

## AFTER CHAPTER 11

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Today's symposium has been a wonderful discussion of the legal implications of some Roman Catholic dioceses' decisions to enter into Chapter 11. We have had very helpful consideration of the good faith issue, contrasting the implications of the earlier mass tort bankruptcies and the more restrictive approach under *Carbon*; the difficult issues of determining who owns what for purposes of establishing the bankrupt estate when both the diocese and individual parishes have claims of some kind on the assets, and the enforceability of possibly fraudulent or preferential transfers of assets to parishes; the extent to which the civil law will take into account or defer to canon law; and the possible restraints under the First Amendment and RFRA on the supervision of the bishop and diocese during reorganization.

For the most part, however, we have not focused on the meanings of bankruptcy for the diocese as an institution and a spiritual/moral entity, other than to agree, as indeed we should, that legal bankruptcy should not lead to moral bankruptcy. We agree that Chapter 11 should not be used to evade moral and legal responsibilities to victims of sexual abuse, but should be a mechanism for the fair and orderly disposition of all legitimate claims while preserving the diocese as a going concern. Chapter 11, in other words, can and should be a mechanism for accountability, not irresponsibility. But what are the broader implications for the Church of having to go through all this — of experiencing what once seemed unthinkable? What will be

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the consequences for the governance of dioceses after Chapter 11? We haven't spent a lot of time talking about that. Of course, that makes sense – we are a group of lawyers and law professors – and not ecclesiologists – theologians whose area of expertise is the nature of the Church. My own training in corporate and securities law certainly did not include ecclesiology, although as the Dean of the Villanova Law School I do spend a lot of time thinking about the nature of a Catholic law school. But the absence of theological training aside, it is appropriate for us to spend some time thinking broadly about what comes after Chapter 11 for the Church. To do so would be consistent with a growing tendency among Catholic lay people, particularly Catholic professionals, to consider what the fallout of the sexual abuse crisis – including the diocesan bankruptcies – should mean for the organization and administration of our dioceses.

Now, it may seem highly presumptuous for us to think or talk about lay participation in Church governance. After all, the Church is organized around the principle of apostolic succession. Bishops are not just managers. They are not accountable to congregations in the way pastors are in the Protestant tradition. They carry unique moral and spiritual authority, and have an ancient juridical status within canon law. While the People of God includes all of us, and not just the hierarchy, as laity our authority in the Church is limited, and not just with respect to doctrinal matters or sacramental functions. Our role in governance of dioceses and parishes has always been highly circumscribed, and much less significant than our role in Catholic hospitals, schools, colleges and universities, where, since the 1960's, lay leaders have replaced or at least complemented clerical leadership. The sense of dismay, alienation and urgency generated by the recent scandals, however, has begun to overcome inhibitions that lay Catholics feel about making a greater claim to authority in Church governance, and the diocesan bankruptcies have certainly created even greater impetus for lay intervention.

What is missing, however, has been a conceptual and practical framework for diagnosing the governance problems and proposing solutions that include a greater role for the laity. Not that there have not been efforts. Last spring the American Church got the Wharton School treatment at a two-day conference organized by prominent Catholic lay people, with speakers including professional management consultants, business school professors and a host of other specialists, most of whom were convinced that an extreme makeover using the tools of modern American managerialism was not only possible, but the key to the survival of the American Church. We heard about the advantages of modern marketing techniques, strategic planning, human resource management, and collaborative decisionmaking processes. I must confess to a bit of skepticism about all this, despite the can-do virtues of the approach, believing that churches grow and flourish primarily through spiritual and moral renewal, and not managerial renewal, but it was still a useful conversation. While reserving judgment about the usefulness of B-school theorizing as a conceptual and practical framework for lay participation in church governance, I would like to turn to an alternative model of governance – that of corporate law – to see whether it offers anything that may be of help.

I began to think of this linkage a couple of years ago through a coincidence of scandals which led to me getting a lot of phone calls from reporters. As someone who writes on corporate and securities matters, I began to get calls from reporters after Enron and its successors became big news. At about the same time, I got calls from reporters who seemed to think that the dean of a Catholic law school would have a lot to say about the sexual abuse problems (I tried not to, at least in the press). In any event, this confluence got me thinking about what, if anything, the two scandals had in common.

We can begin with the common thread of managerial failure: that of CEO's, CFO's,

general counsels, other senior executive officers and boards in the case of the corporations; and that of bishops and their senior officials in the case of the Church. Of course, the reasons for failure were different: primarily greed and self-dealing in the case of corporate managers; self-protective clericalism and astonishing inability to face reality in the case of the Church.

Whatever the source of managerial failure, however, the common problem in both instances was an inability to lead large and complex institutions faithfully and successfully. In addition, both groups shared a particular cognitive failure: over-optimism. Corporate managers believed that accounting shenanigans, economically dubious deals, and conflicts of interest could be obscured by continued increases in the stock price. To some extent they were right; it was primarily when the stock price cratered in down markets that all the nastiness crawled out from under the rocks. Similarly, many bishops believed that a discrete “handling” of problems through confidential settlements, private therapy or pastoral counseling for the offending priest and quiet reassignment would be effective in preventing future problems and avoid scandalizing the laity - a major episcopal concern. Of course they were wrong, and all of it eventually came out, despite the optimistic belief that the situation could be controlled.

