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Make the Bankruptcy Code Humane for Childhood Sexual-Abuse Victims

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The Bankruptcy Code is intended to address financial insolvency and debt restructuring, not to provide justice or compensation for personal injuries and emotional trauma. However, organizations facing large-scale childhood sexual-abuse claims have increasingly been relying on the chapter 11 process to obtain justice.[2]

The legal focus in chapter 11 cases is on the debtor. Left in the wake of these cases are victims[3] of sexual abuse who lose an opportunity to try their case before a jury of their peers because of the Code's automatic-stay provisions. They typically watch their tortfeasor avoid its day of reckoning, and they receive a small fraction of what they are entitled to under state law. As the system now stands, it is bad for the victims and for the public good.

Sexual-abuse bankruptcy cases are a particularly ill fit for the Code for several reasons. First, sexual-abuse cases involve complex legal issues, and the trauma experienced by each victim is specific to them. Unlike an asbestos-driven bankruptcy case, damages must be assessed individually by highly informed experts in the process, but the bankruptcy system lacks the expertise and sensitivity needed to address these issues appropriately. Victims often feel that their experiences are being minimized or overlooked in a process that is primarily focused on the debtor's financial matters and its survival.

Second, there is a strong public policy interest in ensuring that victims of sexual abuse receive fair compensation, and that perpetrators and those that failed to stop them are held accountable. The bankruptcy process, which aims to provide a fresh start for debtors, often conflicts with these public policy goals. Allowing tortfeasors to use chapter 11 as it is currently constituted to reduce their liability for sexual-abuse claims undermines the public's interest in justice and accountability.

Third, the bankruptcy process is often lengthy and stressful, exacerbating the trauma experienced by victims. Victims face challenges in navigating the legal complexities of bankruptcy proceedings, which causes additional confusion, frustration and further traumatization.

Because of these factors, change is needed. While wholesale modifications to the Code should be made, four reforms are promptly needed to remove chapter 11's barriers to the truth, and to create a more just system for the victims of childhood sexual abuse suing the responsible institutions.

Make Victims' Voices Heard

Victims often feel aggrieved because just as their voices are about to be heard in court, bankruptcy is used to silence them once more. The Bankruptcy Code should be amended to permit victims to address the bankruptcy court and bring humanity to an otherwise-sanitized process. The sole purpose of these "victim impact statements" would be to increase engagement and understanding between the bankruptcy court and victims. To encourage candor, and thus enhance the utility of victim impact statements, the information provided through the statements would not be deemed evidence, victims may not be asked questions by any party, and what is said may not be used by any party for any reason in the case or any other case.

Require the Bankruptcy Court to Independently Confirm the Size and Scope of the Property of the Estate

Due to the intersection between Catholic canon law (which typically views diocesan assets separately from parish assets) and secular law (which does not necessarily view such assets separately, depending on organizational structures), significant battles are often fought over what constitutes property of the bankruptcy estate. Likewise, fraudulent-transfer actions are frequently commenced against nondebtor parishes and other charitable trusts wherein diocesan debtors are alleged to have transferred millions of dollars' worth of assets to them to shield those assets from loss in the litigation and subsequent bankruptcy.[4]

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1 Ms. Hamilton is also the author of *God vs. the Gavel: The Perils of Extreme Religious Liberty and Justice Denied: What America Must Do to Protect Its Children.*

2 *See, e.g.*, "Bankruptcy Protection in the Abuse Crisis," BishopAccountability.org, bishop-accountability.org/bankruptcy.htm (listing 40 bankruptcy filings commenced by dioceses within the Catholic Church) (unless otherwise specified, all links in this article were last visited on Sept. 23, 2025); *see also In re Boy Scouts of Am. and Del. BSA LLC*, Case No. 20-10343 (Bankr. D. Del. 2020); *In re USA Gymnastics*, Case No. 18-09108 (Bankr. S.D. Ind. 2018).

3 The term "victims" will be used to refer to the plaintiffs in these cases, rather than "survivors." All are victims under the law, but only some are survivors.

