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# Cy Pres Powers of the Federal Bankruptcy Courts - New Hope for Financially Distressed Charities?

## **Cover Page Footnote**

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# CY PRES POWERS OF THE FEDERAL BANKRUPTCY COURTS—NEW HOPE FOR FINANCIALLY DISTRESSED CHARITIES?

George B. Reese\*

## I. Introduction

It is a hard reality that numerous eastern municipalities are in the midst of financial crises.<sup>1</sup> At the same time, certain private charitable institutions operating in urban areas face financial problems of their own. In the past, these institutions—hospitals, community service centers, and the like—were partially reimbursed by government welfare funds for their “public services” expenditures.<sup>2</sup> But as the pressures on municipal budgets have increased, these reimbursements have become delayed, and sometimes uncertain. Charitable institutions, like the municipalities in which they operate, are now confronted with the task of maintaining normal operations in the face of increasing debt burdens.

One possible solution, albeit a drastic one, is for such corporations to reorganize in bankruptcy.<sup>3</sup> Under the provisions of the Bank-

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1. See generally Bond, *Municipal Bankruptcy under the 1976 amendments to Chapter IX of the Bankruptcy Act*, 5 *FORDHAM URBAN L.J.* 1, 2-4 (1976); see also Note, *The Limits of State Intervention in a Municipal Fiscal Crisis*, 4 *FORDHAM URBAN L.J.* 545 (1976).

2. In an earlier period when governmental services were meager, and in many cases non-existent, public funds were used extensively to subsidize voluntary agencies rendering needed services. In some instances, these payments were in the form of lump sums, as a subsidy to help cover the cost of its operations, in others they were payments for specific services rendered or for individuals receiving care. . . . There are of course occasions for the purchase of services from voluntary agencies and institutions by the government, but for most public services, the government relies and undoubtedly will continue to rely on the governmental welfare agencies.

W. VASEY, *GOVERNMENT AND SOCIAL WELFARE* 92 (1965).

3. In 1973, New York's French and Polyclinic Hospital filed a petition seeking reorganization under Chapter XI of the Bankruptcy Act. The hospital had been formed in 1969 by the merger of two of New York City's oldest voluntary hospitals, both dating back to the nineteenth century. On October 2, 1975, the bankruptcy court ordered the hospital shut down, but subsequently stayed that order indefinitely. *N.Y. Times*, Oct. 9, 1975, at 45, col.5. However, on March 8, 1977, the court ordered the hospital to close down permanently and liquidate its assets. *In re French & Polyclinic Medical School & Health Center, Inc.*, No. 73 B 691 (S.D.N.Y. Mar. 8, 1977).

ruptcy Act (Act),<sup>4</sup> a court in bankruptcy may suspend a corporation's debt service, order current revenues to be applied in payment of current expenses, and most importantly, grant the bankrupt corporation time to realign its resources and reconsider its commitments.<sup>5</sup> In the past, however, the reorganization in bankruptcy of a charitable corporation has been a rare event. These corporations' tax-exempt status<sup>6</sup> formerly provided a strong bulwark against insolvency.<sup>7</sup> But huge operating deficits, coupled with severe cash flow

4. 11 U.S.C. §§ 1-1103 (1970), as amended, (Supp. V, 1975).

5. 11 U.S.C. § 29 (a) (1970), provides that the bankruptcy court may stay suits against the bankrupt which are founded upon claims likely to be eradicated by a discharge in bankruptcy. Chapter XI recognizes application of section 11, and confers upon the court further power to stay other suits. 11 U.S.C. § 714 (1970). The court, on notice and for cause shown, may even stay proceedings to enforce liens on the debtor's property. *In re Atlantic Steel Products Corp.*, 31 F. Supp. 408 (E.D.N.Y. 1939).

6. Section 501(c) of the Internal Revenue Code lists as exempt organizations:

(3) Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or for prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting to influence legislation, and which does not participate in, or intervene in . . . any political campaign on behalf of any candidate for public office.

See also Sugarman and Pomeroy, *Business Income of Exempt Organizations*, 46 VA. L. REV. 424 (1960). The Code also provides that gifts to certain designated charities are deductible by the donor up to specified limits, usually 50 percent of the donor's gross income. I.R.C. § 170(b).

7. One commentator has noted that:

[T]he federal income tax laws by providing tax exemption and encouraging contributions to qualifying nonprofit health institutions, have an important effect on the operation and expansion of voluntary hospitals, homes for the aged and other health facilities. On the other hand, the changing patterns of financing health care have an equally important effect upon the laws which provide tax exemption for these institutions.

Bromberg, *Financing Health Care and The Effect of the Tax Law*, 39 LAW & CONTEMP. PROB. 156 (Autumn 1975). However, the same author also noted that present economic conditions have rendered useless the traditional method of financing hospital operations:

In order to remain financially solvent, it is usually necessary for most hospitals to attempt to operate at an excess of receipts over the sum of disbursements and historical cost depreciation. Under cost reimbursement formulae, replacement and renovation of assets is generally limited to reimbursement based on depreciation, with most "cost plus" exceptions usually being inadequate in inflationary periods . . . . However, in today's inflationary economy, this formula will obviously not be sufficient to enable hospitals to replace assets at current prices. Thus, inflation, coupled with technological advances which make needed replacements more complex and expensive, makes it difficult for hospitals to rely on reimbursement for their future capital needs and compels them to orient their operations towards realizing an excess of receipts over disbursements just to operate.

shortages, may so overwhelm available funds that bankruptcy, once considered a legal oddity, will become a form of relief seriously contemplated by a number of large charitable institutions.

