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by

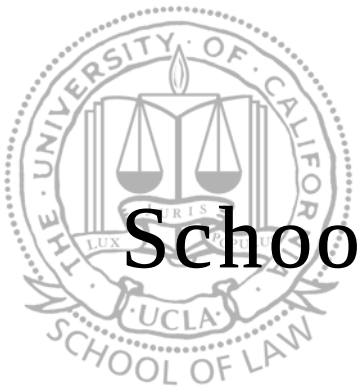
Kenneth N. Klee

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Tithing and Bankruptcy

by

Kenneth N. Klee

If the Bankruptcy Code were a Country and Western song, its refrain would be "Equity is Equality." At its core, the bankruptcy system embodies the principle that creditors with similar rights are treated equally. Debtors are not permitted to prefer their friends at the expense of other creditors. Nor may insolvent debtors tithe[1] or make gifts of their property, giving something away that could have been used to pay their creditors. The principle ranking creditors ahead of gift recipients is so deeply engrained that it dates back to English Law in 1570.[2] A debtor must be just before she is generous.[3]

To implement this policy, for 427 years the law required recipients of an insolvent debtor's donations to return the donated money or property so that it could be distributed to creditors. In 1998, however, with little fanfare and surprising speed, Congress responded to pressure from

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[1]"Tithing is the ancient practice of giving one-tenth of one's annual income to a church." *See* Steven Hopkins, *Is God a Preferred Creditor? Tithing as an Avoidable Transfer in Chapter 7 Bankruptcies*, 62 U. Chi. L. Rev. 1139, 1139 & n.1 (1995). *See also* Mary Jo Newborn Wiggins, *A Statute of Disbelief?: Clashing Ethical Imperatives in Fraudulent Transfer Law*, 48 S.C. L. Rev. 771, 772 n.6 (1997). Tithing has its origins in the Old Testament of the Bible where it has different applications that are "confused, inconsistent, and complex." *See* Oliver B. Pollack, "*Be Just Before You're Generous": Tithing and Charitable Contributions in Bankruptcy*, 29 Creighton L. Rev. 527, 531 (1996). In Pollack's article, a "tithe" is defined as a debtor's donation of one-tenth of her gross income to a religious organization. *See id.*

[2]*See* Statute of 13 Elizabeth, 13 Eliz., ch. 5 (1570).

[3]*See* Boston Trading Group, Inc. v. Burnazos, 835 F.2d 1504, 1508 (1st Cir. 1987) ("'be just before you are generous'") (quotation omitted).

religious groups to insulate churches from disgorging donations.[4] By inserting fewer than 200 words into the Bankruptcy Code, Congress let churches and charities[5] keep gifts that otherwise could be reclaimed for distribution to creditors. In making that change, Congress unwittingly disturbed multiple other sections of the Bankruptcy Code, changing the law in odd and peculiar ways. For example, surprisingly, instead of reducing returns to creditors, the data show that the congressional enactment might increase returns by providing more flexibility in the budgets of Chapter 13 debtors who tithe. Also, somewhat unexpectedly, Congress failed to insulate from attack religious or charitable pledges or the payment of pledges.

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[4]This pressure should persist in other areas since the President of the United States continues to urge a more intertwined relationship between government and faith-based organizations. *See, e.g.*, *Bush's Call to Church Groups To Get Untraditional Replies*, N.Y. TIMES, Feb. 20, 2001, at A1.

[5]Congress added charities to the protected class to make it "religion neutral" and therefore constitutional, but charities were not the ones who lobbied for the bill or who were the obviously intended beneficiaries. *See infra* note 19.

The Religious Liberty and Charitable Donation Protection Act of 1998[6] offers an early warning of the tangle that can be created when faith-based groups lobby for economically helpful legislation that must, of constitutional necessity, be neutral on its face and therefore affect many other institutions and transactions. The Act also raises the question whether Congress collectively has the will to scrutinize such legislation lest any member be accused of being unsympathetic to religious interests, raising the specter that such legislation poses far more serious problems than have been identified in the usual discussions of separation of church and state. It is too soon to tell whether Congressional behavior capitulating to religious interests in passing the Act is limited to bankruptcy legislation, where no meaningful lobby opposed the process, or will be applied in broader contexts when powerful lobbyists weigh in on the other side.

The formal legislative history of the Act is unremarkable. On June 19, 1998, President Clinton signed the Act into law. It had passed the House and Senate unanimously,[7] taking only 262 days from introduction to enactment.[8]

But Congress passed the Act without testing competing empirical assertions underlying these policy issues. As a result, creditors may contend that the Donation Protection Act is little more than unjustified congressional over-reaction to a handful of lawsuits under the Bankruptcy Code. Most debtors have neither the desire nor the income or resources to tithe major sums to churches shortly before they tumble into

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[6]Pub. L. No. 105-183, § 1, 112 Stat. 517 (1998) (hereinafter the "Donation Protection Act" or "Act").

[7]On May 13, 1998, S. 1244 originally passed the Senate 99-1, 144 CONG. REC. S 4772 (daily ed. May 13, 1998), but the dissenting Senator received unanimous consent to change his vote later that day. 144 CONG. REC. S 4814 (daily ed. May 13, 1998). S. 1244 passed the House by voice vote on June 3, 1998, after consideration of H.R. 2604, a companion bill. 144 CONG. REC. H 4005 (daily ed. June 3, 1998).

[8]Senator Grassley introduced S. 1244 on October 1, 1997 and Representative Packard introduced H.R. 2604 on October 2, 1997. *See* 143 CONG. REC. S 10294-95 (remarks of Sen. Grassley Oct. 1, 1997); H 8320 (Oct. 2, 1997); E 2037 (remarks of Rep. Packard Oct. 21, 1997).

bankruptcy. And without threatening their religious mission, most churches could disgorge small tithes or contributions in the rare instances when a trustee sued to avoid them as fraudulent transfers.[9]

[9] *See* Pollack, *supra* note 1, at 560 ("These parties can bear the expenses of litigation and appeal in pursuit of money and principle.").

On the other hand, churches and charities might contend that the Act justifiably protects both a debtor's right to tithe (or donate) and churches and charities from undergoing the serious financial hardship of disgorging money already spent. Just as Congress designed the Internal Revenue Code in part to protect charities and churches from losing donations and tithes through income taxation,[10] so did Congress design the Donation Protection Act in part to prevent bankruptcy trustees from recovering charitable donations and tithes. At first blush it might appear that the Act overturned 427 years of fraudulent conveyance doctrine[11] by insulating recipients of insolvent debtors' gifts from disgorging those gifts to the donor's creditors. In fact, the Donation Protection Act did little to change bankruptcy practice; actual practice for most of those 427 years had not involved attacks on churches and charities.[12]

To appreciate these competing views of the issues, a brief review of bankruptcy practice and lore is useful. Under the predecessor to the 1978 Bankruptcy Code, trustees and debtors in possession employed attorneys who specialized in bankruptcy law.[13] Based on their own consciences and their perceptions of judicial preferences, these attorneys and the trustees they represented were reluctant to sue charities and churches.[14]

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[10]*See* I.R.C. § 501(c)(3) (1994) (exempting religious and charitable corporations from income taxation).

[11]Modern fraudulent conveyance law traces its roots back 427 years to the English Statute of 13 Elizabeth, 13 Eliz., ch. 5 (1570). *See* Hyman L. Asamow, Note, *Fraudulent Conveyances--Steps Necessary Before Creditor Can Set Aside*, 6 N.Y.U. L. REV. 469 (1929). Fraudulent conveyance law had its origins in Roman bankruptcy law. *See* Robert J. Bein, *Robbing Peter to Pay Paul: Charitable Donations as Fraudulent Transfers*, 100 DICK. L. REV. 103, 107-08 (1995).

[12]*See infra* notes 13-16, 97-100 and accompanying text.

[13]*See* REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H. R. DOC. NO. 93-137 pt. I, 93d Cong., 1st Sess. 4 (1973) ("law firms which do receive business tend to monopolize the proceedings in a particular area").

[14]Telephone interview with Leon Forman (Aug. 10, 2000); telephone interview with Lawrence P. King (Sept. 13, 2000);

telephone interview with Harvey R. Miller (Aug. 13, 2000); telephone interview with Leonard M. Rosen (Sept. 13, 2000); telephone interview with Bernard Shapiro (Aug. 6, 2000); and telephone interview with George M. Treister (Aug. 5, 2000).

The 1978 Bankruptcy Code changed this custom by enticing large, mainstream firms to enter bankruptcy practice. Not all of these newcomer firms had the same inhibitions that their predecessor small firms and specialists had about suing charities or churches. During the 1980s some of these large firms represented debtors in possession or trustees in cases where debtors had fraudulently transferred millions of dollars to charities.[15] The attorneys analyzed the amounts at stake and raised fraudulent transfer statutes from their dormancy to recover substantial dollar amounts of charitable donations and tithes. For example, in bankruptcy proceedings involving scam artist J. David Dominelli, the law firm Gibson, Dunn & Crutcher represented the estate and recovered thousands of dollars from charities and churches that were the recipients of Dominelli's donations.[16] Smaller firms and bankruptcy specialists soon followed suit. Churches began to pressure Congress to reform the law, but their efforts achieved little success until the 1990s.

[15]Some noteworthy recoveries occurred in unreported opinions. *See infra* note 16 and accompanying text.

[16]Telephone interview with Bennett Silverman (Dec. 11, 2000).

During the 1990s, the religious right gained new clout with the 1994 election of a Republican majority in the House of Representatives. Even before 1994, churches started a campaign to enact or amend various laws to protect their interests. Early on, Congress passed a broadly drafted Religious Freedom Restoration Act; but in 1997, the Supreme Court declared it unconstitutional, at least as applied to the states, but not with respect to federal bankruptcy law.[17] Churches increased lobbying pressure on Congress to enact more narrowly focused legislation that would pass constitutional muster across the board. In addition, numerous churches demanded an amendment to the Bankruptcy Code to return to practice before the 1980s when trustees did not attack religious donations or tithes.[18] In response, the Republican leadership in Congress joined in introducing, and Congress considered, legislation to insulate churches from returning charitable donations and tithes.[19] During congressional

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[17]*See infra* note 25.

[18]*See generally The Religious Liberty and Charitable Donation Protection Act of 1997: Hearing on S. 1244 Before the Subcomm. On Administrative Oversight and the Courts of the Senate Comm. on the Judiciary*, 105th Cong. (1997) (on file with author); *The Religious Liberty and Charitable Donation Protection Act of 1997: Hearing on H.R. 2604 Before the Subcomm. on Commercial and Administrative Law of the House Comm. on the Judiciary*, 105th Cong. 1-139 (Feb. 12, 1998) (on file with author and available online at <http://commdocs.house.gov/committees/judiciary/hju51375.000/hju51375_of.htm>); *Religious Fairness in Bankruptcy Act of 1997: Hearings on H.R. 2611 Before the Subcomm. on Commercial and Administrative Law of the House Comm. on the Judiciary*, 105th Cong. 1-139 (1997) (on file with author and available online at <http://commdocs.house.gov/committees/judiciary/hju51375.000/hju51375_of.htm>).

[19]Although many Members of Congress introduced bills to remedy this problem, Senators Grassley, Sessions, and Gramm and Representatives Packard, Chenoweth, and Traficant took the lead. One of the bills introduced in the House of Representatives had sixty-seven co-sponsors, including members of the Republican leadership such as Newt Gingrich and Dick Armey. *See* H.R. 2604, 105th Cong. (1997). Although H.R. 2611 only protected religious donees, in order to avoid a possible problem under the Establishment Clause, Congress adopted

hearings only one organization, the National Bankruptcy Conference, opposed it.[20] The opposition was based on the bankruptcy principle of maximizing distributions to creditors: A trustee may recover money that an insolvent debtor donates, even if the donation is charitable or religious in nature. The Conference pointed out that the issue appeared only rarely, and that most churches could disgorge small tithes or contributions in the rare instances when a trustee sues to avoid them as fraudulent transfers without threatening their religious mission or financial security.[21] Congress, however, thought otherwise and quickly passed the Act.

The Donation Protection Act was hastily written and enacted to respond to claims of serious and widespread problems: Bankruptcy judges were granting the requests of bankruptcy trustees to prevent debtors from tithing postpetition and recover from churches the debtor's prepetition tithes. But Congress never conducted systematic research or took evidence on the magnitude of the problems. The legislative record is devoid of systematic data about the

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legislation protecting both secular and religious charities.

[20]*See generally The Religious Liberty and Charitable Donation Protection Act of 1997: Hearing on S. 1244 Before the Subcomm. On Administrative Oversight and the Courts of the Senate Comm. on the Judiciary*, 105th Cong. (1997) (statement of Donald S. Bernstein, National Bankruptcy Conference) (on file with author); *The Religious Liberty and Charitable Donation Protection Act of 1997: Hearing on H.R. 2604 Before the Subcomm. on Commercial and Administrative Law of the House Comm. on the Judiciary*, 105th Cong. 1-139 (Feb. 12, 1998) (statement of Stephen Case, National Bankruptcy Conference) (on file with author and available online at <http://commdocs.house.gov/committees/judiciary/hju51375.000/hju51375_of.htm>); *Religious Fairness in Bankruptcy Act of 1997: Hearings on H.R. 2611 Before the Subcomm. on Commercial and Administrative Law of the House Comm. on the Judiciary*, (1998) (on file with author and reported at http://www.house.gov/judiciary/5232.htm). At the time of this testimony, the author was Chair of the National Bankruptcy Conference's Committee on Legislation.

[21]*See* Pollack, *supra* note 1, at 560 ("These parties can bear the expenses of litigation and appeal in pursuit of money and principle.").

scope of the problem. It is not surprising that certain problems anticipated by Congress would fail to materialize and that unanticipated problems would arise following such hasty enactment.

The Donation Protection Act was thinly justified, and although specialists in the field were reluctant to antagonize churches and their political supporters by deriding the Act publicly, many quietly expressed their concerns. While some shared the view of the National Bankruptcy Conference that the Act was a bad idea in principle because it sharply deviated from the fundamental notion that insolvent debtors should not give away their property before satisfying their creditors, many others objected on far more practical grounds: The Act opened up a loophole that would permit debtors to divert substantial assets away from their creditors. Even the Act's most vigorous supporters could say little more than that they doubted that most people would make such gifts.

