105TH CONGRESS, 2d Session | HOUSE OF REPRESENTATIVES | REPORT 105–556

RELIGIOUS LIBERTY AND CHARITABLE DONATION PROTECTION ACT OF 1997

JUNE 3, 1998.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. GEKAS, from the Committee on the Judiciary, submitted the following

R E P O R T

[To accompany H.R. 2604]

[Including cost estimate of the Congressional Budget Office]

The Committee on the Judiciary, to whom was referred the bill (H.R. 2604) to amend title 11, United States Code, to protect certain charitable contributions, and for other purposes, having considered the same, reports favorably thereon without amendment and recommends that the bill do pass.

TABLE OF CONTENTS

	Page
Purpose and Summary	1
Background and Need for the Legislation	2
Hearings	6
Committee Consideration	6
Committee Oversight Findings	6
Committee on Government Reform and Oversight Findings	6
New Budget Authority and Tax Expenditures	6
Congressional Budget Office Cost Estimate	6
Constitutional Authority Statement	8
Section-by-Section Analysis and Discussion	8
Changes in Existing Law Made by the Bill, as Reported	11

PURPOSE AND SUMMARY

H.R. 2604 protects religious and charitable organizations from having to turn over to bankruptcy trustees donations these organi-

zations received from individuals who subsequently file for bankruptcy relief. In addition, the bill protects the rights of debtors to continue to make religious and charitable contributions after they file for bankruptcy relief.

BACKGROUND AND NEED FOR THE LEGISLATION

Representative Ron Packard (R-Cal.) introduced H.R. 2604 on October 2, 1997. It currently has 125 bipartisan cosponsors. As originally introduced, H.R. 2604 was identical to S. 1244, the "Religious Liberty and Charitable Donation Protection Act of 1997," which was introduced by Senator Charles Grassely (R-Iowa) (for himself and Senators Jeff Sessions (R-Ala.) and Rod Grams (R-Minn.)) on October 1, 1997.[1]

Under certain circumstances, a bankruptcy trustee, pursuant to section 548 of the Bankruptcy Code,[2] may recover assets that were transferred by a debtor before such he or she filed for bankruptcy relief. This provision ensures that these assets are brought into the bankruptcy estate so that they can be equitably distributed to the debtor's creditors.[3]

Some courts have held that a contribution made to a religious or charitable organization by a debtor before he or she filed for bankruptcy relief can be recovered by a bankruptcy trustee as a fraudulent transfer under section 548[4] on the basis that reasonably equivalent value was not received in exchange for the donation.[5] Noting that there was "no exchange of contributions for church services," the Eighth Circuit, for example, concluded that the debtors' religious contributions were recoverable by the trustee under section 548(a)(2) of the Bankruptcy Code.[6] Nevertheless, the court held that the trustee was precluded from recovering the suspect charitable contributions under the Religious Freedom Restoration Act ("RFRA"), 42 U.S.C. § 2000bb.[7]

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[1] S. 1244, subsequently amended to preempt state fraudulent transfer statutes in the context of a bankruptcy case, passed the Senate by a vote of 100 to 0 on May 13, 1998. 105 Cong. Rec. S4823 (daily ed. May 13, 1998).

[2] 11 U.S.C. § 548.

[3] Section 548 of the Bankruptcy Code has been described as "one of the most powerful tools available to the bankruptcy trustee." 5 COLLIER ON BANKRUPTCY ¶ 548.01 (Lawrence P. King *et al.* eds. 15th ed. rev. 1997).

[4] 11 U.S.C. § 548(a)(2)(A). Under this provision, a trustee can avoid a transfer of property made within one year before the filing of the bankruptcy case if the debtor received less than reasonably equivalent value in exchange for such transfer.

[5] *See, e.g., Weinman* v. The Word of Life Christian Center (*In re* Bloch), 207 B.R. 944, 948 (D. Colo. 1997).

[6] *Christians* v. *Crystal Evangelical Free Church* (*In re* Young), 82 F.3d 1407, 1415–16 (8th Cir. 1996), *vacated & remanded,* 117 S. Ct. 2502 (1997), *reinstated on remand,* 1998 U.S. App. Lexis 7348 (8th Cir. Apr. 13, 1998), *petition for cert. filed* 66 U.S.L.W. 3720 (U.S. Apr. 24, 1998) (No. 97–1744).