While committees comprised of victims of sexual abuse are equipped to investigate and litigate these issues, the bankruptcy court has an independent duty to ensure that assets and interests are properly included or excluded from the estate. Accordingly, the bankruptcy court should be authorized to engage the services of an independent forensic accountant to review the assets and interests of a debtor, and of any non-debtor that seeks to be released from liability in a proposed reorganization plan.

The first San Diego diocese case established the utility in doing so. In February 2007, the San Diego diocese filed for bankruptcy protection in the wake of 160 sexual-abuse claims asserted against it. After learning that 770 bank accounts held by 98 San Diego parishes had not been included among the diocese's assets, Hon. **Louise DeCarl Adler** twice asked the San Diego diocese to amend and refile its financial disclosure statements. Frustrated with a lack of candor, she appointed an accountant to audit the diocese's books, and ordered a separate trial to determine the ownership of church property.

Judge Adler soon received the auditor's report, which raised serious questions about the ownership of certain property and the diocese's financial statements, and entered an order to show cause as to why the church's bankruptcy case should not be dismissed. The auditor's report and Judge Adler's order meaningfully changed the case and the pace of its outcome. Shortly after these events, U.S. Magistrate Judge Leo Papas presided over closed-door negotiations that resulted in a global settlement of $198.1 million covering 144 of the clergy-abuse cases, spanning from 1938-93. The amount was more than double the diocese's prior and supposedly "final" offer of $95 million.

Expanding § 524(g) of the Bankruptcy Code to Sexual-Abuse Cases

It is well-documented that a large majority of child sex-abuse victims delay disclosure until well into adulthood[5] due to the trauma inflicted and the impacts on psychological and physical health. In a study of Boy Scout victims, more than half came forward after age 50 to reveal their abuse.[6] Delayed disclosure of harm also occurs in asbestos cases, which have a specific and relevant section under chapter 11.

Almost 25 years ago, § 524(g) was added to the Bankruptcy Code to codify a procedure — pioneered by the U.S. Bankruptcy Court for the Southern District of New York in the *Johns-Manville* bankruptcy case — to permit bankrupt companies faced with continuing liabilities because of their use or distribution of asbestos-containing products to resolve both their current and future asbestos-related liabilities. A conventional chapter 11 case addresses only "claims" against the debtor, and it was argued that the rights of individuals who had been exposed to asbestos-containing products, but who had not yet manifested any injury as of the date of the debtor's bankruptcy, were not claims that were subject to the discharge. If the holders of such "demands" could bring suit (*e.g.*, if they developed an asbestos-related disease) against the company that emerged from bankruptcy protection, it would be nearly impossible for a company with asbestos liabilities to reorganize in bankruptcy.

Section 524(g) allows the reorganization plans of such companies to enjoin the holders of such future asbestos demands against the debtors from pursuing the reorganized company. However, the statute requires that a trust be formed to pay such creditors securities issued by the reorganized company. Section 524(g) also imposes procedural protections designed to ensure that the holders of future demands receive the same treatment as current creditors.

Although the Bankruptcy Code does not expressly authorize third-party releases, § 524(g) permits bankruptcy courts to grant such protection to certain categories of third parties that might be held derivatively liable for the conduct or claims against the debtor, such as those that might be held liable on a veil-piercing theory of liability. Section 524(g)(4) authorizes the bankruptcy court to include such entities within the channeling injunction, as long as the bankruptcy court concludes that the injunction is "fair and equitable" to those who might assert demands subject to the injunction, in light of the third party's contributions to the trust.

Section 524(g)(4) also authorizes third-party releases for the benefit of a debtor's insurer. Where an insurer settles with a debtor before confirmation, § 524(g)(4) permits the insurer to obtain the benefit of the channeling injunction, which protects the insurer from any liability that any person may seek to impose on it that derives from the debtor's liability and results from the insurer's issuance of insurance to the debtor. Since § 524(g)'s enactment, insurers in scores of bankruptcy cases filed by companies with asbestos-related liabilities have settled their coverage disputes with their debtor-insureds, relying on the injunctive protection of § 524(g)(4) to bar all claims against them based on the debtor's asbestos-related liabilities.