One of the premises of corporate law is that managerial failure – whether in the form of ineptitude or self-dealing – can be controlled, or at least minimized by a mix of reliance on market incentives, private contracting, gatekeepers and legal rules such as the principle of fiduciary duty. What was most dismaying about the corporate scandals of the last few years is that none of these protective mechanisms functioned very effectively. Securities markets were distorted by the corruption of analysts, contractual devices such as stock option compensation programs produced perverse incentives, gatekeepers such as auditors were compromised by conflicts of interest, and, most important, the legal concept of fiduciary obligation to the

corporation apparently meant little to the managers who breached their fiduciary duty of loyalty through self-dealing and the independent directors who breached their duty of care by monitoring the managers so ineptly.

The failure of these various means of controlling managerial misfeasance or malfeasance is not encouraging, but at least they do exist, and theoretically can be rebuilt and enhanced, as both Congress and the regulators have been trying to do. Such bulwarks, however, do not really seem to exist in the Church. Bishops do not have boards of directors; they don't really operate in markets (other than the market for promotion within the Church, and perhaps, the market in which religious denominations compete for adherents); and this is by-an-large not the world of contract. To be sure, bishops are constrained by canon law and are accountable at some level to the Holy See, especially on doctrinal matters, but a strong tradition of episcopal independence leaves bishops without any significant supervision in their actual administration of the diocese (which also makes Vatican liability for diocesan obligations unlikely).

What really constrains bishops, therefore, is a moral obligation something like the legal obligation we call fiduciary duty in corporate law. While dioceses do not have shareholders, bishops are entrusted with the care of the faithful and those who benefit from the diocese's missions in education and to the poor and the sick. What we saw in the bishops' handling of the sexual abuse cases was, in effect, a systematic breach of something like fiduciary duty - - a duty to the victims of sexual abuse primarily, but also to the poor and those others dependent on the diocese's financial resources. In that sense, we can say that the bulwark of fiduciary duty failed in the Church context as well as the corporate context.

The consequence of this failure for some American dioceses, of course, is that control of the diocese's assets has been wrested from the bishops' hands through Chapter 11 receivership.

When this happens in the corporate context, the hope is that restructuring of debt, perhaps changes in management personnel, and changes in the business plan will allow the company to reemerge as a going concern. But what are we hoping for when Portland or Tucson emerge from Chapter 11? Should it be a return to business as usual?

As you might suspect, my answer to that question is clearly “no!” I think we should look at Chapter 11 not so much as a gruesome experience in which the state will get its hands on a religious institution, compromising the institution’s ability to make decisions in accordance with its spiritual and moral priorities (although it may also be that), but rather as an opportunity to create a new way of governing the diocese. This reinvention of diocesan governance should serve two goals. First, creation of a governance structure in which episcopal discretion is constrained by greater accountability and transparency in decisionmaking. This is essentially a pragmatic goal. Second, providing a more meaningful role for the People of God, which includes the laity, in the governance of the Church at the diocesan level. This is a theological, or more precisely, ecclesiological goal. Let’s talk about the pragmatic goal.

The pragmatic goal assumes that the bishops’ failures in handling the sexual abuse cases, even when the bishops were well-intentioned, could have been prevented or at least mitigated if the bishops had greater accountability and their decisions more transparency. Does the structure of corporate governance provide a model for achieving those things (not that we should assume that the corporate model offers perfection, as recent events have confirmed)? Here, we need to think of an equivalent to the board of directors, to which the bishop, as a CEO, would report, and to whom he would be in some way accountable. This entity would be different from the various kinds of advisory boards and committees that already exist in many dioceses both in their authority and, presumably, in their independence. There would, however, be an unavoidable

limitation on their authority. It is inconceivable that lay people could hire or fire bishops. The question is thus whether there are intermediate forms of authority - - particularly authority over disposition of diocesan assets, resolution of litigation, the budgeting process and much more - - that a board could exercise in such a way as to constrain episcopal discretion and promote greater information disclosure, at least at the board level. There are some examples around the country of this kind of countervailing intermediate authority, such as diocesan financial councils, although I gather that they are often advisory rather than authoritative, but these examples suggest this is not a pipe dream. The new review boards for handling claims of sexual abuse offer something of a model, in at least one narrow area.

The success of such boards, however, depends on the independence of the “directors,” which is, of course, a classic problem in corporate law. If membership is determined entirely by the bishop, we will have boards of “inside directors:” those trusted to be “safe” or “reliable.” Mechanisms to ensure the independence of diocesan boards thus will have to be developed. This raises the possibility of democratic processes for the selection of members from among and by the faithful, in a manner akin to shareholder election of directors. Insofar as this does not amount to referenda on doctrinal matters, which would undermine the bishops’ teaching authority, and constitutes lay involvement in areas of prudential judgment in which the expertise of faithful laity is both appropriate and needed, it would be a useful means of achieving greater board independence, and hence greater accountability and transparency. Of course, as in corporate law, there is always the question of whether the directors will effectively perform their own fiduciary duty as monitors (“*quis custodiet custodes?*”). There are lots of ways in which directors can fail in that duty, but the diocesan election process may offer a check, by creating an incentive for them to attend to their duties.

This proposal to shift from the model of the “corporation sole,” with the bishop as the only member, to something like the model of an American business corporation also must be evaluated in light of the second, or theological goal - - the fuller integration of the People of God into their church. At this point, however, I will leave that evaluation to the ecclesiologists.