[7] *Id.* at 1420. It should be noted, however, that after the Eighth Circuit issued this holding, the United States Supreme Court rendered a decision questioning the constitutional validity of RFRA. *See City of Boerne* v. *Flores,* 117 S. Ct. 2157 (1997). In light of this decision, the Supreme Court vacated and remanded *Christians* to the Eighth Circuit. 117 S. Ct. 2502 (1997). On remand, the appellant-church argued that RFRA was a valid exercise of Congress' Article I powers and that it did not violate the Establishment Clause of the First Amendment. The Church also asserted that section 548(a)(2)(A) of the Bankruptcy Code violated the First Amendment's Free Exercise Clause. On remand, the Eighth Circuit reinstated its decision, holding that RFRA is "an appropriate means by Congress to modify the United States bankruptcy laws." 1998 U.S. App. Lexis 7348, at *16–17 (8th Cir. Apr. 13, 1998). A petition for certiorari to the Supreme Court has since been filed. 66 U.S.L.W. 3720 (U.S. Apr. 24, 1998) (No. 97–1744).

Other courts have concluded that a debtor received reasonably equivalent value in exchange for his or her religious contributions.[8] These courts consider, for example, whether the debtor received certain services from the religious entity, such as counseling, in exchange for his or her donation. This analysis, which essentially requires courts to value spiritual benefits and to determine whether they were conferred in exchange for the debtor's tithe, has led to disparate case law.

The focus on valuation, however, fails to address several important policy considerations that warrant treating religious and charitable contributions differently from other property transfers under section 548 of the Bankruptcy Code. One such policy consideration pertains to the inherent nature of these contributions and why they are made. Religious contributions are often given from a sense of duty. The practice of tithing, for example, is viewed by some religious organizations as a "fundamental precept and doctrine" based on "divine commandment from God."[9] A representative of The Church of Jesus Christ of Latter-day Saints, in his statement to the Subcommittee on Commercial and Administrative Law, explained:

> We have been taught and believe that the voluntary contribution of a full tithing—with the money or other in-kind contribution being used by the Church to further God's work on earth through the worldwide religious activities and mission of The Church of Jesus Christ of Latter-day Saints—is necessary in order for a member to be in good standing in our Church. We believe devoutly that our living of and obedience to the Lord's law of tithing is a crucial component to our spiritual development on earth and to our eternal salvation. . . . As members of The Church of Jesus Christ of Latter-day Saints, we believe that it is only through these highest ordinances and rites that we can attain eternal salvation and live together with our family throughout eternity.[10]

Arguably, the use of fraudulent transfer provisions to undo tithing may infringe the First Amendment rights of both the donor and donee.[11]

Another policy consideration is that contributions are used by religious and charitable organizations to fund valuable services to society, which serve the common good. This principle is recognized in the Internal Revenue Code's provisions concerning the deductibility of certain charitable contributions.[12]

Furthermore, most religious and charitable organizations lack the means to defend against a recovery action filed by a bank-

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[8] *See, e.g., Ellenberg* v. *Chapel Hill Harvester Church, Inc.* (*In re* Moses), 59 B.R. 815 (Bankr. N.D. Ga. 1986). After noting that the debtors received a variety of services, including counseling, from their church in exchange for their contribution, the bankruptcy court concluded that the trustee failed to sustain its burden of proof on the issue of reasonably equivalent value. *Id.* at 818.

[9] *Religious Liberty and Charitable Donation Protection Act of 1997 and Religious Fairness in Bankruptcy Act of 1997: Hearing on H.R. 2604 and H.R. 2611 Before the Subcomm. on Commercial and Administrative Law of the House Comm. on the Judiciary,* 105th Cong. (Feb. 12, 1998) [hereinafter *Hearing*] (statement of Ralph W. Hardy, Jr., President, Washington, D.C. Stake, The Church of Jesus Christ of Latter-day Saints).

[10] *Id.*

[11] *See, e.g., Hearing, supra* n. 9 (statement submitted for the record by Professor Douglas Laycock, University of Texas Law School).

