(a)(1); *see also id.* § 1106(a)(6).

211. *Id.* § 1106(a)(5), (7).

212. C. R. Bowles & John Egan, *The Sale of the Century or a Fraud on Creditors?: The Fiduciary Duty of Trustees and Debtors in Possession Relating to the "Sale" of a Debtor's Assets in Bankruptcy*, 28(2) U. MEM. L. REV. 781, 788 (1998) ("It is beyond all speculation that a [debtor-in-possession] managing the affairs of a bankruptcy estate is a fiduciary.").

213. *Id.* at 787–96. Bowles and Egan note that cases disagree as to whether the fiduciary duties of a debtor-in-possession are owed solely to creditors of the bankrupt company or also to other entities (focusing primarily on shareholders), *id.* at 789–91, and whether those duties simply mirror common-law duties placed on directors of corporations or whether some extra duties are imposed once bankruptcy begins, *id.* at 792–95. Regardless, it is clear that some duties are owed to creditors, and that those duties at least include the basic duties owed to shareholders at common law, namely the duties of good faith and of loyalty. *See id.* at 795 ("it clearly requires the [debtor-in-possession] to place the interest of the bankruptcy estate above its own interest"). Interestingly, while Bowles and Egan note that "the Code has sufficient protective mechanisms to ensure compliance" with these fiduciary duties, *id.* at 795, the compliance measures relied upon by Bowles and Egan include the ability to replace the debtor-in-possession with a trustee, 11 U.S.C. § 1104 (1994), or to dismiss the case altogether or convert it into another chapter, 11 U.S.C. § 1112 (1994). Bowles & Egan, *supra* note 191, at 795 n.67. The use of a trustee, either in a Chapter 11 case or in a Chapter 7 case after conversion, is fraught with constitutional issues, leaving it at least conceivable that the only

Given these fiduciary duties to creditors of the reorganizing entity, it is conceivable that the diocese serving as a debtor-in-possession will need to put the interests of creditors ahead of the interests of its parishioners.[214] This necessity would create a conflict between the diocese and its parishioners. For example, if the diocese agrees to a settlement with creditors requiring the sale of some of its church-run schools, those parishes with schools that will close may have a property interest in the schools that is counter to the settlement proposed by the diocese. Yet, such closings may be necessary to offer the payments to creditors that are required for an effective bankruptcy reorganization.[215] Likewise, if the diocese chooses to change the territorial boundaries of the individual parishes in its plan of reorganization to ensure more efficient governance, the interests of the diocese may again be at odds with the interests of the parishioners who will need to change churches, perhaps against their will. In each of these situations, the diocese may feel that the modifications are necessary for a successful reorganization, while parishioners will wish to protect their interests in the reorganizations. Parishioners would not have the legal right outside of bankruptcy to prevent a Catholic school from closing or to stop the redistricting of the church boundaries.[216] However, outside of bankruptcy, the church has more freedom to make its own decisions under the constraints of canon law, which presumes that the diocese acts in the interest of the church and those it serves.[217] Within bankruptcy,

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remedy for a church-debtor-in-possession's failure to fulfill its fiduciary duties will be to remove the case from bankruptcy altogether. *See* Lipson, *supra* note 8, at 400–02.

214. Portland Memorandum in Support of Motion to Intervene, *supra* note 12, at 10 ("It is very possible that the Archdiocese's fiduciary obligations will conflict with the interests of the Committee of Parishioners and its members."). However, Bowles and Egan note that in some cases, fiduciary duties may run to corporate shareholders. Bowles & Egan, *supra* note 212, at 791 (citing Commodity Futures Trading Comm'n v. Weintraub, 471 U.S. 343, 355 (1985)). If parishioners resemble shareholders within a corporation, perhaps the fiduciary duties of the diocesan debtor-in-possession also run to the parishioners. However, even in the language cited by Bowles and Egan, the court noted that shareholders have claims against the estate, which may provide a distinction between shareholders and parishioners. *Id.* at 792.

215. Chapter 11 of the Bankruptcy Code envisions a process of creating a plan of reorganization that will be voted on by creditors. To the extent that classes of creditors reject the plan, which presumably creditors who receive little or nothing under the plan will do, the plan must be approved by the court over the objection of the creditors. 11 U.S.C. §§ 1121–1129.

216. *See* Lipson, *supra* note 8, at 386–87 (discussing case law allowing the church to determine the continuation or discontinuation of individual parishes) (citing St. Peter's Roman Catholic Parish v. Urban Redevelopment Auth., 146 A.2d 724, 726 (Pa. 1958)).

217. 1983 CODE C.381, § 1 & 383, § 3.

those interests may succumb to the interests of creditors. In such situations, parishioners should be recognized as parties-in-interest, allowed mandatory intervention, or at least as interested parties, who should be permitted to intervene to protect their otherwise unprotected interests. This ability to intervene in limited situations when the parishioners do not have another party to represent their interest would equate to the limited intervention right presented in the *Public Service* cases. However, the likelihood that some of the diocesan debtor-in-possession's duties will conflict with the diocesan debtor's canon law duties to parishioners should not create a carte blanche right for parishioners to intervene in *every* aspect of the church's bankruptcy proceeding.

