UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re: THE ROMAN CATHOLIC DIOCESE OF ROCKVILLE CENTRE, NEW YORK, Debtor.	Chapter 11 Case No. 20-12345 (MG)

ORDER DENYING THE MOTION OF THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS TO DISMISS THE CHAPTER 11 CASE WITHOUT PREJUDICE

The Court, having considered the *Motion of the Official Committee of Unsecured Creditors to Dismiss the Chapter 11 Case* ("Motion to Dismiss" or "Motion," ECF Doc. # 1912) filed by the Official Committee of Unsecured Creditors ("Committee") and this Court having jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334, the Court finds that good and sufficient cause exists to enter this Order.

The Committee filed its Motion to Dismiss on March 27, 2023. On June 12, 2023, the Court entered a scheduling order for briefing, discovery, and a hearing on the motion. (ECF Doc. # 2144.) Pursuant to that scheduling order, The Roman Catholic Diocese of Rockville Centre, New York ("Debtor") filed its brief in opposition to the Motion on June 26 (ECF Doc. # 2199), and the Committee filed its reply brief in support of the Motion on June 30 (ECF Doc. # 2230). The parties also filed written direct testimony of their respective witnesses on June 30. A hearing was held on July 10 and 11, 2023, where the parties presented their evidence and cross-examined each other's witnesses. The Court took the matter under submission at the conclusion of the hearing.

The Committee moved to dismiss the case pursuant to section 1112(b) of the Bankruptcy Code (the "Code"), which provides that the Court:

> …shall convert a case under this chapter to a case under chapter 7 or dismiss a case under this chapter, whichever is in the best interests of creditors and the estate, for cause unless the court determines that the appointment under section 1104(a) of a trustee or an examiner is in the best interests of creditors and the estate.

11 U.S.C. § 1112(b).

Neither the Committee nor the Debtor argue that conversion to chapter 7 would be possible here, so the only issue is whether the Committee has shown that cause exists warranting dismissal. As the moving party the Committee has the burden of demonstrating cause for conversion by a preponderance of the evidence.[1]

The Committee argues that cause exists pursuant to section 1112(b)(4)(A) of the Code, which defines one illustrative example of cause as a "substantial or continuing loss to or diminution of the estate and the absence of a reasonable likelihood of rehabilitation." 11 U.S.C. § 1112(b)(4)(A). Showing cause under this subsection requires a two-prong showing: 1) loss to the estate; and 2) the absence of a likelihood of rehabilitation. The Court finds that the Committee has failed to make its required showing on the absence of a reasonable likelihood of rehabilitation, and thus has failed to show that cause exists pursuant to section 1112(b)(4)(A).

At the outset, the Court makes clear that, in these circumstances, it considers "rehabilitation" to mean the Debtor's proposal of a workable chapter 11 plan "within a reasonable period of time," as other courts have concluded in cases the Debtor relies on. *See In re Wahlie*, 417 B.R. 8, 11–12 (Bankr. N.D. Ohio 2009). In its briefing, however, the Debtor argued that "'[r]ehabilitation' is not synonymous with 'reorganization.'" *In re Honx, Inc.*, Case No. 22-90035, 2022 WL 17984313 at *3 (Bankr. S.D. Tex. Dec. 28, 2022). Instead, the Debtor contended that it need only "demonstrate[] … [its] commitment to the reorganization effort." *In*

[1] *In re Loco Realty Corp.*, No. 09–11785(AJG), 2009 WL 2883050, at *2 (Bankr. S.D.N.Y. June 25, 2009); *In re St. Stephen's 350 E. 116th St.*, 313 B.R. 161, 170 (Bankr. S.D.N.Y. 2004).

re 221-06 Merrick Blvd. Assocs. LLC, No. 1-10-45657-JBR, 2010 WL 5018265, at *2 (Bankr. E.D.N.Y. Dec. 3, 2010). In making this argument, the Debtor appears to suggest that simply making continued progress towards reorganization is sufficient to show a reasonable likelihood of rehabilitation. This may be true in the earlier phases of a bankruptcy case, when debtors are finding their bearings and exploring their exit options. Indeed, in the *Honx* case, and every other case cited by Debtor on this point, the debtors had been in bankruptcy for less than a year.[2] In contrast here, the Debtor has been in bankruptcy going on three years this fall.