[12] *See, e.g.,* 26 U.S.C. § 170(c).

ruptcy trustee under section 548. As a result, they must either return the funds or divert other resources to pay for defending such recovery actions.[13] Representative Packard, noting that it was "unconscionable" to require a religious organization to return contributions it received from a parishioner who subsequently filed for bankruptcy relief,[14] observed at the hearing on this bill before the Subcommittee on Commercial and Administrative Law that "Churches live on a day-to-day basis" and it "is almost impossible for them to plan for or budget for the return of sizeable contributions." As a result, the current law presented a "terrible hardship" for them, he said.[15] For the same reasons, he likewise supported extending this protection to nonprofit organizations as well.[16]

As to the substantial litigation costs that can be incurred by a religious organization in defending against a fraudulent conveyance action under section 548 of the Bankruptcy Code, the Subcommittee heard from the pastor of the Crystal Evangelical Free Church who testified that his church had expended more than $300,000 to defend a fraudulent transfer action brought by a bankruptcy trustee to recover $13,450 in tithes given by two of its members, a husband and wife who filed for bankruptcy relief.[17] Another witness testified that his religious organization incurred "significant legal expenses" to defend against these actions.[18] He explained:

> In defending demands of bankruptcy trustees, The Church of Jesus Christ of Latter-day Saints is primarily interested in asserting the rights of its members who made the contributions in questions [sic]. These members—who typically have contributed relatively modest amounts but have subsequently fallen on hard times financially—are clearly ill equipped to mount an effective challenge to the impairment of their most fundamental religious beliefs that the trustees' demands present.[19]

H.R. 2604 protects certain charitable contributions made by an individual debtor to qualified religious or charitable entities within one year preceding the filing date of the debtor's bankruptcy petition from being avoided by a bankruptcy trustee under section 548 of the Bankruptcy Code. The bill protects donations to qualified religious organizations as well as to charities, which are defined by reference to the Internal Revenue Code.

H.R. 2604 is not intended to diminish any of the protections against prepetition fraudulent transfers available under section 548 of the Bankruptcy Code.[20] If a debtor, on the eve of filing for bankruptcy relief, suddenly donates 15 percent of his or her gross income to a religious organization, the debtor's fraudulent intent, if any, would be subject to scrutiny under section 548(a)(1) of the Bankruptcy Code. This fifteen percent "safe harbor" merely shifts

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[13] Particularly in light of the longer reachback period permitted under state law made applicable under section 544(b) of the Bankruptcy Code, a charitable organization or religious entity may have to return funds it received from a debtor over a period extending several years. 11 U.S.C. § 544(b).

[14] *See, e.g., Hearing, supra* n. 9 (draft transcript at 19).

[15] *Id.* at 19–20.

[16] *Id.* at 20–21.

[17] *Id.* at 42, 45.

[18] *Id.* at 60. This witness noted, for example, that his church has had to defend against more than 120 lawsuits brought by bankruptcy trustees in ten states. *Id.* at 59–60.

[19] *Id.* (statement of Ralph W. Hardy, Jr., President, Washington, D.C. Stake, The Church of Jesus Christ of Latter-day Saints).

[20] *Id.* (draft transcript at 6–7, 22).

the burden of proof and limits litigation to where there is evidence of a change in pattern large enough to establish fraudulent intent. As Professor Laycock explained during the Subcommittee hearing on this bill:

> [B]oth of these bills include the very important safeguard that they don't touch section 548(a)(1). If I have been going along for years putting $5 a week in the collection plate and all of a sudden, before I file for bankruptcy, I clean out my last account and give 15 percent of my last year's income to my church, the trustee and the bankruptcy judge will look at the timing, the amount, the circumstances, the change in pattern, and they will say those are all badges of fraud. They will say I had the actual intent to hinder or defraud my creditors, and that is recoverable under section 548(a)(1). The fraud scenario is not going to happen.[21]

In addition, H.R. 2604 protects the rights of certain debtors to tithe or make charitable contributions after filing for bankruptcy relief. Some courts have dismissed a debtor's chapter 7 case (a form of bankruptcy relief that discharges an individual debtor of most of his or her personal liability without any requirement for repayment) for substantial abuse under section 707(b) of the Bankruptcy Code based on the debtor's charitable contributions.[22]

The bill also protects the rights of debtors who file for chapter 13 (a form of bankruptcy relief that requires a debtor to commit his or her future income to fund a plan of repayment) to tithe or make charitable contributions. Some courts have held that tithing is not a reasonably necessary expense or have attempted to fix a specific percentage as the maximum that the debtor may include in his or her budget.[23]