Both those who supported the Act and those who worried about its effects made essentially empirical assertions, each predicting how debtors would or would not respond to the change in law. This Article presents the results of a survey of bankruptcy trustees that measures the incidence of debtors' use of the new provisions.[22] The data show that two years into

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[22]A consumer bankruptcy case generally is one of two types. First, a consumer debtor may file for relief under Chapter 7. *See* 11 U.S.C. §§ 109(b), 701-766 (1994). In a Chapter 7 case, the debtor surrenders all property into a bankruptcy estate that is administered by a trustee. *See* 11 U.S.C. §§ 541, 701 (1994). The debtor exempts certain property out of the estate, but the rest is sold and distributed to creditors. *See* 11 U.S.C. §§ 522 (1994 & Supp. IV 1998), 726 (1994). The honest debtor gets a fresh start through the discharge of prebankruptcy debts. *See* 11 U.S.C. §§ 524(a) (1994), 523(a) (1994 & Supp. IV 1998), 727 (1994). Second, a consumer with regular income and limited debts can file for relief under Chapter 13. *See* 11 U.S.C. §§ 109(e), 1301 *et seq.* (1994). In a Chapter 13 case, a debtor retains physical possession of all property but surrenders disposable income to a Chapter 13 trustee for distribution over a three- to five-year period under a repayment plan. *See* 11 U.S.C. §§ 1306(b), 1322(d), 1325 (1994 & Supp. IV 1998), 1326 (1994). The debtor is discharged from most kinds of debts if all payments are completed under the plan. *See* 11 U.S.C. § 1328(a) (1994).

the Act's life, a substantial number of debtors are making donations protected by the Act but few debtors are "abusing" it in the sense of making last-minute donations that reduce their estates substantially. A few debtors, however, have diverted meaningful dollars to charities and churches instead of leaving them in their bankruptcy estates for distribution to creditors. In addition, the data contain important lessons about regional variations in application of theoretically uniform federal law, using the treatment of tithing in bankruptcy cases as an example. Finally, the data suggest that the Act might have unintended consequences that demonstrate the complex and interdependent nature of the consumer bankruptcy system. Although these findings do not resolve the question of principle at issue, they do help frame it and provide the context essential for further discussion.

Part I of this Article describes the substance of the Donation Protection Act and explores doctrinal issues that can be expected to arise. Part II examines recently collected data, assessing two years of experience since enactment of the Donation Protection Act. In particular, it analyzes the results of questionnaires, circulated to every Chapter 7 and Chapter 13 trustee, that sought to elicit the trustees' experiences with charitable and religious contributions in bankruptcy cases during the last two years. After recapitulating the trustees' answers to the questionnaires, Part II explores the data for further lessons and consequences of the Act. Part III examines additional effects of the Donation Protection Act, some of which Congress did not anticipate. Consequences include abuse of the bankruptcy system, more prepetition contributions, postpetition tithing, objections to discharge, denials of discharge, suits for malpractice, lawyer disciplinary actions, and refusal by courts and trustees to enforce the law as enacted. Following the conclusion, an Appendix contains the questionnaires sent by the author to Chapter 7 and 13 trustees.

I. DESCRIPTION OF THE DONATION PROTECTION ACT

The Donation Protection Act contains five essential parts. First, it limits §§ 548 and 544(b) of the Bankruptcy Code to preclude the trustee's ability to make a constructive fraudulent transfer attack on most charitable and religious contributions made by individuals or natural persons.[23]

[23]The Donation Protection Act defines "charitable contribution" to limit its scope to contributions made by debtors who are

Second, it preempts creditors' abilities to use state law to attack these contributions. Third, it limits the relevance of most contributions to the court's determination whether it should dismiss the bankruptcy case as an abuse of Chapter 7 or deny confirmation of a Chapter 13 plan based on insufficient distribution of the debtor's disposable income.[24] Fourth, it applies retroactively. Fifth, it provides that the Donation Protection Act is not a limitation on the Religious Freedom Restoration Act,[25] so churches may assert RFRA to attempt to insulate transfers that are not protected by the Donation Protection Act.

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natural persons. *See* 11 U.S.C. § 548(b)(3)(A) (Supp. IV 1998), *amended by* Donation Protection Act, § 2, 112 Stat. 517 (1998).

[24]Section 1325(b)(2) of the Bankruptcy Code defines "disposable income" as follows:
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> (2) For purposes of this subsection, "disposable income" means income which is received by the debtor and which is not reasonably necessary to be expended—
>
> > (A) for the maintenance or support of the debtor or a dependent of the debtor, including charitable contributions (that meet the definition of "charitable contribution" under section 548(d)(3)) to a qualified religious or charitable entity or organization (as that term is defined in section 548(d)(4)) in an amount not to exceed 15 percent of the gross income of the debtor for the year in which the contributions are made; and
> >
> > (B) if the debtor is engaged in business, for the payment of expenditures necessary for the continuation, preservation, and operation of such business.=ft

See 11 U.S.C. § 1325(b)(2) (1994 & Supp. IV 1998).

[25]Religious Freedom Restoration Act ("RFRA"), 42 U.S.C. §§ 2000bb to 2000bb-4 (1994). The Supreme Court declared that RFRA is unconstitutional, at least as applied to state laws. *See* City of Boerne v. Flores, 521 U.S. 507 (1997) (holding that RFRA exceeds the scope of Congress' enforcement power under section 5 of the Fourteenth Amendment as applied to a state zoning law).

As a general proposition, the Donation Protection Act purports to preclude the trustee from avoiding a natural person's charitable contributions or religious donations as a constructive fraudulent transfer. The preclusion also covers attacks by a debtor in possession or other estate representative.[26] Furthermore, the preclusion applies whether the attack is made as a matter of federal law under § 548 of the Bankruptcy Code[27] or state law, as incorporated by

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[26]In a Chapter 11 case, when a trustee is not serving, the debtor represents the estate as a debtor in possession with the same power to avoid fraudulent transfers that a trustee would have. *See* 11 U.S.C. §§ 1101(1), 1107(a) (1994). Under a confirmed Chapter 11 plan, a representative of the estate may be appointed to retain or enforce claims. *See id.* § 1123(b)(3)(B) (1994). Most courts hold the avoiding power causes of action, including actions to avoid fraudulent transfers, to be claims that may be pursued postconfirmation by a creditors' committee or other duly appointed representative of the estate. *See, e.g.,* Nordberg v. Sanchez (*In re* Chase & Sanborn Corp.), 813 F.2d 1177, 1180 n.1 (11th Cir. 1987); Creditor's Comm. v. Parks Jaggers Aerospace Co. (*In re* Parks Jaggers Aerospace Co.), 129 B.R. 265 (M.D. Fla. 1991). *But see* Foster Dev. Corp. v. Morning Treat Coffee Co. (*In re* Morning Treat Coffee Co.), 77 B.R. 62, 66-68 (Bankr. M.D. La. 1987) (holding trustee's avoidance rights are not property of the estate, and, therefore, cannot be transferred under a plan of reorganization).

[27]Section 3(a) of the Donation Protection Act amends § 548 of the Bankruptcy Code to move constructive fraudulent transfer provisions in former § 548(a)(2) to renumbered § 548(a)(1)(B). *See* Donation Protection Act, § 3(a)(3)-(6). Section 3(a)(7) of the Donation Protection Act adds new § 548(a)(2) of the Bankruptcy Code as follows:

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> A transfer of a charitable contribution to a qualified religious or charitable entity or organization shall not be considered to be a transfer covered under paragraph (1)(B) in any case in which—
>
> > the amount of that contribution does not exceed 15 percent of the gross annual income of the debtor for the year in which the transfer of the contribution is made; or

reference under § 544(b)[28] of the Bankruptcy Code.

> the contribution made by the debtor exceeded the percentage amount of gross annual income specified in subparagraph (A), if the transfer was consistent with the practices of the debtor in making charitable contributions.=ft

[28]Section 3(b) of the Donation Protection Act amends § 544(b) of the Bankruptcy Code to incorporate the same limitations on the trustee's avoiding powers in asserting the rights of actual unsecured creditors that the Donation Protection Act imposes on the trustee's federal avoiding powers under § 548 of the Bankruptcy Code. Section 3(b) of the Donation Protection Act provides as follows:

> TRUSTEE AS LIEN CREDITOR AND AS SUCCESSOR TO CERTAIN CREDITORS AND PURCHASERS.—Section 544(b) of title 11, United States Code, is amended—
>
> by striking "(b) The trustee" and inserting "(b)(1) Except as provided in paragraph (2), the trustee"; and by adding at the end the following:
>
> (2) Paragraph (1) shall not apply to a transfer of a charitable contribution (as that term is defined in section 548(d)(3)) that is not covered under section 548(a)(1)(B), by reason of section 548(a)(2). Any claim recovered by any person to recover a transferred contribution described in the preceding sentence under Federal or State law in a Federal or State court shall be preempted by the commencement of the case.

To fully appreciate the scope of the Act's preemptive effect, a brief review of state fraudulent transfer law is in order. As a matter of general fraudulent transfer law,[29] a creditor may avoid a constructive fraudulent transfer without proving the debtor's state of mind[30] or the state of mind of the transferee.[31] As long as the transfer is made, or the obligation is incurred, for less than a reasonably equivalent value or fair consideration, a creditor can attack the transfer successfully if, at the time the transfer was made,

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[29]Today, states have three basic kinds of fraudulent transfer laws. Some states rely on common law. "The English statute was enacted in some form in many states, but whether or not so enacted, the voidability of fraudulent transfer was part of the law of every American jurisdiction." Uniform Fraudulent Transfer Act Prefatory Note (1993) (copy on file with author). Other states have adopted the Uniform Fraudulent Conveyance Act ("UFCA"), and it is currently the law in four states and the Virgin Islands. *See* MD. CODE ANN., COM. LAW §§ 15-201 to 15-214 (2001); N.Y. DEBT. & CRED. LAW Art. 10 §§ 270 to 281 (McKinney 2001); TENN. CODE ANN. §§ 66-3-301 to 66-3-315 (2001); WYO. STAT. ANN. §§ 34-14-101 to 34-14-113 (Michie 2001); V.I. CODE ANN. §§ 201 to 212. Other states have adopted the Uniform Fraudulent Transfer Act ("UFTA"), and it is currently the law in Alabama, Arizona, Arkansas, California, Colorado, Connecticut, Delaware, the District of Columbia, Florida, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Maine, Massachusetts, Michigan, Minnesota, Missouri, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New Mexico, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Dakota, Texas, Utah, Vermont, Washington, West Virginia, and Wisconsin.

[30]*See, e.g.*, Muhl v. Tiber Holding Corp., 18 F. Supp. 2d 514, 518 (E.D. Pa. 1998) (noting that under New York law, "it is not necessary to prove intent to establish a claim of constructive fraud"); Metropolitan Steel Fabricators, Inc. v. Michalski (*In re* Metro. Steel Fabricators, Inc.), 191 B.R. 150, 153 (Bankr. D. Minn. 1996); Asleson v. West Branch Land Co., 311 N.W.2d 533, 544 (N.D. 1981); Doughty v. Birkholtz, 964 P.2d 1108, 1112 (Or. Ct. App. 1998).

[31]*See, e.g.*, Fisher v. Sellis (*In re* Lake States Commodities, Inc.), 253 B.R. 866, 879 (Bankr. N.D. Ill. 2000) ("the state of mind of the transferee is not an element of either of the two causes of action" [to avoid an actual intent or constructive fraudulent transfer]).

the debtor was insolvent or rendered insolvent, left with an unreasonably small capital, or intended to incur debts beyond its ability to repay.[32] The theory is that when the debtor is in financial difficulty, the debtor's assets essentially belong to the creditors.[33] Stated differently, the insolvent

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[32]*See* 11 U.S.C. § 548(a) (1994 & Supp. IV 1998); UFCA § 4 (rendered insolvent); UFCA § 5 (unreasonably small capital); UFCA § 6 (intended to incur debts); UFTA § 4(a)(2)(i)-(ii) (unreasonably small assets and intention to incur debts beyond ability to repay); UFTA § 5(a) (rendered insolvent). Intention to incur debts beyond one's ability to repay is different than actually intending to make a fraudulent transfer. The former is a constructive fraudulent transfer that focuses on the transferor's actions after the transfer is made whereas the latter focuses on the transferor's intent in making the transfer itself.

[33]*See* Marsh v. Kaye, 61 N.E. 177, 177 (N.Y. 1901) ("it may be said that every man's property is a trust fund for the payment of his debts") (*dictum*); Candee v. Lord, 2 N.Y. 269, 274 (N.Y. 1848) (the debtor is a "quasi trustee for his creditors" and his assets are "the fund upon which they must depend for payment"). *But see* GARRARD GLENN, THE LAW OF FRAUDULENT CONVEYANCES §§ 10, 227 (1931) ("in no sense of the word can it be said that a debtor holds his general estate in trust for his creditors"). Whether an insolvent debtor holds property in trust for his creditors is an essential component to resolve the tension between the insolvent debtor's freedom to tithe and his creditors' rights to payment. At least in the corporate context, when the debtor is in the vicinity of insolvency the directors owe primary fiduciary duties to creditors rather than shareholders. *See* Miramar Res., Inc. v. Schultz (*In re* Schultz), 208 B.R. 723, 729-30 (Bankr. M.D. Fla. 1997); Brandt v. Hicks, Muse & Co. (*In re* Healthco Int'l, Inc.), 208 B.R. 288, 300 (Bankr. D. Mass. 1997); Credit Lyonnais Bank Nederland, N.V. v. Pathe Communications Corp., No. 12150, 1991 WL 277613, at *34 (Del. Ch. Dec. 30, 1991). *See generally*, Christopher L. Barnett, *Healthco and the 'Insolvency Exception": An Unnecessary Expansion of the Doctrine?*, 16 BANKR. DEV. J. 441 (2000). Such a corporation holds its assets in trust for creditors. *See, e.g.*, Wood v. Dummer, 30 F. Cas. 435, 436-37 (D. Me. 1824) (No. 17,944). It remains to be seen whether courts will extend this trust fund doctrine to partnership and individual debtors. Only individuals may be debtors in Chapter 13 cases. *See* 11 U.S.C. § 109(e) (1994).

or financially-distressed debtor loses the autonomy to make gifts of her assets and should not be at liberty to give away assets for less than a reasonable economic equivalence.[34] As a corollary of this, the donee is not entitled to retain the donation at the expense of the donor's creditors, regardless of the donee's knowledge.[35]

[34]*See* Boston Trading Group, Inc. v. Burnazos, 835 F.2d 1504, 1508 (1st Cir. 1987) ("'be just before you are generous'"). The original proposition was stated by Blackstone in his commentaries on distributing a decedent's estate. *See* 1 WILLIAM BLACKSTONE, COMMENTARIES *511-512, which states as follows:

> [I]t is [the executor's] business first of all to see whether there is a sufficient fund left to pay the debts of the testator: the rule of equity being, that a man must be just, before he is permitted to be generous.=ft

[35]Just as a donee may not retain stolen property against the claim of the true owner, so should the donee disgorge an insolvent donor's tithe to the donor's creditors as the beneficial owners of the property.

But debtors do give away assets. Some make regular gifts to spouses and children.[36] Some make regular charitable or religious donations, contributions or tithes.[37] And some make irregular gifts.[38] The Donation Protection Act insulates most charitable and religious gifts, whether or not part of a regular history of giving or tithing, from attack as constructive fraudulent transfers.