The Court recognizes that the passage of time alone cannot be used to measure whether there is a reasonable likelihood of rehabilitation. The Court understands that in complex cases where debtors are forced to make operational changes and vet fundamentally different exit options in parallel, cases may remain open for years before a viable path to reorganization is established. Finding that cause for dismissal exists simply because two or three years have elapsed in such a case could undo years of progress toward rehabilitation.

Time is beginning to weigh against the Debtor here, however, because none of the dynamics in this case serve to explain why it is approaching three years with no proposal of a confirmable plan. While the Debtor may be selling some assets to fund its own plan contributions, it has not had to undertake any drastic operational changes—nor does it propose to as a means of exiting bankruptcy. Furthermore, while the first plans of reorganization were only proposed in the earlier part of this year, it is no secret that the Debtor's target plan structure has

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[2] *See Honx*, 2022 WL 17984313 at *3 (refusing to find cause existed approximately eight months into case, and distinguishing "rehabilitation" from "reorganization" where the debtor entered bankruptcy for the legitimate purpose of paying asbestos claimants, even though there was no business to reorganize); *In re 221-06 Merrick Blvd. Assocs. LLC*, 2010 WL 5018265, at *2 (refusing to find cause existed less than a year into the case, where debtor had obtained proposals that provided chance of successful reorganization within a few months of the motion being decided); *In re Basil Street Partners, LLC*, 477 B.R. 856, 862 (Bankr. M.D. Fla. 2012) (refusing to find cause existed where motion was made after eight months, and debtor had a proposed equity infusion into the business and framework for a proposed plan).

always been one by which it would continue to operate in the same manner, and certain third parties would help fund the plan contributions in exchange for releases. When the Court considers what progress would be indicative of a "commitment to the reorganization effort," the Court is hard-pressed to imagine anything other than the Debtor's proposal of workable plan in the near future. For that reason, the Court considers that "rehabilitation" in these circumstances means the proposal of a confirmable plan by the Debtor within a reasonable amount of time.

It became clear through the briefing and the hearing that the likelihood of any proposed plan being confirmable depends largely, if not exclusively, on the plan contributions from third parties that will be receiving releases under the plan. The Court generally assumes that in order to confirm a plan with third-party releases, the Debtor will need to receive "overwhelming" support from creditors under the Second Circuit's decision in *Purdue*. *See Purdue Pharma L.P. et al. v. The Official Committee of Unsecured Creditors of Purdue Pharma L.P. et al. (In re Purdue Pharma L.P. et al.)*, 69 F.4th 45, 78–79 (2d Cir. 2023). The Court assumes that the only way to do this here is for the third parties to make substantial monetary contributions that will incentivize creditors to favor approval of a plan over litigating their individual claims in state court.

The Committee put forth two general categories of evidence in support of its argument that the Debtor cannot do so here. Neither did anything to show whether the Debtor has a reasonable likelihood of proposing a confirmable plan in the near future.

First, all of the evidence put forth by the Committee regarding creditor opposition in this case was focused on the creditor body's opposition to the Debtor's first proposed plan of reorganization. The Debtor agrees, however, that its first proposed plan is not confirmable. Nevertheless, the Debtor contends that it is reasonably possible that it will propose an amended

plan with increased third-party contributions that will garner sufficient creditor support. The Committee's evidence regarding creditor opposition to the Debtor's first plan, even if completely admissible and afforded maximum weight, simply does not relate to whether this future event will occur.

Second, the expert testimony of the Committee's financial advisor, Mr. Paul Shields, did not bear on the Debtor's chances of reorganization. The testimony offered by the Committee only pertained to the losses being suffered by the Debtor's estate during this bankruptcy case. This may certainly be relevant to the losses prong under section 1112(b)(4)(A), and of course could theoretically threaten the chances of a successful reorganization if it were to continue indefinitely. But this testimony does nothing to show that there is an absence of a reasonable likelihood for rehabilitation at present moment. The Committee's expert report says nothing about the potential for adequate contributions from third parties in this case, which again, continues to be the sticking point on the likelihood of rehabilitation. Even more generally, the Committee's expert report says nothing about the present benefits to the estate (and thus creditors) of reaching a resolution in bankruptcy versus individual recoveries in state court.