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[21] *Id.* at 39. Likewise, Senator Grassley, testifying with regard to an identical provision in his bill, S. 1244, stated:

> [T]he bill does not amend section 548(a)(1) of the Bankruptcy Code. This section lets bankruptcy courts recover any transfer of assets on the eve of bankruptcy if the transfer was made to delay or hinder a creditor. Therefore, if the bill is enacted, we don't have to worry about a sudden rash of charitable giving in anticipation of bankruptcy. Such transfers would obviously be for the purpose of hindering creditors and would still be subject to the bankruptcy judge's powers. In other words, there really isn't much room for abuse as a result of my legislation. *Id.* at 7.

[22] *See, e.g., In re* Faulkner, 165 B.R. 644, 649 (Bankr. W.D. Mo. 1994) (finding substantial abuse "due to the amount of disposable income which would be available in the absence of charitable contributions"); *In re* Lee, 162 B.R. 31, 42 (Bankr. N.D. Ga. 1993) ("Because debtors have not tithed consistently and because their church does not require tithing as a condition for full membership privileges, the monthly expense for tithing is unreasonable.").

[23] *See, e.g., In re* Reynolds, 83 B.R. 684, 684–85 (Bankr. W.D. Mo. 1988) (denying confirmation on ground that amount of "semi-biblical tithe" exceeded 3 percent of debtor's gross income); *In re* Curry, 77 B.R. 969, 969 (Bankr. S.D. Fla. 1987) (finding that a charitable contribution "does not constitute a reasonably necessary living expense"); *In re* Sturgeon, 51 B.R. 82, 84 (Bankr. S.D. Ind. 1985) (holding monthly $140 tithe was "not a necessary living expense" so debtor must commit this "amount to her plan as . . . part of her disposable income"). Other courts have held that tithing is a proper item of a chapter 13 debtor's proposed budget and confirmed plans providing for tithing. *See, e.g., In re* Bien, 95 B.R. 281, 283 (Bankr. D. Conn. 1989); *In re* Navarro, 83 B.R. 348, 356 (Bankr. E.D. Pa. 1988) (stating that the court was "not prepared to conclude that tithing and religious education are per se unreasonable choices for the maintenance and support of a chapter 13 debtor's family"); *In re* Green, 73 B.R. 893, 896 (Bankr. W.D. Mich. 1987), *aff'd,* 103 B.R. 852 (W.D. Mich. 1988) ("To deny confirmation of this plan solely because Mrs. Green [the debtor] tithes would be to deny her the benefits of the Bankruptcy Code because of conduct mandated by her religious beliefs.").

HEARINGS

On February 12, 1998, the Committee's Subcommittee on Commercial and Administrative Law held a hearing on H.R. 2604, the "Religious Liberty and Charitable Donation Protection Act of 1997," and H.R. 2611, the "Religious Fairness in Bankruptcy Act of 1997."[24] Testimony was received from nine witnesses: Senator Charles E. Grassley (R-Iowa); Representatives Helen Chenoweth (R-Idaho) and Ron Packard (R-Ca.); Stephen H. Case, Davis, Polk & Wardwell, on behalf of the National Bankruptcy Conference; Michael P. Farris, President, Home School Legal Defense Association; Dr. Stephen Paul Goold, Crystal Evangelical Free Church; Ralph W. Hardy, Jr., President, Washington, D.C. Stake, The Church of Jesus Christ of the Latter-day Saints; Professor Douglas Laycock, University of Texas Law School; and Steven McFarland, Director, Center for Law and Religious Freedom.

COMMITTEE CONSIDERATION

The Subcommittee on Commercial and Administrative Law was discharged from further consideration of H.R. 2604 on May 7, 1998. Thereafter, the Committee met in open session on May 14, 1998 and ordered favorably reported the bill H.R. 2604 without amendment by voice vote, a quorum being present.

COMMITTEE OVERSIGHT FINDINGS

In compliance with clause 2(l)(3)(A) of rule XI of the Rules of the House of Representatives, the Committee reports that the findings and recommendations of the Committee, based on oversight activities under clause 2(b)(1) of rule X of the Rules of the House of Representatives, are incorporated in the descriptive portions of this report.

COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT FINDINGS

No findings or recommendations of the Committee on Government Reform and Oversight were received as referred to in clause 2(l)(3)(D) of rule XI of the Rules of the House of Representatives.