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[36]*See, e.g.,* Jacobson v. Church of Manalapan, Inc. (*In re* Jackson), 249 B.R. 373 (Bankr. D.N.J. 2000); *In re* Buxton, 228 B.R. 606 (Bankr. W.D. La. 1999).

[37]*See, e.g.*, Christians v. Crystal Evangelical Free Church (*In re* Young), 82 F.3d 1407 (8th Cir. 1996), *vacated by* 521 U.S. 1114 (1997), *remanded to* 141 F.3d 854 (8th Cir. 1998) (reinstating 82 F.3d 1407); Weinman v. World of Life Christian Ctr. (*In re* Bloch), 207 B.R. 944 (D. Colo. 1997); Morris v. Midway S. Baptist Church (*In re* Newman), 203 B.R. 468 (D. Kan. 1996); *In re* Bien, 95 B.R. 281 (Bankr. D. Conn. 1989).

[38]*See, e.g.*, Murray v. La. State Univ. Found. (*In re* Zohdi), 234 B.R. 371 (Bankr. M.D. La. 1999); Rimmel v. Goldman (*In re* Goldman), 111 B.R. 230 (Bankr. E.D. Mo. 1990).

The Donation Protection Act goes much farther than simply limiting the acts of trustees in seeking to avoid charitable and religious contributions and donations by preempting the field.[39] Creditors of individual debtors also are precluded from commencing or continuing litigation against charitable or religious institutions even though they could have done so under state law in the absence of bankruptcy.[40] True, bankruptcy law preempts state law in other contexts by precluding creditors from pursuing avoiding power causes of action.[41] But the purpose for this preemption is to permit the trustee to pursue those causes of action for the benefit of the entire creditor body.[42] That rationale is specifically repudiated by the Donation Protection Act, which extinguishes all specified creditors' causes of action and precludes their revival against the debtor even after the bankruptcy case concludes.[43] Thus, bankruptcy policy is turned on its head.

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[39]The Donation Protection Act, 112 Stat. 517, amended Bankruptcy Code § 544(b)(2) to read as follows:

> Any claim by any person to recover a charitable contribution described in the preceeding sentence under Federal or State law in a Federal or State court shall be preempted by the commencement of the case.=ft

[40]*See* Miller v. Grace Fellowship, Inc. (*In re* Witt), 231 B.R. 92, 98 (Bankr. N.D. Okla. 1999).

[41]*See, e.g.*, Glenny v. Langdon, 98 U.S. 20, 29-30 (1878) (action for fraudulent conveyance may only be brought by creditors in trustee's name with leave of court if trustee refuses to act); Koch Ref. v. Farmers Union Cent. Exch., Inc., 831 F.2d 1339, 1342-43 (7th Cir. 1987) ("The trustee's single effort eliminates the many wasteful and competitive suits of individual creditors.").

[42]*See, e.g.*, Buncher Co. v. Official Comm. of Unsecured Creditors, 229 F.3d 245, 250 (3d Cir. 2000) ("[A]ny recovery is for the benefit of all unsecured creditors, including those who individually had no right to avoid the transfer.").

[43]*See* 11 U.S.C. § 548(a)(1)(B) & (2) (Supp. IV 1998). Ordinarily, if the trustee or debtor does not pursue or settle a fraudulent transfer cause of action during the bankruptcy case, creditors are free to pursue it after bankruptcy. *See, e.g.*, Knapp v. Seligson (*In re* Ira Haupt & Co.), 398 F.2d 607, 612-13 (2d Cir. 1986) (Bankruptcy Act case).

Instead of maximizing returns to creditors, the Donation Protection Act uses preemption to diminish returns to creditors.

There are limits, however, on this protection. The Donation Protection Act does not preclude the trustee from attacking a fraudulent transfer made with actual intent to hinder, delay, or defraud creditors (referred to as an "actual intent fraudulent transfer").[44] Moreover, it allows the trustee to attack certain constructive fraudulent transfers in excess of fifteen percent of the individual debtor's gross annual income.[45] Without requiring proof of the debtor's fraudulent intent, the Donation Protection Act permits the trustee to avoid transfers exceeding fifteen percent of the individual debtor's gross annual income unless "the transfer was consistent with the practices of the debtor in making charitable contributions."[46] The Donation Protection Act fails to define "practices," leaving courts to figure out whether the identity of the donee, frequency of contribution, amount of contribution, or other factors are relevant.[47] One case involved a debtor who donated $20,000 after his income increased shortly before bankruptcy: Rejecting the donation as inconsistent with the debtor's "past practices," that court compared the challenged transfer as a percentage of the

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[44]The Donation Protection Act does not limit the trustee's attack under § 548(a)(1)(A) of the Bankruptcy Code to avoid transfers made with the actual intent to hinder, delay, or defraud creditors. *See* 11 U.S.C. § 548(a)(1)(A) (Supp. IV 1998).

[45]The trustee may avoid constructive fraudulent transfers in excess of fifteen percent of the individual debtor's gross income unless the debtor shows that the transfer was consistent with the practices of the debtor in making charitable contributions. 11 U.S.C. § 548(a)(2)(B) (Supp. IV 1998).

[46]*See* § 3(a)(7) of the Donation Protection Act, 112 Stat. 527, amending § 548(a) of the Bankruptcy Code to incorporate this standard.

[47]*See* Jacobson v. Church of Manalapan, Inc. (*In re* Jackson), 249 B.R. 373, 377 (Bankr. D.N.J. 2000) (even though debtor made donations to church each year, $20,000 donation from windfall bequest made five months before bankruptcy was not consistent with debtor’s past practices).

debtor's income with prior transfers as a percentage of income.[48]

[48] *See id.*

The Donation Protection Act provides a safe harbor, protecting from attack as a constructive fraudulent transfer each transfer not exceeding fifteen percent of the individual debtor's gross annual income.[49] On its face, the Donation Protection Act has no provision to aggregate transfers before application of the fifteen percent of gross income test.[50] Thus, a court might allow a debtor to tithe all of her disposable income to various charities as long as no particular charity receives more than fifteen percent.[51] Courts, however, could interpret the Act to require the aggregation of all charitable contributions.[52] Unless the

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[49]*See* 11 U.S.C. § 548(a)(2) (Supp. IV 1998).

[50]Since § 548 of the Bankruptcy Code examines transfers made in the year before the commencement of the bankruptcy case, presumably a court would aggregate charitable donations and tithes made during the one year period. *See* 11 U.S.C. § 548(a)(1) (Supp. IV 1998). The aggregation issue is complicated because the trustee also might be able to use § 544(b) of the Bankruptcy Code to assert the rights of an actual unsecured creditor to avoid the transfer under nonbankruptcy law. *See* 11 U.S.C. § 544(b) (Supp. IV 1998). Under nonbankruptcy law the reach-back period over which a creditor may attack transfers often exceeds one year. *See, e.g.,* UFTA § 9 (four years). Therefore, a court might aggregate the debtor’s transfers over a period that exceeds one year.

[51]*See* Murray v. La. State Univ. Found. (*In re* Zohdi), 234 B.R. 371, 386 (Bankr. M.D. La. 1991) ("the ultimate effect of this ruling is arguably to insulate all transfers from avoidance under § 548(a)(2) that are (on a transfer-by-transfer basis) below the fifteen percent amount, regardless of the aggregate amount of charitable contributions during the year before bankruptcy"). *But see infra* notes 52 & 53 and accompanying text. Of course the debtor may be able to tithe more than fifteen percent to a particular charity if she shows that the transfer was consistent with the practices of the debtor in making charitable contributions. 11 U.S.C. § 548(a)(2)(B) (Supp. IV 1998). The trustee, however, may be able to attack tithes even if they are less than fifteen percent if made with the actual intent to hinder, delay, or defraud creditors. 11 U.S.C. § 548(a)(1)(A) (Supp. IV 1998).

[52]Lebovits v. Chase Manhattan Bank (*In re* Lebovits), 223 B.R. 265, 273 (Bankr. E.D.N.Y. 1998) ("The amendment provides,

courts presume aggregation of all charitable contributions, however, in theory, before filing a bankruptcy petition, a debtor could transfer just less than fifteen percent of her annual income to each of seven charities and clean out her estate entirely. The charities would be protected from constructive fraudulent transfer attack.[53]

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among other things, that an individual consumer debtor may donate up to fifteen(15%) percent of his income to his church or synagogue.") In the Chapter 13 context, § 1325(b)(2)(A) specifically limits charitable contributions made in the bankruptcy plan to fifteen percent of the debtor's gross income. *See In re* Cavanagh, 242 B.R. 707, 710-11 (Bankr. D. Mont.) ("The court in *Buxton* reasoned that Congress must have intended some limitation on a debtor's right to make charitable contributions, and that the court must still determine whether those expenses are reasonable. In this Court's view such reasoning ignores the plain language of § 1325(b)(2)(A), which sets forth Congress' specific intention to establish a limit for charitable contributions at 15 percent of the Debtor's gross income.") (internal citation omitted), *aff'd*, 250 B.R. 107 (B.A.P. 9th Cir. 2000).

[53]Because the charitable donation safe harbor in § 548(a)(2) only insulates transfers from attack as constructive fraudulent transfers, transfers made on the eve of bankruptcy probably could be avoided if the trustee in bankruptcy proves that they are made with actual intent to hinder, delay, or defraud the debtor's creditors. *See* 11 U.S.C. § 548(a) (Supp. IV 1998).

The Donation Protection Act applies retroactively to pending cases.[54] But a bankruptcy case is the whole bankruptcy adjudication, whereas a proceeding in the case is one particular lawsuit. The Bankruptcy Code and Judicial Code differentiate cases from proceedings. For example, the Judicial Code gives federal district courts exclusive jurisdiction over bankruptcy cases.[55] On the other hand, district courts have nonexclusive jurisdiction over proceedings that arise under the Bankruptcy Code or arise in or are related to bankruptcy cases.[56] The trustee avoids a fraudulent transfer by commencing an adversary proceeding in the bankruptcy case.[57] Presumably, courts and trustees will interpret the Donation Protection Act to apply to proceedings filed after June 19, 1998 in cases pending on that date. Retroactive application to proceedings pending on June 19, 1998 is likely, although less clear. To give the effective date provision of the Donation Protection Act substantive content, however, courts probably will interpret the Act to apply retroactively to proceedings as well as cases pending on or after the date of enactment.[58]

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[54]Section 5 of the Donation Protection Act, 112 Stat. 527, provides that the Donation Protection Act applies to any case that is pending or commenced on or after the date of enactment of the Donation Protection Act. Discussion of retroactivity problems is beyond the scope of this article. *See generally* Louis Kaplow, *An Economic Analysis of Legal Transitions*, 99 HARV. L. REV. 509 (1986) (providing normative economic analysis of transition issues in retroactive legislation).

[55]*See* 28 U.S.C. § 1334(a) (1994).

[56]*See* 28 U.S.C. § 1334(b) (1994).

[57]*See* FED. R. BANKR. P. 7001(1) (requiring suits to recover money or property to be commenced as adversary proceedings.)

[58]Two courts have so held without discussing the difference between cases and proceedings. *See* Miller v. Grace Fellowship, Inc. (*In re* Witt), 231 B.R. 92, 98 (Bankr. N.D. Okla. 1999); Cedar Bayou Baptist Church v. Gregory-Edwards, Inc., 987 S.W.2d 156, 159 (Tex. App. 1999). The Court of Appeals for the Eleventh Circuit recently distinguished cases from proceedings in interpreting the 1994 amendments to the Bankruptcy Code. *See* Christo v. Padgett (*In re* Christo), 223 F.3d 1324, 1332 (11th Cir. 2000) (citing Young v. Sultan Ltd. (*In re* Lucasa Int'l Ltd.), 6 B.R. 717, 719 n.5 (Bankr.

S.D.N.Y. 1980) ("In the context of the jurisdictional grants given by the 1978 statute, the word 'case' refers to the commencement of a bankruptcy by the filing of a petition")), *cert. denied*, 121 S. Ct. 1190 (2001).

Finally, it is unclear how the Donation Protection Act relates to other provisions of the Bankruptcy Code. A court might assume that the spirit of the Act should affect interpretation of other sections of the Code. For example, it might exclude the consideration of tithes in determining whether the nondischargeability of a student loan will work a hardship on the debtor.[59] Alternatively, it might assume that Congress legislated narrowly to address specific problems and that the Donation Protection Act has no application beyond its specific focus.[60]

II. EMPIRICAL DATA

Whatever uncertainties in interpretation of the Donation Protection Act remain, it has nonetheless become the law, expanding the rights of debtors to direct assets away from their creditors both pre- and postfiling. What remains unknown is whether debtors in fact have engaged in such behavior.[61] To answer this question, the author designed and circulated two questionnaires to gather data on its impact.

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[59] *See* Ritchie v. Northwest Educ. Loan Ass'n (*In re* Ritchie), 254 B.R. 913, 919-21 (Bankr. D. Idaho 2000) (debtor's religious tithing had to be excluded in determining whether debtor would be exposed to undue hardship if not discharged of student loan); Lebovits v. Chase Manhattan Bank (*In re* Lebovits), 223 B.R. 265, 272 (Bankr. E.D.N.Y. 1998) (concluding that the Donation Protection Act precludes creditors from questioning the debtor's tithes in student loan nondischargeability proceedings). *Cf.* Educ. Credit Mgmt. Corp. v. McLeroy (*In re* McLeroy), 250 B.R. 872, 875-76 (N.D. Tex. 2000) (citing, but reversing, bankruptcy court's holding excluding consideration of tithes from evaluation of debtor's income in determining hardship discharge of educational loans).

[60] *See In re McLeroy*, 250 B.R. at 880 ("The plain language of the Bankruptcy Code's relevant section as amended by the [Donation Protection Act] only addresses the avoidance powers of the bankruptcy trustee. The Act makes no mention of conferring any additional rights upon any other party and is devoid of any reference to § 523(a)(8).").

[61] For a comprehensive review of tithing and charitable donation cases before the Donation Protection Act, *see* Pollack, *supra* note 1, at 541-75.

A. METHODOLOGY

Every debtor who files for bankruptcy either under Chapter 7 or Chapter 13 is assigned to a trustee. The trustees are themselves specialists, with some serving the investigation and liquidation functions essential to Chapter 7 and others involved in the longer term job of working out budgets and supervising payments over time.[62] The author designed a separate questionnaire for Chapter 7 and Chapter 13 trustees, then mailed an appropriate questionnaire to each of the 1,274 Chapter 7 trustees and the 198 Chapter 13 trustees identified by the Administrative Office of the United States Courts.[63] The trustees responded by email, facsimile, and regular mail. On receipt, the author or his research assistants coded the data in the questionnaires into Excel databases, one for Chapter 13 trustees and the other for Chapter 7 trustees.[64]

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[62]The author sent the questionnaire and cover letter electronically or by mail to 198 Chapter 13 trustees. The Administrative Office of the United States Courts supplied the author with the identities and addresses of the trustees. The author supplemented this list from a web page of the United States Department of Justice *at* http://www.usdoj.gov/ust/library/chapter13/ch13lib.htm (last visited June 21, 2000).