The concepts underlying § 524(g) — the appointment of an "unknown claims" representative, the creation of a trust to which claims are channeled and third-party releases — have often been adopted in sexual-abuse bankruptcies, yet there is no statutory language expressly authorizing these mechanisms. Now that the U.S. Supreme Court has held that third-party releases are unlawful as not being expressly authorized by the Bankruptcy Code,[7] the time is particularly ripe to expand § 524(g) to any case in which multiple claims are filed against the debtor arising out of the alleged sexual abuse of a child. Three reasons justify this result.

First, one of the significant advantages of § 524(g) is the establishment of a trust fund to compensate victims. This mechanism ensures that all claimants receive fair and equitable compensation, no matter when they come forward. In sexual-abuse cases, where many victims delay reporting due

4 *See, e.g., Official Comm. of Unsecured Creditors v. Listecki*, No. 13-3495 (7th Cir. 2015) (holding that Religious Freedom Restoration Act did not protect Milwaukee Archdiocese from fraudulent-transfer claims involving transfer of funds into cemetery trust); *Comm. of Tort Litigants v. Cath. Diocese of Spokane*, No. CV-05-0274-JLQ, 2006 WL 211792 (E.D. Wash. Jan. 24, 2006) (finding that tort claimants' committee had standing to challenge debtor's characterization of parish churches', schools' and cemeteries' property); *In re Roman Cath. Bishop of Great Falls, Montana*, 584 B.R. 335 (Bankr. D. Mont. 2018) (same).

5 Andrew Ortiz, "Delayed Disclosure: 2024 Factsheet," CHILD USA, childusa.org/wp-content/uploads/2024/06/Delayed-Disclosure-2024.pdf.

6 *Id.*

7 *See Harrington v. Purdue Pharma LP*, 603 U.S. 204 (2024).

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to the trauma experienced, this provision ensures that their claims are addressed justly.

Second, the continuous litigation faced by organizations accused of widespread sexual abuse can be financially crippling and can distract from their primary mission. By applying § 524(g), these organizations can contribute to a trust fund and gain protection from further lawsuits, allowing them to focus on rehabilitation and prevention efforts.

Third, nonprofit religious institutions accused of widespread sexual abuse often have nondebtor affiliates that may wish to fund a trust in consideration for a global release but can no longer do so over the objection of creditors. In certain circumstances, the prohibition against nonconsensual third-party releases provides valuable protection to creditors from having their claims released against their will. In other circumstances, having the ability to approve nonconsensual third-party releases will help maximize the contribution from the proposed releasee, thereby increasing the distribution to all creditors. Such releases should be subject to a 90 percent supermajority, as opposed to the 75 percent currently required under § 524(g), providing greater protection from any perceived inequity in compelling a third-party release in child sex-abuse cases.

Expand Rule 2004 Investigations

Rule 2004 of the Federal Rules of Bankruptcy Procedure provides interested parties in a bankruptcy proceeding with the ability to obtain prelitigation discovery that is generally broader in scope than what the Federal Rules of Civil Procedure would allow. The scope of the examination can include the debtor's financial condition, the debtor's acts and conduct, any matter that might affect the administration of the debtor's estate, and the debtor's right to a discharge.

Sexual-abuse bankruptcies present unique challenges because of the need to (1) make certain that victims' claims are treated fairly and equitably based on the nature of the abuse and the debtor's assets available to satisfy such claims, and (2) assure the public that adequate steps are being taken to reduce the chances of future abuse. Bankruptcy Rule 2004 should be modified to ensure the thorough and fair examination of the circumstances surrounding the bankruptcy, permitting an examination of the following:

- an understanding of the nature and duration of the abuse, which can help in establishing the severity of claims;
- any remedial policies and responses to sexual-abuse allegations;
- information concerning an affiliated entity's finances and financial projections if they seek a release under the reorganization plan; and
- any other matter relevant to the allegations of abuse and the debtor's response to same.

Conclusion

Modifying the Bankruptcy Code to better address sexual-abuse bankruptcy cases offers a structured and equitable solution to a profoundly complex and sensitive issue. These proposed changes could provide a means for fair compensation, promote transparency and accountability, and give a voice to victims. As society continues to reckon with the widespread impact of sexual abuse, adapting existing legal frameworks to better serve justice and healing is both necessary and prudent. abi