NEW BUDGET AUTHORITY AND TAX EXPENDITURES

Clause 2(l)(3)(B) of House Rule XI is inapplicable because this legislation does not provide new budgetary authority or increased tax expenditures.

CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

In compliance with clause 2(l)(3)(C) of rule XI of the Rules of the House of Representatives, the Committee sets forth, with respect to the bill, H.R. 2604, the following estimate and comparison prepared

[24] As introduced by Representives Helen Chenoweth (R.-Idaho) and James Traficant (D.-Ohio) on October 6, 1997, H.R. 2611 provides that a donation to a religious group or entity made by a debtor out of a sense of religious obligation is deemed to have been made in exchange for a reasonably equivalent value. This bill proposes to amend section 548(d) of the Bankruptcy Code by adding a new subsection creating an exemption for donations made based on religious obligation.

by the Director of the Congressional Budget Office under section 403 of the Congressional Budget Act of 1974:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, May 19, 1998.

Hon. HENRY J. HYDE,
Chairman, Committee on the Judiciary,
House of Representatives, Washington, DC.

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 2604, the Religious Liberty and Charitable Donation Protection Act of 1997.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contacts are Susanne S. Mehlman (for federal costs), who can be reached at 226–2860, and Leo Lex (for the state and local impact), who can be reached at 225–3220.

Sincerely,

JUNE E. O'NEILL, *Director.*

Enclosure.

cc: Hon. John Conyers, Jr.,
Ranking Minority Member.

H.R. 2604—Religious Liberty and Charitable Donation Protection Act of 1997

CBO estimates that enacting H.R. 2604 would have no significant impact on the federal budget. Because enactment of H.R. 2604 would not affect direct spending or receipts, pay-as-you-go procedures would not apply. H.R. 2604 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act of 1995. The bill would have an impact on the budgets of state, local, or tribal governments only if those governments were creditors in a bankruptcy case affected by this bill. However, because of the small number and size of such cases, CBO estimates that the possible budgetary impact of this bill would be minimal.

Under current law, several courts have required that the charitable contributions that a debtor makes within a one-year period prior to declaring bankruptcy be refunded to the debtor's bankruptcy estate. Also, some courts have considered a debtor's contributions to charity as indicating that bankruptcy protection is unnecessary and consequently have dismissed the debtor's petition for bankruptcy. H.R. 2604 would amend federal bankruptcy law to prohibit creditors from seizing certain charitable contributions after an individual declares bankruptcy. This bill also would prohibit bankruptcy courts from considering whether a debtor makes charitable contributions when determining whether to dismiss a petition for bankruptcy.

Based on information from the Administrative Office of the United States Courts, CBO estimates that fewer than 1 percent of all bankruptcy cases that consumers file involve the contested issue of charitable contributions made by a debtor. Enacting H.R. 2604 could increase the workload of the courts and U.S. trustees if fewer cases are dismissed. At the same time, the bill could decrease the workload of the courts and U.S. trustees if less time is spent ques-

tioning charitable contributions and ordering charitable organizations to return such contributions. Although CBO is not certain whether the net impact of the bill would be a savings or a cost, we expect that any impact would be negligible because H.R. 2604 would affect so few cases. Because CBO estimates that enacting H.R. 2604 would not affect the total number of cases initially filed and the level of filing fees (which are recorded as governmental receipts and as offsetting collections to the U.S. Trustee System Fund), we estimate that pay-as-you-go procedures would not apply.

The CBO staff contacts for this estimate are Susanne S. Mehlman (for federal costs), who can be reached at 226–2860, and Leo Lex (for the state and local impact), who can be reached at 225–3220. This estimate was approved by Paul N. Van de Water, Assistant Director for Budget Analysis.

CONSTITUTIONAL AUTHORITY STATEMENT

Pursuant to Rule XI, clause 2(l)(4) of the Rules of the House of Representatives, the Committee finds the authority for this legislation in Article I, section 8, clause 4 of the Constitution.

SECTION-BY-SECTION ANALYSIS

Section 1. Short Title. The title of H.R. 2604 is the "Religious Liberty and Charitable Donation Protection Act of 1997."