[63]The author sent the Chapter 7 questionnaire and cover letter electronically or by mail to 1274 Chapter 7 panel trustees. The identities and addresses of the trustees were supplied by the Administrative Office of the United States Courts and extracted from a web page of the United States Department of Justice *at* http://www.usdoj.gov/ust/library/chapter07/7.htm (last visited June 21, 2000). Approximately ten of the Chapter 7 questionnaires were returned as undeliverable, and the author was unable to locate forwarding addresses.

[64]Upon receipt of a completed questionnaire, the author created hard copies, if necessary, and assigned each questionnaire a number in chronological order. The author or his research assistants wrote follow-up letters or made follow-up emails, faxes, or telephone calls to trustees who failed to respond or who responded with incomplete data. Copies of blank questionnaires are reproduced in the Appendix. Readers may view the data base *at* http://www.law.ucla.edu/erg/pubs.html (last visited June 8, 2001).

The Chapter 13 questionnaire was accompanied by a cover letter[65] explaining briefly how the Donation Protection Act changed fraudulent conveyance law and requesting information about religious tithes and charitable contributions in Chapter 13 cases since June 19, 1998, the date of enactment of the Donation Protection Act. The questionnaire asked the trustees to specify or estimate the total number of Chapter 13 cases in which they had served that were commenced on or after June 19, 1998. Most trustees had actual data on this issue because they keep track of each debtor in a different case file. The questionnaire also asked the trustees to identify the number of Chapter 13 cases where confirmation of a plan was denied or modified or the case was dismissed or converted based on tithes or charitable contributions. Almost all of the trustees estimated this data because they do not keep track of their pending cases on this basis. The questionnaire asked the Chapter 13 trustees to specify the number of cases in which the Donation Protection Act reduced distributions to creditors compared to what distributions would have been under the law in place before enactment of the Donation Protection Act. The trustees' responses to this question were estimates based on subjective comparisons of results.

The Chapter 7 questionnaire was also accompanied by a cover letter[66] explaining briefly how the Donation Protection Act has changed fraudulent conveyance law and requesting information about religious tithes and charitable contributions in Chapter 7 cases since June 19, 1998, the date of enactment of the Donation Protection Act. The questionnaire asked the trustees to specify or estimate the total number of Chapter 7 cases in which they had served that were commenced on or after June 19, 1998. Almost all trustees had actual data on this issue because they keep this information to report to either the Office of United States Trustee or the Bankruptcy Administrator. The questionnaire also asked the trustees to identify the number of Chapter 7 cases that involved and did not involve charitable donations or tithes. Most trustees estimated these data. The questionnaire asked the Chapter 7 trustees to specify the number of cases in which the Donation Protection Act reduced distributions to creditors compared to what distributions would have been under the law in place before enactment of the

[65]Readers may view the Chapter 13 cover letter *at id.*

[66]Readers may view the Chapter 7 cover letter *at id.*

Donation Protection Act. In response, the trustees necessarily provided estimates based on their subjective comparison with results before the effective date of the Donation Protection Act. The questionnaire also asked trustees for data concerning avoiding power causes of action involving charitable donations, tithes, or pledges. Some trustees responded with specific data, but others provided estimates for their responses. The questionnaire also asked trustees to provide data concerning instances in which a debtor was denied a discharge or suffered a nondischargeable debt due to a charitable donation or tithe. Most trustees who answered this question estimated their answer. Finally, the questionnaire adduced data on the conversion and dismissal of Chapter 7 cases due to charitable donations or tithes. Most trustees provided estimates in their responses to these questions.

B. Chapter 13 Cases

According to data compiled by the Administrative Office of the United States Courts, debtors commenced 769,774 Chapter 13 cases between June 30, 1998 and June 30, 2000.[67] As noted in the Appendix, over thirty-seven percent of the Chapter 13 trustees completed and returned the questionnaire. These trustees reported working on 254,086 Chapter 13 cases commenced on or after June 19, 1998, or about thirty-three percent of the Chapter 13 cases commenced.

Trustees reported data for 210,680, or about 83%, of the 254,086 cases they administered.[68] The cases for which

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[67] *See* Administrative Office of the United States Courts, Table F-2, U.S. Bankruptcy Courts Business and Nonbusiness Bankruptcy Cases Commenced, by Chapter of the Bankruptcy Code, During the Twelve Months Period Ended June 30, 1999 and Table F-2, U.S. Bankruptcy Courts Business and Nonbusiness bankruptcy Cases Commenced, by Chapter of the Bankruptcy Code, During the Twelve Months Period Ended June 30, 2000 *at* http://www.uscourts.gov/news.html (last visited August 10, 2000) ("A.O. Tables"). *See also* News Release, Aug. 11, 2000, summarizing results at http://www.uscourts.gov/press_releases/press_8112000.pdf (last visited June 8, 2001).

[68] This leaves 43,406 unreported cases where trustees failed to supply data. Presumably, some trustees identified the total number of Chapter 13 cases on which they worked but chose not

trustees provided data are referred to as "reported cases." Among these 210,680 reported cases, charitable donations or tithes were involved in 47,146 cases, or about 22% of the reported cases. If these data are representative of all Chapter 13 cases, this means that within the two years of enactment about one in every four families in Chapter 13 has claimed a place in their budget for charitable giving.

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to estimate data for all or part of their cases.

The trustees report that charitable donations or tithes reduced the dividend to creditors compared with the result that would have obtained under Chapter 13 before enactment of the Donation Protection Act in about 4.7% of the reported cases. The trustees thus identify charitable contributions as affecting creditor distributions[69] in about twenty-one percent of the cases in which charitable donations or tithes were involved.[70]

The trustees' assessments, however, may be understated. Except for those cases in which the debtor has ample assets to pay all creditors in full, assets contributed to charities and churches almost necessarily reduce distributions to unsecured creditors.[71] The trustees may be accounting for 100% plans, so that creditors are paid in full over the life of the plan regardless of whether the debtor makes any charitable contributions.

The trustees may give a smaller estimate of the impact of the new law because the question asked the trustees to compare results to what would have happened under Chapter 13 had the Donation Protection Act not been enacted. Some courts allowed tithing in Chapter 13 cases before enactment of the Donation Protection Act.[72]

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[69]The questionnaire, which is reproduced in full in the Appendix, asked the trustees the following question:

> With respect to the chapter 13 cases **filed after June 18, 1998** in which you served as trustee, the Religious Liberty and Charitable Donation Protection Act **decreased** the amount that would have been distributed to creditors compared to what they would have received had the Chapter 13 plan been **confirmed under the previous law** in _____ cases.=ft

[70]*See, e.g., In re* McDaniel, 126 B.R. 782, 784-85 (Bankr. D. Minn. 1991); *In re* Bien, 95 B.R. 281, 283 (Bankr. D. Conn. 1989); *In re* Navarro, 83 B.R. 348 (Bankr. E.D. Pa. 1988).

[71]Theoretically, there also would be no reduction in distributions to creditors if the confirmed plan distributed nothing to unsecured creditors and the entire recovered contribution would defray administrative expenses. *See* 11 U.S.C. § 1326(b) (1994).

[72]*See, e.g., In re* Bien, 95 B.R. 281; *In re* Navarro, 83 B.R.

348; *In re* Green, 73 B.R. 893 (Bankr. W.D. Mich. 1987), *aff'd*, 103 B.R. 852 (W.D. Mich. 1988).

A third and most likely explanation for possible understatement is that the trustees were making a substantive judgment about the effects of tithing. If the debtor's debts are substantial and the amount reserved for charitable contributions is modest, the effects of tithing may have a mathematically traceable effect on the distribution to creditors, but the substantive effect may be negligible. For example, according to actual data collected about 1991 Chapter 13 debtors by professors Sullivan, Warren and Westbrook,[73] the average debtor had total debts of $50,783, consisting of $29,879 in secured debts and $20,706 in unsecured debts.[74] By comparison, in 1991, the average annual charitable or religious contributions were $899 for contributing households, without regard to solvency.[75] Thus, contributions amount to only 1.77% of average total debts and 4.34% of average unsecured debts of 1991 Chapter 13 debtors.[76] The average annual charitable or religious contributions would undoubtedly be less for financially troubled households nationally. In

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[73]*See* Teresa A. Sullivan, et al., *Consumer Debtors Ten Years Later: A Financial Comparison of Consumer Bankrupts 1981-1991*, 68 Am. Bankr. L.J. 121, 128 (1994). These debt figures are means. Median figures for 1991 Chapter 13 debtors are $31,077 in total debts of which $10,953 are secured debts and $13,023 are unsecured debts. *See id.*

[74]Adjusting for inflation, in 1999 dollars the average Chapter 13 debtor would have total debts of $62,209, consisting of $36,602 in secured debts and $25,365 in unsecured debts. The annual consumer price index ("CPI") for 1991 was 136.2, for 1998 was 163.0, and for 1999 was 166.6. The January through June 2000 CPI is 170.8. Averaging these yields 166.8 or 166.9 as an approximate CPI for the July 1998 through June 2000 data period. Thus 1.225 is the appropriate multiplier to make 1991 numbers comparable to the data base.

[75]*See* Office of Educational Research and Improvement, Digest of Education Statistics, 1999 (Table No. 30 Percentage of Households Contributing To Education And Other Charitable Organizations And Average Annual Donation, By Type Of Charity: 1989, 1991, 1993, And 1995) *available at* http://web.lexis-nexis.com/statuniv (last visited Dec. 26, 2000).

[76]The percentages would not change when adjusted for inflation to 1999 dollars, because both the numerator, relating to contributions, and denominator, relating to total debts, would adjust at the same rate.

many cases, the costs of recovering these contributions would approach or exceed the amounts recovered.

Charitable donations may have another effect on consumer bankruptcy cases. Now that the law protects some donations, debtors may try to reduce their disposable incomes beyond an amount acceptable for plan confirmation. According to the trustees, from June 1998 through June 2000, charitable donations and tithing had a negligible impact on case administration. Of the Chapter 13 reported cases, only 109, or .05%, involved denial of a plan confirmation based on a claim for charitable contributions. Moreover, 799, or .38%, involved modifications of plans based on charitable contributions or tithes.[77] In addition, charitable contributions and tithes caused dismissals in another sixty reported cases and conversions in only sixteen reported cases.[78] Altogether, this means that the plan initially proposed by the debtor was rejected, modified, or adversely affected in some way in about .467% of all reported cases. If those data are extrapolated to the 769,774 debtors who filed petitions under Chapter 13 from July 1998 through June 2000,[79] an estimated 3600 debtors stumbled in the proposal or consummation of a plan that involved ongoing charitable contributions.

In addition to providing basic data about charitable donations in Chapter 13 cases, the trustees also offered their views about the effect of the Act. Most of the trustees thought the Donation Protection Act had very little impact on Chapter 13 cases,[80] although some found the amount of donations

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[77]Readers may view the data base *at* http://www.law.ucla.edu/erg/pubs.html (last modified April 6, 2001). Since most Chapter 13 plans last three to five years and the Donation Protection Act has only been effective for somewhat over two years, it may be premature to gauge the data on plan modification. *See* 11 U.S.C. § 1322(d) (1994).

[78]Readers may view the data base *at* http://www.law.ucla.edu/erg/pubs.html (last modified April 6, 2001).

[79]*See* A.O. Tables, *supra* note 67.

[80]Typical responses: “I don’t think it has made a big impact;” “The impact . . . has been relatively minor;” “has had no practical impact;” and “has had little, if any, impact.”

or tithes that debtors reported to be increasing.[81] Because the trustees may be more inclined to notice donations that have a substantive impact, the suggestion of a trend toward increasing donations may be of some significance.

[81]For example: "Frequency of tithing cases is increasing . . .," and "I see an increasing number of debtors who can afford to make regular substantial contributions." According to ABC News, America's leading charities had contributions increase in 1999 by 13 percent over 1998. *See* http://www.abcnews.go.com/sections/us/DailyNews/philanthropy001029.html (last visited Dec. 21, 2000). *Accord* http://www.amarillonet.com/stories/103000/usn_charity.shtml (last visited June 8, 2001) (citing Chronicle of Philanthropy).

A few trustees suggested that the Act indirectly decreased distributions to secured creditors as well as unsecured creditors.[82] The reduction to unsecured creditors is obvious: To the extent the debtors pay tithes, they reduce the amount available for general distribution to their unsecured creditors. But the suggestion that secured creditors might also receive lower distributions is more subtle. A debtor with higher expenses, including those associated with tithing, may be forced to refinance secured debt over a longer period of time. In that event, interest will accrue on the secured debt to a greater extent than had the tithes been used to reduce principal or service interest. Because unpaid interest can accrue at high compound rates, ultimately delayed service of secured debt can reduce payments to unsecured creditors under the plan far in excess of the face amount of the tithes. The number of plans in which debtors pay only their secured creditors, often called zero-payment plans to reflect the absence of distribution to the unsecured creditors, is small but significant.[83] In those cases, distributions to secured creditors, rather than unsecured creditors, will be affected by the debtors' decision to dedicate a portion of current income to tithing.

This point is even more complex when it is embedded in the reality of how debtors and Chapter 13 trustees construct Chapter 13 plans. Debtors have limited income; as a result, Chapter 13 trustees often push and pull the valuation of collateral, determination of interest rates, and length of repayment of secured debts until they fit the available income. As a practical matter, therefore, carving charitable donations out of the budget may simply reduce the amount that is left for secured creditors under the plan.

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[82]"Creditors are impacted because payments on secured and priority debt is delayed, and fewer funds are available for distribution to unsecured creditors."

[83]For example, in one empirical study, professors Sullivan, Westbrook and Warren found that, of 591 Chapter 13 cases, 17 proposed payment to unsecured creditors of one percent or less. TERESA A. SULLIVAN, ET AL., AS WE FORGIVE OUR DEBTORS: BANKRUPTCY AND CONSUMER CREDIT IN AMERICA, 45 n.27 (1989). Although some judges confirm zero plans, many judges, however, refuse to confirm zero plans. *See* NAT'L BANKR. R. COMM'N, BANKRUPTCY: THE NEXT TWENTY YEARS, FINAL REPORT 235, 267 n.330 (1997) (an informal survey of twenty-four Seventh Circuit bankruptcy judges revealed that eleven never confirmed zero payment plans).

Although the Act's effect on creditors could have been anticipated at the time it was passed, one unexpected consequence on plan repayment may emerge. Some trustees thought the Act's support of postpetition tithing might be increasing the success rate of Chapter 13 plans and the length of time over which debtors can actually repay unsecured creditors by building flexibility into a debtor's budget. A debtor is committed to make all the payments specified in the plan; if the payments are not made, the trustee can move to dismiss the case. Currently two-thirds of Chapter 13 cases are dismissed because the debtor fails to make scheduled payments.[84] A debtor who has an entry in the budget for a charitable donation has flexibility; money could be diverted from the charitable donation portion of the budget to allow the debtor to comply with the plan.