CONCLUSION

Parishioners have important interests in the bankruptcy reorganizations of their churches. Even if their interests are not financial, they have an interest in being able to adequately practice their faith. Although one can have belief without buildings, for many Catholics, the ability to fully practice their faith includes the ability to send their children to religious schools, to gather for services in a building dedicated to that purpose, or to have funds available to support church projects.[218] In most situations, the interests of the diocese are aligned with those of its parishioners, for the bishop has a duty under canon law to support the ecclesiastic functions of the church. However, as a debtor-in-possession in bankruptcy, the diocese also has a fiduciary duty to the creditors of the church. Undoubtedly, those interests will sometimes conflict. In these situations, courts should allow parishioners to intervene in the bankruptcy proceedings to ensure that their interests are protected. Absent such a conflict of interest between the diocese and the parishes, intervention would only add more parties to already complicated bankruptcy proceedings.

Perhaps the best solution for resolving the property dispute between parishes, the diocese, and claimants of those entities has already been discovered and does not involve parishioner intervention at all. In the Tucson bankruptcy, the Plan of Reorganization proposes that the Archdiocese incorporate each parish separately under state law, allowing

218. *See* Hayes, *supra* note 12, at 3.

each parish to hold title to its own property.[219] Such incorporation would not harm parishioners, who would be unlikely to notice a practical difference in their parish.[220] Although not a perfect solution,[221] such an arrangement would begin to resolve the property disputes.

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219. Tucson Debtor's Plan of Reorganization, *supra* note 73, at 48–49. *See also Roundtable Discussion*, *supra* note 76, at 40–41 (discussing corporate structures of non-Catholic churches and potential for different results); Felicia Anne Nadborny, Note, *"Leap of Faith" into Bankruptcy: An Examination of the Issues Surrounding the Valuation of a Catholic Diocese's Bankruptcy Estate*, 13 AM. BANKR. INST. L. REV. 839, 861 (2005) (considering alternative corporate structures for the church).

220. Tucson Debtor's Plan of Reorganization, *supra* note 73, at 48–49.

221. Though the issues are beyond the scope of this Article, substantive consolidation and the doctrine of piercing the veil may present significant problems to the parishes seeking to protect themselves by incorporation. *See Roundtable Discussion*, *supra* note 76, at 35, 39 (comments of Prof. Laycock); Lipson, *supra* note 8, at 390–92 (discussing possibility of "substantive consolidation") and 389 (discussing Prof. Manny's suggestions that the church organize in such a manner prior to the bankruptcy cases). The concept of substantive consolidation mirrors the idea of piercing the corporate veil in the for-profit context, whereby a company can be held liable for the debts of a separate company when the two companies are found to have a sufficiently close relationship. Professor Lipson identifies a number of considerations for substantive consolidation focusing on the relationship between the parties, the appearance to outsiders, and necessity. *Id.* at 391. These mirror the considerations for piercing the corporate veil in the business context. *See* Sea-Land Servs., Inc. v. The Pepper Source, 941 F.2d 519, 520 (7th Cir. 1991) (focusing on lack of separation between companies and apparent sanctioning of "fraud or [] injustice" (quoting Van Dorn Co. v. Future Chem. & Oil Corp., 753 F.2d 565, 569–70 (7th Cir. 1985))).

Even if the parishes are considered separate corporate entities, the question of intermingled parish and diocesan property does not end. Parent, subsidiary, and sister corporations may be held responsible for each other's debts when equity so requires. A state law corporate structure may not shield the Church from extensive liability if the corporate veil is pierced. *See, e.g.*, Melissa Coulombe Beauchesne, Note, *Corporate Law:* Doe v. Gelineau, *732 A.2d 43 (1999)*, 5 ROGER WILLIAMS U. L. REV. 683 (2000) (discussing *Doe v. Gelineau*, 732 A.2d 43 (1999), a case involving piercing in the context of a Roman Catholic Church); *see also Roundtable Discussion*, *supra* note 76, at 35 (comments of Nancy Peterman). The law and literature surrounding piercing the corporate veil is extensive, but a few factors predominate, particularly commingling of funds and failure to operate at arms-length. In Tucson's bankruptcy, for example, the parishes loaned money to the Diocese that the Diocese then used to settle outstanding tort claims. In addition, the parishes turned over excess collections to the Diocese for investment. Tucson Disclosure Statement, *supra* note 6, at 26. In each case, the Diocese was to pay back the loans/deposits, with a .75% interest rate. *Id.* at 22. However, the Diocese failed to make the required payments to the Parishes, *id.* at 26, presenting two possible problems. First, the .75% interest rate is substantially lower than traditional loan interest rates, indicating a lack of arms-length dealing between the parishes and the diocese. Second, the failure of the parish to enforce its repayment rights further indicates a lack of separation between the Diocese and its parishes. The Tort Claimants in the Spokane bankruptcy alluded to possible veil piercing if the parishes were deemed to be separate legal entities. Committee of Tort Litigants' Memorandum of Points and Authorities in Support of Motion for Partial Summary Judgment, Comm. of Tort Litigants v. The Catholic Bishop of Spokane (*In re* The Catholic Bishop of Spokane), Adv. Proc. No. 05-80038, at 20 (Bankr. E.D. Wash. Apr. 7, 2005).