Section 2. Definitions. This section defines "charitable contribution" and "qualified religious or charitable entity or organization." A "charitable contribution" is defined by reference to section 170(c) of the Internal Revenue Code of 1986.[25] In addition, the contribu-

[25] 26 U.S.C.§ 170(c). Section 170(c) of the Internal Revenue Code defines "charitable contribution" as follows:

(c) Charitable contribution defined.—For purposes of this section, the term "charitable contribution" means a contribution or gift to or for the use of—

(1) A State, a possession of the United States, or any political subdivision of any of the foregoing, or the United States or the District of Columbia, but only if the contribution or gift is made for exclusively public purposes.

(2) A corporation, trust, or community chest, fund, or foundation—

(A) created or organized in the United States or in any possession thereof, or under the law of the United States, any State, the District of Columbia, or any possession of the United States;

(B) organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals;

(C) no part of the net earnings of which inures to the benefit of any private shareholder or individual; and

(D) which is not disqualified for tax exemption under section 501(c)(3) by reason of attempting to influence legislation, and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

A contribution or gift by a corporation to a trust, chest, fund, or foundation shall be deductible by reason of this paragraph only if it is to be used within the United States or any of its possessions exclusively for purposes specified in subparagraph (B). Rules similar to the rules of section 501(j) shall apply for purposes of this paragraph.

(3) A post or organization of war veterans, or an auxiliary unit or society of, or trust or foundation for, any such post or organization—

(A) organized in the United States or any of its possessions, and

(B) no part of the net earnings of which inures to the benefit of any private shareholder or individual.

(4) In the case of a contribution or gift by an individual, a domestic fraternal society, order, or association, operating under the lodge system, but only if such contribution or gift is to be used exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals.

tion must be made by a natural person and in the form of either a "financial instrument," as defined in section 731(c)(2)(C) of the Internal Revenue Code of 1986, or cash.

A "qualified religious or charitable entity or organization" is defined by reference to applicable provisions of the Internal Revenue Code.[26] Included within the meaning of this term, for example, are entities organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes. It also includes the United States, States and municipalities, if the gift or contribution is made exclusively for public purposes.

Section 3. Treatment of Prepetition Qualified Charitable Contributions. Subsection (a) of Section 3 amends section 548(a)(2)(A) of the Bankruptcy Code, which, in pertinent part, permits a bankruptcy trustee to avoid or set aside a transfer of assets or an obligation incurred by the debtor where the debtor received "less than a reasonably equivalent value" in exchange for such transfer or obligation.[27] The determination of whether or not reasonably equivalent value was received by the debtor requires a two-prong analysis.[28] The first part of the analysis focuses on whether value was received. The second part requires a determination of whether the transfer was made in exchange for the value received.[29]

Subsection (a) excepts from section 548(a)(2)(A) a charitable contribution to a qualified religious or charitable entity or organization on either of the following grounds:

> (1) The amount of the contribution does not exceed 15 percent of the debtor's gross annual income for the year in which the transfer was made by the debtor.
>
> (2) If the contribution exceeded this 15 percent safe harbor, such transfer nevertheless was consistent with the debtor's practice of making charitable contributions.

The 15 percent safe harbor is necessary to protect the tithing practices of certain religious faiths.[30] It is intended to apply to transfers that a debtor makes on an *aggregate* basis during the one-year reachback period preceding the filing of the debtor's bankruptcy case. Thus, the safe harbor protects annual aggregate contributions up to 15 percent of the debtor's gross annual income.[31]

Subsection (b) amends section 544(b) of the Bankruptcy Code, which empowers a bankruptcy trustee to utilize applicable state law to undo certain property transfers made by a debtor prior to

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(5) A cemetery company owned and operated exclusively for the benefit of its members, or any corporation chartered solely for burial purposes as a cemetery corporation and not permitted by its charter to engage in any business not necessarily incident to that purpose, if such company or corporation is not operated for profit and no part of the net earnings of such company or corporation inures to the benefit of any private shareholder or individual.

For purposes of this section, the term "charitable contribution" also means an amount treated under subsection (g) as paid for the use of an organization described in paragraph (2), (3), or (4).

[26] This term is defined in the bill by reference to subsections 170(c) (1) and (2) of the Internal Revenue Code.

[27] 11 U.S.C. § 548(a)(2)(A).

[28] 5 Collier on Bankruptcy ¶ 548.05[1][b] (Lawrence P. King *et al.* eds. 15th ed. rev. 1997).