One trustee noted that wide utilization of charitable contributions "has resulted in personal budgets that are less restrictive and more realistic. The positive result of passage of this Act will not only be a clearer understanding of the allowances of 'donations' but that the success/completion factor of Chapter 13 will be increased as well." Another reported that the Act "probably has the effect of having debtors giving me a more realistic budget on their church donations" than before passage of the Act. Indeed if this result comes to pass, Congress should consider building in a cushion for debtors generally to eliminate the anomaly under the Act that only debtors who donate or tithe enjoy the cushion.

This suggestion is particularly important in light of the practices in some courts to allow no emergency or reserve fund.[85] The Act may have had the quite inadvertent effect of making plans more realistic for debtors who tithe, an effect that ultimately could inure to benefit both debtors and creditors. Debtors will benefit because they will be able to

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[84] *See* NAT'L BANKR. R. COMM'N, BANKRUPTCY: THE NEXT TWENTY YEARS, FINAL REPORT 233 (1997).

[85] *See, e.g., In re* Reyes, 106 B.R. 155 (Bankr. N.D. Ill. 1989) (court refused to allow the debtor to budget $40 a month for contingencies); *In re* Krull, 54 B.R. 375 (Bankr. D. Colo. 1985) (court refused to allow the debtor to budget $35 per month for contingencies).

reduce tithes or charitable contributions to fund temporary shortfalls that would otherwise result in a defaulted plan. Creditors might suffer an original detriment because some money that would have gone to them will instead be used for tithing, but they might ultimately benefit because increased flexibility in the debtor's budget will result in more completed plans.

The Act has some flexibility in it, opening the possibility that different trustees may adopt different practices about what level of donations are and are not acceptable and what proof of donations shall be required. While the Act sets a floor, as Part III demonstrates below, there remain a number of open questions of administration. Some trustees reported that the Donation Protection Act caused them to be liberal in their allowance of tithing expenses that remained under fifteen percent of gross income.[86] Others stated that they still required the debtor to prove a history of tithing even if the amount is less than fifteen percent of the debtor's gross income.[87] The concept of Local Legal Culture, first documented in the bankruptcy field by Professors Sullivan, Warren and Westbrook,[88] may flourish here as it does in a host of other Chapter 13 practices.[89]

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[86]For example: "I always allow tithes;" and "I have had situations where the debtor's counsel informs me pointedly that I cannot question the charitable donation."

[87]Representative responses: "I require proof that this is a habit. . . . If they cannot prove it, the debtor's attorney voluntarily amends the plan to eliminate the expense;" "debtors must show a history of the donation;" and "our interest is not necessarily the amount but confirming that they have a historical record supporting the donations."

[88]*See generally* Teresa A. Sullivan, et al., *The Persistence of Local Legal Culture: Twenty Years of Evidence From the Federal Bankruptcy Courts*, 17 HARV. J.L. & PUB. POL'Y 801 (1994).

[89]*See generally* Gordon Bermant & Ed Flynn, *Measuring Projected Performance in Chapter 13: Comparisons Across States*, 19 AM. BANKR. INST. J. 22, 34-35 (Aug. 2000). It remains to be determined whether the "local legal culture" will depend more on the geographical area in which a case is filed or the identity of the particular judge or Chapter 13 trustee who has dominion over the case.

C. Chapter 7 Cases

The response rate for Chapter 7 trustees was lower than for Chapter 13 trustees. Approximately 16.4%[90] of the Chapter 7 panel trustees completed and returned the questionnaire, about half the response rate of the Chapter 13 trustees.[91] According to data compiled by the Administrative Office of the United States Courts, 1,878,861 Chapter 7 cases were commenced between June 30, 1998 and June 30, 2000.[92] Chapter 7 panel trustees who returned the questionnaire reported working on 297,306, or about 15.8%, of the Chapter 7 cases commenced on or after June 19, 1998. The data reflect the trustees' experience in 252,936, or about 13.3%, of all Chapter 7 cases commenced.

The relatively low response rate of the Chapter 7 panel trustees might be attributable to several factors. Chapter 7

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[90]Two hundred ten Chapter 7 panel trustees (out of 1274 solicited) returned completed questionnaires which the author received between July 12 and October 2000.

[91]As referenced *infra* in text accompanying note 170, any return rate over thirty percent generally is considered successful. *See* The Pew Research Center For The People & The Press, March 27, 1998, *Opinion Poll Experiment Reveals Conservative Opinions Not Underestimated, But Racial Hostility Missed at* http://www.people-press.org/resprpt.htm, (last visited Oct. 19, 2000). The response rate of the Chapter 7 panel trustees is less than half the rate of response of the Chapter 13 trustees.

[92]*See* A.O. Tables, *supra* note 67. *See also* News Release, August 11, 2000, summarizing results *at* http://www.uscourts.gov/press_releases/press_8112000.pdf (last visited June 8, 2001).

trustees have a much shorter encounter with most consumer debtors. Typically, they review files and question the debtors at the first meeting of creditors and never see the debtors again. The examinations are short, and the trustees receive minimal payment. Unlike Chapter 13 trustees who supervise payments over three to five years, Chapter 7 trustees have little reason to keep extensive records. Moreover, a much larger proportion of Chapter 7 trustees are part-time, and they may not be set up to monitor this kind of information.[93]

[93]The mean case load for a Chapter 13 trustee was 3888 during the two-year measuring period. By comparison, the mean case load for a Chapter 7 trustee was 1475. *See id.*

Several trustees responded to the questionnaire by explaining that they did not keep data on the issues addressed by the questionnaire and were unwilling to estimate results.[94] The high variation in results[95] from trustees within the same state might support an inference that Chapter 7 trustees as a group do not have a high degree of confidence in their understanding of the incidence of tithing in their cases.[96]

The assistance provided by the National Association of Chapter 13 Trustees in disseminating the questionnaire and urging its completion is more likely to account for a higher response rate than any other factor. Even with a relatively low response rate, the Chapter 7 trustees' written comments offer an important glimpse into tithing in Chapter 7 cases.

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[94]OFFICIAL BANKRUPTCY FORM 6, Schedule J, requires a debtor to provide a Chapter 7 trustee or Chapter 13 trustee with data regarding a debtor's intended future charitable contributions and tithes. Chapter 13 trustees also have access to what the debtor proposes to contribute or tithe under a Chapter 13 plan. These data are irrelevant to Chapter 7 trustees who focus exclusively on a debtor's prepetition conduct.

[95]For example, one Florida Chapter 7 trustee estimated that 1800 of 2400, or seventy-five percent, of Chapter 7 debtors made charitable contributions or tithed whereas three other Florida Chapter 7 trustees estimated that none of 4000, none of 3150, and none of 500 of debtors did so. Two other Florida Chapter 7 trustees estimated that 300 of 2400, or 12.5%, and 200 of 2000, or 10% of debtors did so. These disparities might be explained based on different practices in different judicial districts within the state, but that explanation does not seem likely. Applying a chi-square test reveals that these disparities are statistically significant ($n=14,450$; chi-square 7781; $p<.001$).

[96]The data neither confirm nor disprove this hypothesis with any acceptable degree of statistical significance.

Most of the trustees thought the Donation Protection Act had very little or no impact on Chapter 7 cases.[97] Some attributed this to debtors' limited resources.[98] Others candidly admitted that the Act had no significant impact because the judges in their districts did not like to get into religious issues and second guessing charitable contributions even before the Act was passed.[99] Still other trustees saw little impact due to their personal proclivity or tendency not to pursue charitable contributions or tithes.[100]

On the other hand, some trustees reported that tithing was quite important in the small number of cases in which tithing is involved.[101] And a few trustees viewed the Donation Protection Act as special interest legislation that opened the door for abuse.[102] One trustee speculated that debtors were

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[97]Trustees reported the Donation Protection Act was "not much of a factor," “not a big issue here," and "not an issue."

[98]For example, one trustee opined that "very few debtors can afford to pay tithes." Another noted, "in my cases, debtors don't have the incomes to make substantial charitable donations or tithes."

[99]Trustees reported that "our courts have been tolerant of tithes," and "our judges don't like to get into religious issues and second guess charitable contributions unless very egregious." One trustee expressed a personal preference to pursue tithes but noted "in this district, the generally accepted practice is not to challenge charitable donations."

[100]Representative responses include: "I am pleased Congress enacted legislation to protect charities/churches. . . . I have never sued to recover charitable contributions to legitimate charities or churches." "If tithes are part of a person's religious conviction, I personally have difficulty objecting to that conviction in the bankruptcy arena."

[101]For example, "I have only had one case . . . [but] in that case the donations were extreme: fifty thousand within the year of filing;" "The debtor's principal donated $1.6 million to many charities;" "Debtors transferred $35,000 on the eve of Bankruptcy;" and "I probably can count on one hand the amount of cases that had unusually high contributions."

[102]Representative comments include: "I believe it set up possibility for abuse;" "it does open the possibility for debtors to abuse their creditors;" "the law violates

deliberately refusing to disclose amounts they were tithing.[103] Other trustees reported that the Donation Protection Act completely eliminated their earlier practice of avoiding charitable donations and tithes.[104]

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creditors' rights;" and "A silly act pushed through by conservative religious zealots. Its function has provided a shield for a select few . . . . Another gold star for the best Congress that money can buy."

[103]"It is rare that I see anyone list regular charitable contributions on his statement of expenses. I believe both the city debtors and the country debtors who go to church are giving to the church. . . . For the most part they are very proud people and they would no more tell you or me what they are giving to their church than they would discuss their sex lives. It is between them and God."

[104]For example, "Prior to enactment of the law, I had 15 to 20 fraudulent conveyance claims per year. . . . I routinely settled such claims on the basis of 50% settlement with the religious institution. Subsequent to the enactment of the law I have not had one case."

The numerical data are somewhat surprising. Charitable donations or tithes were involved in about 11.5% of the reported cases. If these data are representative of the population of individual debtors in Chapter 7 nationwide, then about 216,000 Chapter 7 debtors made prebankruptcy charitable donations in cases commenced between July 1998 and June 2000.[105]

The questionnaire sought data on charitable contributions and tithing without attempting to distinguish the two. Clearly, the 11.5% rate is well above the estimated national average of four to five percent rate for all families that claim to tithe.[106] But the rate is well below the forty-eight percent of households that claimed to make at least one contribution to a charity in 1995.[107]

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[105] *See* A.O. Tables, *supra* note 67.

[106] *See* Pollack, *supra* note 1, at 537 & n.54 (estimating that the rate of true tithers is four to five percent).

[107] *See* Bureau of Census, Statistical Abstract of the United States 404 (1999) (Table No. 645 Charity Contributions—Percent of Households Contributing, by Dollar Amount, 1991 to 1995, and Type of Charity, 1995)., *available at* http://www.census.gov/prod/www/statistical-abstract-us.html (last visited June 8, 2001).

The report of 11.5% of debtors making charitable donations appears to be inconsistent with the widely held view that very few bankrupt debtors tithe or otherwise make charitable contributions. In the Chapter 7 context, prepetition charitable contributions are important as a source of recovery of funds for distribution to creditors. Trustees examine prepetition tithes and contributions with a view to possible avoidance, asking the recipient to disgorge what was given by the insolvent debtor shortly before the bankruptcy filing. In most cases, when debtors tithe, the amount is too small to justify the trustee bringing suit.[108] Perhaps this explains the trustees' estimate that from July 1998 through June 2000, in about .6% of the Chapter 7 reported cases, or an estimated 11,300 cases nationwide, charitable donations or tithes reduced the dividend to creditors.[109] Once again, while there may be a mathematical effect on distributions in nearly every case, the trustees may be making a substantive judgment that the amount that could be recovered is so modest either in relation to the cost of recovery or in relation to the size of the debts over which the recovery must be distributed that the effect on any one creditor is vanishingly small.

The trustees estimate that charitable donations and tithing have an even smaller impact on case administration. Of the 249,555 reported cases, only 11 involved avoiding power actions related to a charitable donation or tithe and one involved a charitable pledge. Based on this response, it is possible to estimate that trustees moved to avoid charitable contributions in about 90 Chapter 7 cases during July 1998 through June 2000.

In evaluating this number, however, it is important to note that trustees generally have two years from the time the debtor files for bankruptcy to initiate preference and

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[108]For example, "many debtors show an expense for donating tithes monthly, but it's usually a nominal amount;" "Few debtors make charitable contributions, and amounts contributed are too small to make any significant difference;" and "In a number of cases, contributions have been indicated, but they were not significant enough to make an issue of them."

[109]Many Chapter 7 cases are no asset cases so amounts recovered in avoidance actions would pay administrative expenses rather than be distributed to creditors. *See* 11 U.S.C. § 726(a) (1994).

fraudulent transfer avoidance actions.[110] In the author's experience, even though trustees review schedules and examine debtors early in the Chapter 7 case, trustees often wait to file suit on the day before the statute of limitations expires.[111] Therefore the very small number of reported cases may arise because most reported cases were not two years old when the data were collected.

Based on the responses from trustees, no debtors had discharges denied or debts declared nondischargeable due to charitable contributions or tithes. And the data for dismissal and conversion are barely noticeable. Charitable contributions and tithes caused dismissals in twenty-six cases and conversions in twenty-four Chapter 7 reported cases. The statute of limitations cannot explain the impact of charitable contributions and tithes on discharge and dischargeability because these actions must be brought immediately.[112] Thus by any measure, tithes and charitable contributions are not a factor in the overwhelming majority of these areas.

D. Lessons to be Learned

The clear purpose of the Donation Protection Act was to insulate institutions that receive tithes and debtors who make tithes from attack in bankruptcy cases. Powerful religious institutions exerted their influence with Congress successfully to restore bankruptcy practice to their favor. To date, based on the data and the reported opinions, most judges appear to adhere to the will of Congress and enforce the letter of the law as they are bound to do. Even so, the Donation Protection Act permits future abuse of the consumer bankruptcy system. By insulating charitable and religious donees from the ordinary rules of gift giving by insolvent debtors, the Donation Protection Act encourages debtors to

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[110] *See* 11 U.S.C. § 546(a) (1994).

[111] Trustees may bring avoiding power actions against creditors long after the debtor has received a discharge. If a trustee identifies several avoidable transfers, sometimes a trustee will bring suit early to avoid a small transfer. This strategy can lead to settlement and help build a war chest to finance larger litigation, and it can also educate the bankruptcy judge about issues that will recur in numerous similar litigations.

[112] *See* Fed. R. Bank. P. 4004(a), 4007(c).

diminish distributions to their creditors.