The Court considers that even if it credits all of the evidence offered by the Committee, that the Committee still failed to show the absence of a reasonable likelihood of rehabilitation within a reasonable amount of time in its case in chief. Furthermore, the Debtor also presented evidence showing that its prospects for reorganization are not as bleak as the Committee argues they are—mainly, by pointing to developments that have happened in continued negotiations and mediation toward a consensual resolution since this Motion was filed.

The Debtor first highlighted that after the Motion to Dismiss was filed, the parties requested appointment of a judicial co-mediator in an attempt to reach a consensual resolution

for the entire bankruptcy case. On April 17, 2023, the Court entered an order taking judicial notice of the appointment of United States Magistrate Judge Sarah L. Cave as the co-mediator in the four declaratory judgment actions pending in the Southern District of New York related to the insurance coverage that is at issue in this case. (*See* ECF Doc. # 2018.) The Committee acknowledges this, but claims that it has not been involved in the mediation since May 19. During the hearing, however, the Debtor reported that it has continued mediation at the mediators' directive—presumably with other parties that are critical to a resolution, like insurers and potential third-party releasees.

Indeed, the Debtor also notes that since the Committee's filing of the Motion to Dismiss, the Debtor has negotiated with third parties to increase their plan contributions from $11 million to $40 million. While the Committee contends that these contributions are still inadequate, particularly because of alleged decreases in value of other estate assets since the Motion was filed, the Court considers that these increases are indicative of meaningful progress and may not necessarily be the best and final offer in any event.

The Debtor also reports that it has made additional disclosures regarding the finances of certain third party releasees. The Court expects that the Debtor will continue to facilitate such disclosures, as the Court was clear with the Debtor that in order to confirm a plan containing third party releases, the Court will be required to consider the extent of the disclosure regarding those parties' finances under *Purdue*. In confirming the reorganization plan in *Purdue*, the bankruptcy court noted that the third parties receiving releases "were required to provide extraordinary disclosure regarding . . . their assets and liabilities," which it considered relevant to assessing whether the third-party releases resulted in fair payment to the claimants. *In re Purdue Pharma L.P.*, 633 B.R. 53, 61 (Bankr. S.D.N.Y. 2021). The Second Circuit embraced

consideration of this factor on appeal; in its decision, the Court listed a number of factors that courts should consider in determining whether to approve plans containing third party releases, with the seventh and final factor being "whether the plan provides for the fair payment of enjoined claims." *In re Purdue Pharma L.P.*, 69 F.4th at 79.

For these reasons, the Court finds that the Committee failed to show that there is an absence of a reasonable likelihood of rehabilitation within a reasonable period of time. Because the Committee has failed to make this showing, it has also failed to show that cause exists to dismiss the chapter 11 case pursuant to section 1112(b)(4)(A) of the Code.

Therefore, it is hereby **ORDERED**:

1. The Motion to Dismiss is **DENIED**, but importantly, the Court notes that it is **DENIED WITHOUT PREJUDICE**. The Court concludes that Committee's arguments may be better pressed after the Debtor is afforded an opportunity to propose an amended plan of reorganization. In briefing and presenting evidence on the issue of likelihood of rehabilitation, both parties effectively staked their arguments regarding dismissal on the Debtor's ability to propose a confirmable plan of reorganization. As discussed above, the Court considers that the Debtor has only withstood the Motion to Dismiss here at this time because it took the position that it would be able to propose such a plan within a reasonable amount of time. At the hearing on the Committee's Motion to Dismiss, the Court inquired with the Debtor about what timeframe it considered reasonable for proposing an amended plan of reorganization. Counsel for the Debtor responded that it considered October 31, 2023 to be a reasonable deadline for proposing a plan. Counsel for the Committee responded that it considered 30 days to be a reasonable deadline.

2. The Court finds that the Debtor's deadline is more reasonable under these circumstances. For that reason, the Court **ORDERS** that the Debtor shall file an amended plan of reorganization and disclosure statement, or at minimum, a term sheet for a plan that is supported by both the Debtor and the Committee, by October 31, 2023.

3. This Court shall retain jurisdiction to hear and determine all matters arising from the implementation of this Order.

IT IS SO ORDERED.
Dated: July 18, 2023
New York, New York

/s/ Martin Glenn
MARTIN GLENN
Chief United States Bankruptcy Judge