[29] *Id.*

[30] *See Hearing, supra* n. 9 (statement submitted for the record by Ralph W. Hardy, Jr., President, Washington, D.C. Stake, The Church of Jesus Christ of Latter-day Saints).

[31] *Id.* (statement submitted for the record by Professor Douglas Laycock, University of Texas Law School).

filing for bankruptcy relief.[32] Trustees use section 544(b) to avoid fraudulent transfers made outside the one-year reachback period of section 548 as some states have much longer periods for avoiding such transfers.[33] Subsection (b) specifically exempts the applicability of section 544(b) to charitable contribution transfers, as defined in section 2 of the bill.

Subsection (c) makes conforming amendments to section 546 of the Bankruptcy Code, which sets forth various limitations on a bankruptcy trustee's avoiding powers.[34]

Section 4. Treatment of Post-petition Charitable Contributions. Section 4 protects the right of certain debtors to tithe or make charitable contributions after they file for bankruptcy relief.

Under current law, a chapter 13 trustee or an unsecured creditor may object to the confirmation of a chapter 13 plan if it fails to provide that all of the debtor's projected "disposable income"[35] will be applied to make payments under the plan.[36] Subsection (a) amends section 1325(b)(2)(A) of the Bankruptcy Code to include within the definition of "disposable income" charitable contributions by the debtor that do not exceed 15 percent of the debtor's gross income.

This provision defines "charitable contribution" and "qualified religious or charitable entity or organization" as these terms are defined in section 2 of H.R. 2604. Unlike section 3, however, religious or charitable contributions that exceed 15 percent of the debtor's gross income are not protected even if they comport with the debtor's prior charitable practices.

Subsection (b) amends section 707(b) of the Bankruptcy Code, which authorizes the court to dismiss a chapter 7 case filed by an individual debtor on the ground that it constitutes substantial abuse of that chapter's provisions. Subsection (b) restricts a court from considering whether a chapter 7 debtor has made or continues to make charitable contributions, as defined in section 2 of H.R. 2604, in deciding to dismiss the case for substantial abuse under section 707(b).

This provision also employs the definitions set forth in section 2 for "charitable contribution" and "qualified religious or charitable entity or organization." Accordingly, contributions that do not meet these definitions remain subject to judicial scrutiny under section 707(b). The provision is not intended to limit judicial review concerning the issue of fraud.[37]

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[32] 11 U.S.C. § 544(b).

[33] Under New York law, for example, the reachback period can be six years. N.Y.C.P.L.R. § 213.

[34] 11 U.S.C. § 546.

[35] The Bankruptcy Code defines "disposable income" as income in excess of the debtor's reasonably necessary expenses for his or her support and that of his or her family. 11 U.S.C. § 1325(b)(2)(A). If the debtor is engaged in business, this term means income in excess of expenses necessary for the continuation, preservation and operation of such business. 11 U.S.C. § 1325(b)(2)(B).

[36] 11 U.S.C. § 1325(b)(1)(B).

[37] At the Subcommittee hearing on H.R. 2604, Representative Packard testified:

> We have tried desperately to craft language that would protect and avoid and prevent fraud. No one, certainly this member, does not wish to lay any groundwork that would allow someone to fraudulently use the church or a charitable organization to make a contribution to avoid their creditors if they are going into bankruptcy. I would be the very last to wish for that. We have tried to put language in this bill that would protect against that kind of fraudulent effort.

Hearing, supra n. 9 (draft transcript at 22).

Section 5. Applicability. This section makes H.R. 2604 applicable to pending cases as well as to cases commenced after its date of enactment.

Section 6. Rule of Construction. Section 6 provides that H.R. 2604 is not intended to limit the applicability of the Religious Freedom Restoration Act of 1993.[38]

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italics, existing law in which no change is proposed is shown in roman):

TITLE 11, UNITED STATES CODE

* * * * * * *

CHAPTER 5—CREDITORS, THE DEBTOR, AND THE ESTATE

* * * * * * *

SUBCHAPTER III—THE ESTATE

* * * * * * *

§ 544. Trustee as lien creditor and as successor to certain creditors and purchasers

(a) * * *

[(b) The trustee] *(b)(1) Except as provided in paragraph (2), the trustee* may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502(e) of this title.