As noted above, the law specifically states that in making a determination whether to dismiss a Chapter 7 filing for substantial abuse the court may not take into consideration whether the debtor has tithed or continues to tithe.[113] Chapter 13 law requires the court to exclude tithes from the definition of disposable income available to repay creditors under a plan.[114] But the passage of a law does not assure that interpretation and implementation of the law will be made in accordance with Congressional intent. Both the reported cases and collected data refute the author's expectation[115] that courts and trustees would continue to use the debtor's tithing as a basis to dismiss Chapter 7 cases[116] or deny confirmation of Chapter 13 plans.[117] In particular, of

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[113]*See* 11 U.S.C. § 707(b) (Supp. IV 1998).

[114]*See* 11 U.S.C. § 1325(b)(2)(A) (Supp. IV 1998).

[115]The author expected that a significant number of judges would disagree with Congressional policy to protect tithers and donees embraced in the Donation Protection Act. The author also expected these judges to avoid special interest legislation and dilution of distributions to creditors by converting or dismissing cases or denying confirmation of Chapter 13 plans at about the same rate as they had done before enactment of the Donation Protection Act. Based on the collected data and reported opinions, very few courts have performed in accord with these expectations. *See infra* notes 116-17 and accompanying text. The author underestimated the tendency of most judges to follow the statute or their underlying agreement with Congressional policy underlying the law. In part this may be due to a desire by some courts to protect charitable contributions from the scope of fraudulent transfer laws. *See* Julianne Belaga, *Now You See It, Now You Don't: The Impact of RFRA's Invalidation on Religious Tithes in Bankruptcy*, 14 BANKR. DEV. J. 343, 344 (1998) ("The obstacle in the path of fraudulent conveyance laws was one for which numerous courts had searched.").

[116]But some courts still consider tithing as the basis to dismiss a bankruptcy case. *See In re* Smihula, 234 B.R. 240, 243 (Bankr. D.R.I. 1999).

[117]But some courts still consider tithing as a basis to deny confirmation of a Chapter 13 plan. *See In re* Buxton, 228 B.R.

the 249,555 Chapter 7 reported cases and 29,155 cases in which tithing was involved, charitable donations and tithes accounted for dismissal in only 16 cases. Of the 210,680 Chapter 13 reported cases and 47,146 in which tithing was involved, only 109 resulted in dismissal due to charitable contributions or tithes. Based on these data, charitable donations and tithes appear to have reverted to the nearly invulnerable status they enjoyed under the Bankruptcy Act where they were immune in practice but not in theory. But it would be a mistake to assume that charitable donations and tithes have once again become a nonissue in bankruptcy cases following enactment of the Donation Protection Act.

These data show that charitable donations or tithes are involved in twenty-two percent of Chapter 13 cases and eleven percent of Chapter 7 cases.[118] This means that an estimated 249,000 new consumer bankruptcy cases each year involve insolvent debtors who made charitable donations or tithes. Presumably, in most cases the amounts donated or tithed are modest and not significant to the creditors. But over time, in a small number of cases, debtors will make large contributions or tithes before bankruptcy or under a Chapter 13 plan. If commentators and the media magnify these abuses as they did with debtor abuses of unlimited homestead exemptions,[119] these few cases involving large contributions could undermine public confidence in the consumer bankruptcy system.

606, 611 (Bankr. W.D. La. 1999).

[118]It is possible that there is an overreporting bias in the data from trustees whose experience with tithes makes this issue salient.

[119]For example, the media frequently reported that, fearing bankruptcy, former Commissioner of Major League Baseball Bowie Kuhn moved from New York to Florida and purchased a multimillion dollar home subject to Florida's unlimited homestead exemption. *See* David Margolic, *Bowie Kuhn is Said to be in Hiding*, N.Y. TIMES, June 19, 1990, at D1.

Moreover, when the data are analyzed more closely, interesting trends emerge. The literature has noted over the years that regional variations in social norms and local legal culture account for disparities in the relative use of Chapter 7 and Chapter 13.[120] Indeed, data from reported cases show that Chapter 7 filings far outstrip Chapter 13 filings in Maine, New Hampshire, Rhode Island, and West Virginia, while the reverse is true by a wide margin in most of the Southern states.[121] This result is not surprising and not new.[122]

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[120]*See, e.g.*, Teresa A. Sullivan et al., *The Persistence of Local Legal Culture: Twenty Years of Evidence from the Federal Bankruptcy Courts*, 17 HARV. J.L. & PUB. POL'Y 801 (1994); Jean Braucher, *Lawyers and Consumer Bankruptcy: One Code, Many Cultures*, 67 AM. BANKR. L.J. 501 (1993).

[121]In these northern states, fourteen Chapter 7 cases were filed for every Chapter 13 case filed. In seven southern states (Georgia, Alabama, North Carolina, Tennessee, South Carolina, Texas and Arkansas) an average of .85 Chapter 7 cases were filed for every Chapter 13 case. Readers may view the Chapter 7 to Chapter 13 filing data *at* http://www.law.ucla.edu/erg/pubs.html (last visited June 8, 2001). *Accord* A.O. Tables, *supra* note 67.

[122]*See, e.g.*, Gordon Bermant, *Exploring the Demographics of Consumer Chapter Choice*, 18 AM. BANKR. INST. L.J. 26, 27 (1999) ("the states with the highest Chapter 13 filing rates occupy the southern tier of the country, with the exception of Utah"); Michael Bork & Susan D. Tuck, Adjustment of Debts of an Individual with Regular Income (Working Paper 1) (Jan. 1994) (unpublished manuscript, on file with author) (finding that Chapter 13 is most commonly found in southeastern states and that Chapter 13 cases accounted for more than fifty percent of total case filings since 1981 in nine districts, eight of which were in the Southeastern states); Teresa A. Sullivan et al., *The Persistence of Local Legal Culture: Twenty Years of Evidence From the Federal Bankruptcy Courts*, 17 HARV. J.L. & PUB. POL'Y 801 (1994); Michael Bork & Susan D. Tuck, Administrative Office of United States Courts, Bankruptcy Statistical Trends: Chapter 13; Adjustment of Debts of an Individual with Regular Income (Working Paper I) (Jan. 1994) (finding that Chapter 13 is most commonly used in Southeastern states excluding Florida, and that Chapter 13 cases accounted for more than 50 percent of total case filings since 1981 in nine judicial districts, eight of which were Southeastern states).

What is new is the result when tithing is factored into the mix. As noted above, the data show that Chapter 13 debtors tithe in roughly twenty-two percent of the reported Chapter 13 cases whereas Chapter 7 debtors tithe in only about 11.5% of the reported Chapter 7 cases. The difference is significant, if not surprising. This disparity might arise from the use of postpetition income to tithe in Chapter 13 cases versus prepetition income in Chapter 7 cases. But the nonuniformity of the relationship between tithing and the chapter under which the case proceeds raises questions about the validity of this hypothesis. For example, the hypothesis does not explain the phenomenon in Rhode Island where most cases are filed under Chapter 7 but tithing is high.[123] In Rhode Island, tithing reached 46.8% of all filed cases, a finding made more remarkable by the fact that 94% of Rhode Island bankruptcy cases are filed under Chapter 7 rather than split one-third/two-thirds between Chapter 13 and Chapter 7.[124] These data rank Rhode Island ahead of high-tithing high-Chapter 13 states such as Utah.[125] Moreover, the tithing differential between Rhode Island and Utah is statistically meaningful with a chi-square statistic of 116.48 (n=4530; $p < 0.0001$ (corrected for continuity)). These data suggest the pertinence of other factors in a locality that strongly affects debtor and creditor outcomes.

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[123]For the two-year period commencing July 1, 1998 and ending June 30, 2000, Rhode Island had 9479 Chapter 7 cases but only 601 Chapter 13 cases. By comparison, Utah (another high tithing state) had 17,253 Chapter 7 cases and 11,018 Chapter 13 cases. *See supra* note 67, A.O. Tables.

[124]The 46.8% incidence of tithing in Rhode Island Chapter 7 cases ranks Rhode Island third behind South Carolina and New Mexico. *See* http://www.law.ucla.edu/erg/pubs.html (last visited June 8, 2001).

[125]Utah, with a 31.1% incidence of tithing in Chapter 7 cases, ranks sixth. *See id.* In fact, compared to the South, Utah has more tithing than expected in Chapter 7 cases by a factor of 2 (or the South has less tithing than expected) with a chi-square statistic of 874.08 (n=69,678; $p<0.0001$ (corrected for continuity)). *See id.* This highlights the comparison between Utah and Rhode Island as a phenomenon that might lead to additional research.

The region within which a case is filed also tends to affect the debtor's propensity to tithe.[126] This regional effect is discernable when the natural log of the ratio of Chapter 13 tithing cases to nontithing cases is plotted on one axis against the natural log of the ratio of Chapter 13 cases to Chapter 7 cases on the other axis. Here the data show that the rate of Chapter 13 tithing cases is higher in southern states (20%) than in nonsouthern states (10%), with a significance level of .05 (one-tailed t-test).[127]

These data cannot be explained solely on the basis of underlying regional religious differences. According to the Bureau of Census, in 1997, seventy-three percent of the civilian population eighteen years of age and older living in the South[128] were members of a church or synagogue.[129] Although this is much higher than the fifty-one percent rate for the West, it is about the same as the seventy percent rate for the

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[126]As noted, Rhode Island with low Chapter 13 filings but high tithing is an exception to the basic proposition that region affects tithing since other states in the East have much lower propensities to tithe. For example, comparing the data between Rhode Island and New York produces statistically significant results. (n=14166; chi square = 3672; p<.001 (corrected for continuity)). *See id.*

[127]The data also indicate that Chapter 13 debtors tithe at a higher rate in those states where the ratio of Chapter 13 to Chapter 7 cases is higher (Pearson's r = 36, p = .04). Those states where the Chapter 13 to Chapter 7 ratio is highest are from the South (Georgia, Alabama, North Carolina, Tennessee, South Carolina, Texas).

[128]The Bureau of Census defines the "South" to include Kentucky, Tennessee, Virginia, North Carolina, South Carolina, Georgia, Florida, Alabama, Mississippi, Texas, Arkansas, Oklahoma, and Louisiana. *See* Bureau of Census, Statistical Abstract of the United States 71n.5 (1999) (Table No. 89 Religious Preference, Church Membership, and Attendance: 1980 to 1998) *available at* http://www.census.gov/prod/www/statistical-abstract-US.html (last visited June 8, 2001).

[129]*See id.* at 71. Of course it is possible that members of different religions tithe at different rates and that they are disproportionately represented in the different regions. No data are available to resolve these issues definitively.

East and the seventy-three percent rate for the Midwest. Thus religious membership alone cannot explain the proclivity of debtors in the South to tithe more in Chapter 13 cases.

The foregoing analysis suggests that despite the constitutional requirement that the Bankruptcy Laws of the United States be uniform, the consumer bankruptcy system is complex and diverse. Congress has done nothing to document this diversity or investigate its root causes. Nevertheless, by legislating the Donation Protection Act, Congress has changed the way our consumer bankruptcy system works. As Congress intended, substantial numbers of debtors are making charitable contributions and religious donations that are nearly impervious to attack in Chapter 7 cases and that reduce the return to creditors but keep the contributions flowing in Chapter 13 cases. Although not many debtors have yet begun to abuse the opportunity to make charitable contributions and religious donations, time will tell whether debtor abuse will increase. Most fundamentally, however, Congress evidently has unwittingly increased the success rate of Chapter 13 plans by providing a protected source of discretionary income for tithes and donations that is built into the Chapter 13 debtor's budget.

The two years of data analyzed in this Article provide a starting point but do not comprise a time series from which scholars might evaluate long-term trends. The analysis suggests important questions about local legal culture, including the role of judges, lawyers, and community standards in producing variable results under a uniform federal law. Follow-up projects might measure the extent to which debtors abuse the Donation Protection Act or the Act enhances consummation rates for Chapter 13 debtors who tithe or budget for charitable contributions. Scholars need to conduct additional research to identify the causes of variability in tithing and use of Chapter 13.

III. OTHER EFFECTS OF ENACTMENT

Prior to enactment of the Donation Protection Act, commentators and congressional witnesses had identified problems that the bill would create or had failed to address.[130] Congress addressed some of these problems but

[130] *See, e.g., supra* note 20, testimony on behalf of National Bankruptcy Conference.

ignored others. Some unanticipated problems emerged after enactment of the Act, and additional problems may yet develop as a result of its enactment. Speedy passage of the Act to accommodate the religious right has caused and may yet cause side effects.

A. Less credit for Religious Borrowers?

Before passage of the Donation Protection Act, one commentator speculated that "protecting religious contributions in Chapter 13 would achieve an undesirable result: less consumer credit available for religious borrowers."[131] This hypothesis is based on law and economics theory that "rational creditors in an efficient credit market . . . will adjust their credit practices for those applicants who are perceived more likely to make religious contributions."[132]

Despite this theory, it is doubtful that consumer creditors, who market on a volume basis, would adjust their practices at all to account for borrowers who make religious contributions and might file for Chapter 13, particularly when those borrowers comprise a small percentage of overall borrowers.[133] The costs of obtaining information about a

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[131]Leonard J. Long, *Religious Exercise as Credit Risk*, 10 Bankr. Dev. J. 119, 129 (1993/1994).

[132]*See id. See also* Mary Jo Newborn Wiggins, *A Statute of Disbelief?: Clashing Ethical Imperatives in Fraudulent Transfer Law*, 48 S.C. L. Rev. 771, 787 (1997) ("[S]ome creditors can protect themselves, to a certain extent, by asking questions about their debtor's giving habits prior to making loans.").

[133]Absent data showing that solvent tithing consumers are more likely to repay their debts than nontithing consumers, any adjustment is likely to decrease credit extension to tithing consumers with a smaller decrease to tithing consumers who reside in the South. *See supra* Part II.C. (analyzing data showing that consumer-debtors in the South have a higher propensity to file debt repayment plans under Chapter 13 than to file a liquidation case under Chapter 7). On average, creditors recover more in Chapter 13 cases than in Chapter 7 cases. *See* 11 U.S.C. § 1325(a)(4) (1994) (requiring unsecured creditors to receive at least as much under a Chapter 13 plan as they would in a Chapter 7 case).

borrower's religious proclivities could well exceed the benefit from obtaining the information. Moreover, although information regarding a borrower's religious contributions is correlated with a borrower's propensity to tithe, it may not be predictive of whether the borrower will become insolvent or tithe abusively. Furthermore, some borrowers could regard a lender's request for religious information as intrusive, leading them to borrow from lenders who do not request this information. To gain competitive advantage by avoiding adverse publicity and offending religious customers, lenders might consciously decide not to request religious information from borrowers. In the author's experience, when consumer creditors decide whether to extend credit, they do not ask borrowers for religious contribution data.

Even if the Donation Protection Act does not affect the cost of consumer credit, it should give rise to some unintended consequences and the intended consequences might open the door to abuse of the bankruptcy system.