(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).

* * * * * * *

§ 546. Limitations on avoiding powers

(a) * * *

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(e) Notwithstanding sections 544, 545, 547, [548(a)(2)] *548(a)(1)(B)*, and 548(b) of this title, the trustee may not avoid a transfer that is a margin payment, as defined in section 101, 741, or 761 of this title, or settlement payment, as defined in section 101 or 741 of this title, made by or to a commodity broker, forward contract merchant, stockbroker, financial institution, or securities

[38] 42 U.S.C. § 2000bb.

clearing agency, that is made before the commencement of the case, except under section [548(a)(1)] *548(a)(1)(A)* of this title.

(f) Notwithstanding sections 544, 545, 547, [548(a)(2)] *548(a)(1)(B)*, and 548(b) of this title, the trustee may not avoid a transfer that is a margin payment, as defined in section 741 or 761 of this title, or settlement payment, as defined in section 741 of this title, made by or to a repo participant, in connection with a repurchase agreement and that is made before the commencement of the case, except under section [548(a)(1)] *548(a)(1)(A)* of this title.

(g) Notwithstanding sections 544, 545, 547, [548(a)(2)] *548(a)(1)(B)* and 548(b) of this title, the trustee may not avoid a transfer under a swap agreement, made by or to a swap participant, in connection with a swap agreement and that is made before the commencement of the case, except under section [548(a)(1)] *548(a)(1)(A)* of this title.

(g) Notwithstanding the rights and powers of a trustee under sections 544(a), 545, 547, 549, and 553, if the court determines on a motion by the trustee made not later than 120 days after the date of the order for relief in a case under chapter 11 of this title and after notice and a hearing, that a return is in the best interests of the estate, the debtor, with the consent of a creditor, may return goods shipped to the debtor by the creditor before the commencement of the case, and the creditor may offset the purchase price of such goods against any claim of the creditor against the debtor that arose before the commencement of the case.

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§ 548. Fraudulent transfers and obligations

(a)*(1)* The trustee may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within one year before the date of the filing of the petition, if the debtor voluntarily or involuntarily—

[(1)] *(A)* made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted; or

[(2)(A)] *(B)(i)* received less than a reasonably equivalent value in exchange for such transfer or obligation; and

[(B)(i)] *(ii)(I)* was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation;

[(ii)] *(II)* was engaged in business or a transaction, or was about to engage in business or a transaction, for which any property remaining with the debtor was an unreasonably small capital; or

[(iii)] *(III)* intended to incur, or believed that the debtor would incur, debts that would be beyond the debtor's ability to pay as such debts matured.

(2) 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—

(A) 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

(B) the contribution made by a 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.

* * * * * * *

(d)(1) * * *

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(3) In this section, the term "charitable contribution" means a charitable contribution, as that term is defined in section 170(c) of the Internal Revenue Code of 1986, if that contribution—

(A) is made by a natural person; and

(B) consists of—

(i) a financial instrument (as that term is defined in section 731(c)(2)(C) of the Internal Revenue Code of 1986); or

(ii) cash.

(4) In this section, the term "qualified religious or charitable entity or organization" means—

(A) an entity described in section 170(c)(1) of the Internal Revenue Code of 1986; or

(B) an entity or organization described in section 170(c)(2) of the Internal Revenue Code of 1986.

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CHAPTER 7—LIQUIDATION

* * * * * * *

§ 707. Dismissal

(a) * * *

(b) After notice and a hearing, the court, on its own motion or on a motion by the United States trustee, but not at the request or suggestion of any party in interest, may dismiss a case filed by an individual debtor under this chapter whose debts are primarily consumer debts if it finds that the granting of relief would be a substantial abuse of the provisions of this chapter. There shall be a presumption in favor of granting the relief requested by the debtor. *In making a determination whether to dismiss a case under this section, the court may not take into consideration whether a debtor has made, or continues to make, charitable contributions (that meet the definition of "charitable contribution" under section 548(d)(3)) to any qualified religious or charitable entity or organization (as that term is defined in section 548(d)(4)).*

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CHAPTER 13—ADJUSTMENT OF DEBTS OF AN INDIVIDUAL WITH REGULAR INCOME

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SUBCHAPTER II—THE PLAN

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§ 1325. Confirmation of plan

(a) * * *

(b)(1) * * *

(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

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