B. Abuse of the Bankruptcy system

The Donation Protection Act protects tithes in two fundamental ways. First, it limits the trustee's ability to pursue charities and churches to return prepetition constructive fraudulent transfers. Second, it permits a Chapter 13 debtor to tithe under a Chapter 13 plan. Each method of protection encourages debtor abuse that can undermine the integrity of the consumer bankruptcy system.

Under the Donation Protection Act, the trustee will not be able to recover most constructive fraudulent transfers from charities and churches. With more than a million households filing for bankruptcy each year, it is only a matter of time before some debtors will contribute large sums of money to charities and churches on the eve of filing for bankruptcy protection. Some will do so in ignorance of the Donation Protection Act, and others will do so after consultation with their attorneys. In either event, where the contributions constitute large sums of money, the return to creditors will be sharply eroded and the consumer bankruptcy system will less effectively further its goals.[134]

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[134]Courts recognize that the Bankruptcy Code's goals include providing debtors with a fresh start while protecting creditors. *See, e.g.,* Christians v. Crystal Evangelical Free Church (*In re* Young), 82 F.3d 1407, 1420 (8th Cir. 1996),

vacated by 521 U.S. 1114 (1997), *remanded to* 141 F.3d 854 (8th Cir. 1998) (reinstating 82 F.3d 1407).

Likewise, the observant Chapter 13 debtor may insist on tithing fifteen percent of her *gross* annual income,[135] although it may constitute the lion's share or all of her disposable income.[136] As a result, unsecured creditors may receive little or nothing under a Chapter 13 plan. The resulting creditor disappointment could erode support of the consumer bankruptcy system much the way it was eroded between 1979 and 1984 when so-called zero plans[137] were permitted in some circuits before Congress imposed a disposable income test.[138]

C. VULNERABLE PLEDGES

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[135]On average, outside of bankruptcy, tithe-payers give 2.1% of gross income: Virginia Hodgkinson & Murray Weitzman, Independent Sector, Giving & Volunteering in the U.S., Findings from a National Survey (1999 ed.) *at* HTTP://www.independentsector.org/GrandV/default.html (last visited Nov. 14, 2000). Indeed, the tithing rate for Mormons who tithe averages only seven percent of gross income. *See* DEAN HOGE ET AL., MONEY MATTERS–PERSONAL GIVING IN AMERICAN CHURCHES 12 (1996).

[136]Most of a Chapter 13 debtor's gross income is spent on living expenses. *See* NAT'L BANKRUPTCY R. COMM'N, BANKRUPTCY: THE NEXT TWENTY YEARS 266 (1997) (stating that a Chapter 13 debtor with good legal advice will list high enough expenses to leave no disposable income).

[137]A "zero plan" is a Chapter 13 plan in which secured creditors are paid something, but unsecured creditors are paid nothing. *See, e.g., In re* Sadler, 3 B.R. 536 (Bankr. E.D. Ark. 1980); 8 COLLIER ON BANKRUPTCY ¶ 1325.08[1] (Lawrence P. King ed., 15th ed. rev. 1996).

[138]*See* Conrad K. Cyr, *The Chapter 13 "Good Faith" Tempest: An Analysis and Proposal For Change*, 55 AM. BANKR. L.J. 271, 279 (1981) (stating that courts' predisposable income test efforts to derive a minimum payment standard from the former "good faith" standard were fueled by perceived "distressing abuses of the liberal debtor relief provisions of the Bankruptcy Code"); Paul M. Black & Michael J. Herbert, *Bankcard's Revenge: A Critique of the 1984 Consumer Credit Amendments to the Bankruptcy Code*, 19 U. RICH. L. REV. 845, 845-51 (1985); Irving A. Breitowitz, *New Developments in Consumer Bankruptcies: Chapter 7 Dismissal on the Basis of "Substantial Abuse*," 51 AM. BANKR. L.J. 327, 327-44 (1985).

Although the Donation Protection Act is amply drawn to prevent the trustee from recovering most fraudulent transfers of money or property, it appears that Congress overlooked the trustee's ability to attack the debtor's incurrence of pledges as fraudulent transfers or payment of pledges as avoidable preferences. On its face, the Donation Protection Act does not preclude the trustee from attacking pledges that are valid debts under nonbankruptcy law.[139] Trustees might attempt two lines of attack. First, existing fraudulent transfer law permits avoidance of fraudulently incurred *obligations*.[140] To the extent the debtor made a religious or charitable pledge while the debtor was insolvent, the trustee might still be

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[139]Whether a pledge to make a charitable donation is an enforceable debt under nonbankruptcy law depends on state contract law and particularly on the treatment of consideration. Some states require that classic contractual consideration (or a substitute such as promissory estoppel) is necessary before a pledge to make a charitable donation will be considered a legally enforceable debt. *See, e.g.,* Arrowsmith v. Mercantile-Safe Deposit & Trust Co., 545 A.2d 674 (Md. 1988); *In re* I&I Holding Corp. v. Gainsburg, 12 N.E.2d 532 (N.Y. 1938) (under New York law charitable pledge supported by consideration of the promises of others); Keuka College v. Ray, 100, 60 N.E. 325 (N.Y. 1901) (under New York law promissory estoppel substitutes charity's detrimental reliance for consideration). Other states maintain that enforceability hinges on consideration yet strain the definition of consideration in holding pledges enforceable. *See, e.g.,* Dillard Univ. v. Local Union 1419, Int'l Longshoremen's Ass'n, 144 So.2d 710 (La. Ct. App. 1962) (stating that "the intention to confer a benefit" is a sufficient consideration); Hirsch v. Hirsch, 289 N.E.2d 386, 390 (Ohio Ct. App. 1972) (stating that consideration consisted of "the accomplishment of the purposes for which [the charitable] institution or organization was organized and created"). Several states reject the consideration requirement and hold pledges enforceable as a matter of public policy. *See, e.g.,* Salsbury v. Northwestern Bell Tele. Co., 221 N.W.2d 609 (Iowa 1974); Jewish Fed'n v. Barondess, 560 A.2d 1353 (N.J. Super. Ct. Law Div. 1989). *See generally* Pollack, *supra* note 1, at 574-75 (citing *In re* 375 Park Ave. Assocs., Inc., 182 B.R. 690, 692-93 (Bankr. S.D.N.Y. 1995)).

[140]*See* 11 U.S.C. 548(a)(1) (Supp. IV 1998) (permitting avoidance of transfers or obligations).

able to avoid the pledge as a constructively fraudulently incurred obligation unless it was made too long before bankruptcy.[141] But the trustee will lose if the debtor was solvent[142] when he made the pledge or the trustee cannot prove insolvency. Second, preference law permits the trustee to recover payment of the pledge from the donee if it was made within ninety days of bankruptcy while the debtor is insolvent.[143]

D. Pitfalls for Debtors and Their Attorneys

Certain tests prescribed by the Donation Protection Act

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[141]Fraudulent transfer statutes limit a creditor's or trustee's ability to reach back to attack transfers. For example, under § 548 of the Bankruptcy Code, the trustee is limited to attacking transfers that were made within the year before the date of the filing of the debtor's bankruptcy petition. *See* 11 U.S.C. § 548(a) (Supp. IV 1998). Section 544(b) of the Bankruptcy Code gives the trustee the power to avoid transfers that are avoidable under nonbankruptcy law by actual unsecured creditors. *See* 11 U.S.C. § 544(b) (Supp. IV 1998). These nonbankruptcy laws vary in their reach back period, but the period can be many years. *See, e.g.*, UFTA § 9 (fixing four-year reach back period for most kinds of transfers); Cal. Civ. Code § 3439.09 (West 2000) (same).

[142]The trustee may only avoid a constructive fraudulent transfer by proving that the transfer was made while the debtor was insolvent or rendered insolvent or that the debtor intended to incur debts beyond his or her ability to repay. *See supra* note 32.

[143]*See* 11 U.S.C. § 547(b) (1994). Generally speaking, the trustee may avoid a transfer as a preference if it involves property of the debtor; is made to or for the benefit of an unsecured or undersecured creditor; is made for or on account of an antecedent debt, within ninety days before bankruptcy; and is made while the debtor was insolvent. *See id.* Courts have held a pledge to be a debt since it is a legally enforceable obligation made in consideration of the promises of others. *See, e.g.*, *In re* Morton Shoe Co., Inc., 40 B.R. 948, 951 (Bankr. D. Mass. 1984). *See generally*, Russell G. Donaldson, Annotation, *Lack of Consideration as Barring Enforcement of Promise to Make Charitable Contribution or Subscription—Modern Cases*, 86 A.L.R.4th 241 (1991).

are sufficiently vague and at war with the policies underlying the logic of the Bankruptcy Code that debtors and their attorneys need to proceed with caution in utilizing these new provisions. Aggressive use of the Donation Protection Act can lead to denial of Chapter 13 plan confirmation, dismissal of the case, loss of discharge, and criminal penalties for debtors, as well as malpractice and other liabilities for debtors' attorneys.

1. *Denial of Chapter 13 Plan Confirmation*

If a debtor proposes a Chapter 13 plan increasing the amount of future tithes compared to the debtor's prepetition history, the court could deny confirmation on two grounds. First, the court could deny confirmation on the ground that the plan does not devote all "disposable" income to payments under the plan.[144] Despite the suggestion in § 1325(b)(2)(A)[145] that debtors have an absolute right to tithe up to fifteen percent of their gross annual income, the court could examine the "necessity" of the payment.[146] On the other hand, a court might read § 1325(b)(2)(A) literally and adopt an objective test that permits confirmation of plans in which tithes do not exceed fifteen percent of the debtor's gross income.[147] These differing approaches to § 1325(b)(2))(A) could result in the inconsistent administration of justice between districts and even within districts with more than one judge. Second, courts could deny confirmation if a plan is not proposed in good faith.[148] Whether or not the court permits the debtor's tithes to reduce disposable income, the court could deny confirmation if the facts and circumstances of the tithing indicate that the debtor is not acting in good faith.[149]

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[144]*See In re* Buxton, 228 B.R. 606, 611 (Bankr. W.D. La. 1999).

[145]11 U.S.C. § 1325(b)(2)(A) (Supp. IV 1998).

[146]*See In re* Buxton, 228 B.R. at 611.

[147]*See* Drummond v. Cavanagh (*In re* Cavanagh), 250 B.R. 107 (B.A.P. 9th Cir. 2000).

[148]The statute requires the court to determine whether the plan is proposed in good faith. *See* 11 U.S.C. § 1325(a)(3) (1994).

[149]*See In re* Cavanagh, 250 B.R. 107 (debtor provided ample testimony that he had acted in good faith); *In re* Buxton, 228

2. *Dismissal of the Case or Loss of Discharge*

B.R. at 611 (level of charitable contributions is so high postpetition compared with debtor's prepetition contributions as to suggest a lack of good faith).

The Donation Protection Act still leaves trustees and creditors with substantial opportunities for challenging a debtor's prepetition transfers, especially last minute transfers that appear to be made to avoid paying creditors. The temptation offered by the Donation Protection Act to debtors to make contributions on the eve of filing for bankruptcy might prove to be great in rare cases where debtors have cash or other property that they cannot exempt.[150] Debtors' attorneys will be asked whether the debtor may tithe or make charitable gifts.[151] Attorneys are required to zealously represent their clients,[152] but there are risks. As noted above, because the Donation Protection Act restricts or eliminates the trustee's ability to attack donations as constructive fraudulent transfers, the trustee may attack the charitable donation as an actual intent fraudulent transfer.[153] If creditors or the trustee consider the charitable donation to be offensive, they may sue to deny the debtor's discharge or to dismiss the case as a bad faith filing.[154] Likewise, the Chapter 7 debtor's discharge can be denied if the charitable

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[150]Case law is split whether debtors may convert nonexempt property into exempt property on the eve of bankruptcy. *Compare, e.g.,* Hanson v. First Nat'l Bank in Brookings, 848 F.2d 866 (8th Cir. 1988) *with, e.g.,* Norwest Bank Neb., N.A. v. Tveten, 848 F.2d 871 (8th Cir. 1988).

[151]*See In re* Cavanagh, 242 B.R. 707, 711-12 (Bankr. D. Mont. 2000), *aff'd*, 250 B.R. 107 (B.A.P. 9th Cir. 2000); Lebovits v. Chase Manhattan Bank (*In re* Lebovits), 223 B.R. 265, 273 (Bankr. E.D.N.Y. 1998).

[152]*See* MODEL RULES OF PROF'L CONDUCT R. 1.7.

[153]*See supra* note 44; 11 U.S.C. § 548(a)(1)(A) (Supp. IV 1998).

[154]*See In re* Smihula, 234 B.R. 240, 243 (Bankr. D.R.I. 1999). Chapter 7 contains express authorization for bankruptcy judges to dismiss cases that are filed in bad faith. *See* 11 U.S.C. § 707(b) (Supp. IV 1998). And courts have found the same concept imbedded in the more general dismissal "for cause" provisions of Chapters 11 and 13. *See* 11 U.S.C. §§ 1112(b) & 1307(c) (1994). *See, e.g., In re* Casse, 198 F.3d 327 (2d Cir. 1999) (Chapter 13 case); *In re* Penny, 243 B.R. 720 (Bankr. W.D. Ark. 2000) (same); *In re* Pacific Rim Invs., LLP, 243 B.R. 768 (D. Colo. 2000) (Chapter 11 case); *In re* Hammersmith Trust, LLC, 243 B.R. 795 (Bankr. M.D. Fla. 1999) (same).

donation or tithe is found to be an actual intent fraudulent transfer or the debtor fails to provide specific details about the contributions.[155] In this regard, the debtor's actual fraudulent intent can be inferred even in the absence of a misrepresentation.[156]

3. *Criminal Penalties*

Technically, a debtor who makes a charitable donation or religious tithe on the eve of bankruptcy could be subject to federal or state criminal prosecution. For example, federal law permits criminal prosecution of a person who files a bankruptcy case for the purpose of executing a scheme to defraud[157] or who fraudulently transfers property in contemplation of filing a bankruptcy case.[158] And some state laws likewise permit criminal prosecution of debtors who make or defend actual intent fraudulent transfers, even if the debtor's intent is only to hinder or delay creditors rather than defraud them.[159]

Whether a prosecutor would exercise discretion to prosecute a debtor is open to speculation. But the Donation Protection Act will result in more successful fraudulent transfer civil actions against debtors the notoriety of which will expose them to increased risks of prosecution.

Thus, although Congress sought to protect debtors' religious freedoms, in theory it might actually have set the stage to increase the risk of debtors' prosecution.

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[155]Sections 727(a)(2) & (5) are possible grounds of attack. *See* 11 U.S.C. § 727(a)(2) & (5) (1994). It is unclear whether RFRA limits the disclosure requirements of Bankruptcy Code §§ 521(1) and 727(a)(5). *See supra* note 25 and accompanying text.

[156]*See* McClellan v. Cantrell, 217 F.3d 890 (7th Cir. 2000) (finding actual fraud for purposes of nondischargeability under § 523 of Bankruptcy Code even in absence of deliberate misrepresentation or misleading omission).

[157]*See* 18 U.S.C. § 157(1) (1994).

[158]*See* 18 U.S.C. § 152(7) (1994).

[159]*See, e.g.*, CAL. PENAL CODE § 531 (West 2000).

4. *Malpractice and Other Risks for the Debtor's Attorney*

If the debtor loses her discharge on account of advice of counsel to make a "fraudulent" prepetition charitable donation or tithe, the debtor[160] or trustee could sue the debtor's lawyer for malpractice. A lawyer who counsels a client to make a fraudulent transfer might violate the applicable Code of Professional Conduct.[161] Courts in some jurisdictions have held that a lawyer who violates the applicable Code of Professional Conduct performs below the standard of care.[162]

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[160]Unless exempted or abandoned from property of the estate, the malpractice cause of action would be property of the estate prosecutable by a Chapter 7 trustee or Chapter 13 debtor. *See, e.g.,* Johnson, Blakely, Pope, Bokor, Ruppel & Burns, P.A. v. Alvarez (*In re* Alvarez), 224 F.3d 1273, 1275 (11th Cir. 2000), *cert. denied*, 121 S. Ct. 1083 (2001); Alipour v. Thomas (*In re* Alipour), 252 B.R. 230, 235 (Bankr. M.D. Fla. 2000).

[161]*See, e.g.*, CAL. RULE OF PROF'L CONDUCT R. 3-210--Advising the Violation of Law ("A member shall not advise the violation of any law, rule, or ruling of a tribunal unless the member believes in good faith that such law, rule, or ruling is invalid.") and CAL. PENAL CODE § 531 (West 2000).

[162]*See, e.g.,* Baxt v. Liloia, 656 A.2d 835 (N.J. Super. Ct. App. Div. 1995) (stating that in New Jersey "the Rules of Professional Conduct set forth an appropriate standard of care by which to measure an attorney's conduct."), *remanded by* 663 A.2d 1353 (N.J. 1995), *remanded to* 664 A.2d 948 (N.J. Super. Ct. App. Div. 1995), *aff'd as modified by* 714 A.2d 271 (N.J. 1998). In other states, the Rules of Professional Conduct are limited to lawyer discipline and violations do not appear to create civil liability. *See, e.g.*, MD. RULES OF PROF'L CONDUCT, Preamble ("Violation of a Rule should not give rise to a cause of action nor should it create any presumption that a legal duty has been breached. The Rules are designed to provide guidance to lawyers and to provide a structure for regulating conduct through disciplinary agencies. They are not designed

Therefore one unintended consequence of the Donation Protection Act could be occasional additional malpractice actions against debtors' attorneys.

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to be a basis for civil liability."). Nevertheless, the United States District Court for the District of Maryland has applied Maryland Rules of Professional Conduct outside the disciplinary context in disqualifying counsel in collateral litigation. *See* Buckley v. Airshield Corp., 908 F. Supp. 299 (D. Md. 1995); Blumenthal Power Co. v. Browning-Ferris, Inc., 903 F. Supp. 901 (D. Md. 1995); Gaumer v. McDaniel, 811 F. Supp. 1113 (D. Md. 1991), *cited with approval in* Post v. Bregman, 707 A.2d 806, 817 (Md. 1998), *aff'd,* No. 93-1126, 1994 WL 177283 (4th Cir. 1994) (unpublished).

There also may be consequences for the attorney who counsels a fraudulent transfer or a criminal act. In some states, an attorney who provides counsel or participates in a scheme to defraud creditors may be subject to civil liability,[163] discipline,[164] and perhaps disbarment.[165] It is even possible that the attorney may be committing a crime by aiding and abetting a fraudulent transfer.[166] In other states, however, the attorney will not be criminally liable[167] or subject to civil liability[168] unless the attorney personally

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[163]*See* McElhanon v. Hing, 728 P.2d 256, 264 (Ariz. Ct. App. 1985), *aff'd in part, vacated in part*, 728 P.2d 273 (Ariz. 1986) (court finds attorney to be conspirator holding that the privilege protecting an attorney from civil liability for acts in representing a client does not extend to "the intentional acts of furthering and participating in a fraudulent conveyance").

[164]*See, e.g.*, Yokozeki v. State Bar, 11 Cal. 3d 436, 445 n.4 (1974) (lawyer's holding property in client trust account for the purpose of hindering creditors constitutes participation in a scheme to defraud creditors "which is a crime and a proper subject for disciplinary action") (citation omitted). *Accord* Townsend v. State Bar, 197 P.2d 326 (Cal. 1948) (lawyer disciplined with three-year suspension for counseling his client to deliver property deed to her mother before judgment could be recorded).

[165]*See, e.g.,* Allen v. State Bar, 20 Cal.3d 172, 178 n.1 (1977) (attorney who set up fraudulent stock purchases and perjured himself at his deposition was disbarred for participating in a scheme to defraud which "is a crime and properly subjects an attorney to disciplinary actions").

[166]*See* CAL. PENAL CODE § 531 (West 2000). *Cf. Allen*, 20 Cal. 3d at 178 (attorney who set up fraudulent stock purchases and perjured himself at his deposition participated in a scheme to defraud which "is a crime").

[167]*See* Fraidin v. Weitzman, 611 A.2d 1046, 1080 (Md. Ct. Spec. App. 1992) (holding that "there can be no conspiracy where an attorney's advice or advocacy is for the benefit of the client and not for the attorney's sole personal benefit" but noting that "an attorney who has actual knowledge that his client is engaged in unlawful activity may not aid, assist or encourage the carrying on of that unlawful activity").

[168]*See* Thomson Kernaghan & Co. v. Global Intellicom, Inc., No.

benefits from the transaction.[169]

CONCLUSION

The Donation Protection Act intended to restore and has been effective in restoring the *de facto status quo ante* 1980 by granting charities and religious institutions *de jure* immunity to most constructive fraudulent transfer attacks. Certain theoretical concerns that could emerge have not emerged to date in the data or reported decisions. For example, the Donation Protection Act makes little difference in actual case administration.

By hastily responding to religious group pressure, however, Congress fixed a problem with respect to disgorgement of donations at the expense of creating systemic consequences. The data reveal a meaningful number of cases in which debtors make charitable contributions or tithes. Moreover, it is inevitable that the Donation Protection Act will enable a few wealthy debtors to make large contributions or tithes that

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99 Civ. 3005 (DLC), 1999 WL 717250, *1 (S.D.N.Y. Sept. 14, 1999) (granting a motion to dismiss a fraudulent conveyance action against an attorney who "is alleged to have participated . . . 'in the formulation of the plan' to make the transfer," involving complete asset stripping, which was allegedly "a fraudulent conveyance because either it was made with actual intent to defraud or because [the transferor] was insolvent at the time of the transfer and did not receive reasonably equivalent value"); Foufas v. Leventhal, No. 94 Civ. 7924 (NRB), 1995 WL 332020, *2 (S.D.N.Y. June 5, 1995) ("New York courts recognize no cause of action against a person . . . who was neither a transferee nor a beneficiary of an allegedly fraudulent transfer."); Geren v. Quantum Chem. Corp., 832 F. Supp. 728, 736 (S.D.N.Y. 1993) ("the action for fraudulent conveyance does not create an independent remedy of money damages against third parties who aided the debtor's transfer"). *Cf.* Kartiganer Assocs. P.C. v. New Windsor, 485 N.Y.S.2d 782, 783-84 (N.Y. App. Div. 1985) (attorney not liable for inducing client to breach contract with another if attorney acts on client's behalf and within scope of authority).

[169] *See* Thomson Kernaghan & Co., 1999 WL 717250, *5 (no fraudulent transfer action can be maintained against a lawyer who participates in a transaction unless he is a transferee).

will reduce distributions to creditors. Furthermore, the data reveal that the Donation Protection Act applies with regional variability that evidences nonuniform application of United States bankruptcy laws and differences in tithing practices. Of greater significance, the Act might have the unintended consequence of resulting in the completion of more Chapter 13 plans due to a built-in budgetary cushion for authorized charitable and religious donations. In fact, once debtors' lawyers become aware of the predictable correlation between success and tithing, even more debtors should provide for charitable donations or tithes in their Chapter 13 budgets.

On balance, although the Donation Protection Act has the virtue of letting people tithe as part of their religion, it does so at the possible cost of undermining the integrity of the bankruptcy system. Time will tell whether abuse of the bankruptcy system will grow as debtors and their lawyers become more familiar with the Donation Protection Act. Only then will the costs and benefits of the Act be apparent.

Appendix

This Appendix examines the data for sampling errors and appends exemplars of the questionnaires with aggregate numerical results. Although the reported cases are not drawn from a random sample, there is no reason to suspect that any sampling bias would affect the reliability of the results. There is no evidence to suggest that responses to the questionnaire were self-selected based on volume of caseload, attitudes toward tithing, or regional factors. The author mailed the questionnaire to all Chapter 13 trustees, and the percentages of trustees responding and cases represented in the data are substantial. More than thirty-seven percent of the Chapter 13 trustees completed and returned the questionnaire. Seventy-five Chapter 13 trustees (out of 198 solicited) returned completed questionnaires, which were received by the author between June 21 and October 2000. Seventy of the questionnaires provided usable data. One trustee sent a letter stating she was appointed July 1, 2000 and had not yet been assigned any cases. As noted in the text, the response rate for Chapter 7 trustees was lower than for Chapter 13 trustees. Approximately 16.4% of the Chapter 7 panel trustees completed and returned the questionnaire, about half the response rate of the Chapter 13 trustees. This raises the question whether the response rates undermine the vitality of the data for Chapter 7 cases or both Chapter 7 and Chapter 13 cases.

Commentators often consider a return to a mail-in survey over thirty percent to be a meaningful response rate.[170] Although it is difficult to test whether and how much error is introduced by response rates, there is some evidence that low (40%) response rates are not problematic in public opinion surveys. In order to probe for bias in the results, it is possible to split the sample into two halves, high- and low-response states, based on the percentage of known bankruptcy cases in each state that the respondents reported. The hypothesis is that high-response states will provide a more accurate picture of the incidence of tithing-related cases.

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[170] *See* The Pew Research Center For The People & The Press, March 27, 1998, *Opinion Poll Experiment Reveals Conservative Opinions Not Underestimated, But Racial Hostility Missed*, *available at* http://www.people-press.org/resprpt.htm (last visited Oct. 19, 2000).

The results suggest that response rates do not present a serious problem for either Chapter 13 or Chapter 7 bankruptcy cases. The donation or tithing rate for Chapter 13 cases was nineteen percent for high-response states and twenty-four percent for low-response states. The difference is statistically significant (chi-square = 742, $p < .001$) but not enough of a difference to be substantively important for the purposes of this research. From a policy standpoint, the data do not reflect large differences in tithing based on response rates. The Chapter 13 difference between an eighteen percent and twenty-two percent tithing rate might not be random, but it is of little consequence in assessing the impact of the Act.

For Chapter 7 cases the difference is even smaller, eleven percent for high-response states and twelve percent for low-response states. This difference, too, is statistically significant (chi-square=23, $p < .001$) but the difference is substantively irrelevant.

Chapter 13 Trustee Questionnaire

Please complete and return to Prof. Klee by mail at P.O. Box 951476, Los Angeles, CA 90095-1476, by Fax to 310-206-7902, or by email to klee@law.ucla.edu
If you don't have specific data, please estimate your answers.

Religious Liberty and Charitable Donation Protection Act
Questionnaire for Professor Klee
Summer 2000

1. Your Name _____. Today's Date: _____.
2. The District(s) in which you serve as a Chapter 13 trustee _____.
3. Please state the number of chapter 13 cases in which you served as trustee that were **filed after June 18, 1998**? 254,086.
4. Please state the **number** of chapter 13 cases in which you served as trustee that were **filed after June 18, 1998** --
   (a) that involved charitable donations or tithes. 47,146.
   (b) that did **not** involve charitable donations or tithes. 162,353.
   (c) where **confirmation** of a chapter 13 plan was **denied** due in whole or in part to the debtor's charitable donations or tithes. 109.
   (d) that were **dismissed** due in whole or in part to the debtor's charitable donations or tithes. 60.
   (e) where the case was **converted** due in whole or in part to the debtor's charitable donations or tithes. 16.
   (f) where a chapter 13 **plan** was **amended or modified** due in whole or in part to the debtor's charitable donations or tithes. 799.
5. With respect to the chapter 13 cases **filed after June 18, 1998** in which you served as trustee, the Religious Liberty and Charitable Donation Protection Act **decreased** the amount that would have been distributed to creditors compared to what they would have received had the Chapter 13 plan been **confirmed under the previous law** in 10,268 cases.
6. Please state below or on a separate page any other views you have about The Religious Liberty and Charitable Donation Protection Act or any aspect of its enforcement in bankruptcy cases and proceedings.

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Chapter 7 Trustee Questionnaire

Please complete and return to Prof. Klee by mail at P.O. Box 951476, Los Angeles, CA 90095-1476, by Fax to 310-206-7902, or by email to klee@law.ucla.edu

If you don't have specific data, please estimate your answers.
Religious Liberty and Charitable Donation Protection Act
Ch. 7 Questionnaire for Professor Klee

Summer 2000

1. Your Name _____. Today's Date: _____.
2. The District(s) in which you serve as a Chapter 7 trustee _____.
3. Please state the number of chapter 7 cases in which you served as trustee that were **filed after June 18, 1998**? 297,306.
4. Please state the **number** of chapter 7 cases in which you served as trustee that were **filed after June 18, 1998** --
   (a) that involved charitable donations or tithes. 29,155.
   (b) that did **not** involve charitable donations or tithes. 220,400.
   (c) where **an avoiding power** cause of action (section 522, 543, 544, 547, 548, 549, 550, 551, or 553) was brought based on charitable donations or tithes, 11 or a pledge relating to the same.1.
   (d) that were **dismissed under section 707(b)** due in whole or in part to the debtor's charitable donations or tithes. 4.
   (e) where the case was **converted** due in whole or in part to the debtor's charitable donations or tithes. 24.
   (f) that were **dismissed other than under section 707(b)** due in whole or in part to the debtor's charitable donations or tithes 22.
   (g) where the debtor's **discharge was denied** due in whole or in part to the debtor's charitable donations or tithes. 0.
   (h) where a debt was held to be **nondischargeable** due in whole or in part to the debtor's charitable donations or tithes. 0.
5. With respect to the chapter 7 cases **filed after June 18, 1998** in which you served as trustee, the Religious Liberty and Charitable Donation Protection Act **decreased** the amount that would have been distributed to creditors compared to what they would have received had the Chapter 7 case been

filed **under the previous law** in 1,593 cases.

6. Please state below or on a separate page any other views you have about The Religious Liberty and Charitable Donation Protection Act or any aspect of its enforcement in bankruptcy cases and proceedings.

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