Forced to conduct their interim operations with restricted funding, some institutions have increasingly looked to private endowments to maintain services at adequate levels.<sup>8</sup> Yet such endowments tend to be tied to all the hedges and restrictions that human wisdom can devise or human vanity dictate. In present circumstances, such restrictions seem to cause a misallocation of precious financial resources.

State law has long provided a means of removing restrictions—the cy pres doctrine—when changing circumstances render them either unreasonable or impossible to enforce.<sup>9</sup> According to this doctrine, a gift in trust or otherwise which is determined to have been made pursuant to a general charitable intent will not fail under the changed circumstances,<sup>10</sup> but instead will be judicially modified to carry out, as nearly as possible, the donor's presumed wishes.<sup>11</sup>

*Id.* at 157.

8. See, e.g., *In re Staten Island Hosp.*, N.Y.L.J., April 26, 1976, at 9, col. 4 (Sur. Ct. 1976). The current problems of reduced resources and endowment are shared by many of the voluntary hospitals in the New York metropolitan area. See *N.Y. Times*, Feb. 4, 1973, at 46, col. 3.

9. RESTATEMENT (SECOND) OF TRUSTS § 399 (1959) describes the cy pres doctrine as follows: If property is given in trust to be applied to a particular charitable purpose, and it is or becomes impossible or impracticable or illegal to carry out the particular purpose, and if the settlor manifested a more general intention to devote the property to charitable purpose, the trust will not fail but the court will direct the application of the property to some charitable purpose which falls within the general charitable intention of the settlor.

No charitable organization may receive a gift made for one purpose and use it for another, unless a court applying the cy pres doctrine so commands. *In re Lawless' Will*, 194 Misc. 844, 87 N.Y.S.2d 386 (Sur. Ct. 1949), *aff'd*, 277 App. Div. 1045, 100 N.Y.S.2d 537 (2d Dep't 1950); *Knickerbocker Hosp. v. Goldstein*, 181 Misc. 540, 41 N.Y.S.2d 32 (Sup. Ct. 1943).

10. Reverter due to the failure of a trust's purposes would be unlikely in the case of a charitable trust because of the possible application thereto of the cy pres doctrine. See *Hanover Bank v. The United Brethren's Church*, 134 N.Y.S.2d 356, 360 (Sup. Ct. 1954). See note 20 *infra*.

11. In most states, the cy pres doctrine has been codified. N.Y. EST., POWERS & TRUSTS LAW § 8-1.1(c) (McKinney 1967) provides:

The supreme court and, where the disposition is made by will, the surrogate's court in which such will is probated have jurisdiction over the dispositions referred to and authorized by paragraphs (a) and (b) [charitable trusts], and whenever it appears to such court that circumstances have so changed since the execution of an instrument

A charitable corporation contemplating a petition in bankruptcy might also wish to seek cy pres relief from the bankruptcy court. However, the dearth of case law involving such bankruptcies has left unclear whether the two proceedings could be combined—that is, whether a bankruptcy court, as part of a plan of reorganizations, could modify restrictions on charitable endowments in a fashion similar to state cy pres relief. This Article will examine the nature of the cy pres doctrine and the jurisdiction of the bankruptcy court to determine whether the court may grant such relief to financially-distressed charities.

## II. Cy Pres Under State Law

When the terms of a charitable trust become impossible or impractical to execute, the trustee must ask a court of competent jurisdiction to apply the cy pres doctrine and reform the trust.<sup>12</sup> The trustee has no authority to deviate from the trust provisions on his own.<sup>13</sup>

The court's primary objective in a cy pres proceeding is to determine the intent of the trust creator.<sup>14</sup> First, the court must ascertain whether the creator intended to benefit a specific beneficiary or simply a general class of persons. If specific charitable intent is discerned, then cy pres may not be applied;<sup>15</sup> but if the court concludes that the creator was motivated by a general charitable in-

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making a disposition for religious, charitable, educational or benevolent purposes as to render impracticable or impossible a literal compliance with the terms of such disposition, the court may, on application of the trustee or of the person having custody of the property subject to the disposition and on such notice as the court may direct, make an order or decree directing that such disposition be administered and applied in such manner as in the judgment of the court will most effectively accomplish its general purposes, free from any specific restriction, limitation or direction contained therein; provided, however, that any such order or decree is effective only with the consent of the creator of the disposition if he is living.

12. *In re Koons' Will*, 206 Misc. 856, 858, 135 N.Y.S.2d 733, 735 (Sup. Ct. 1954); *Knickerbocker Hosp. v. Goldstein*, 181 Misc. 540, 543, 41 N.Y.S.2d 32, 34-35 (Sup. Ct. 1943).

13. See 4 SCOTT ON TRUSTS § 391 (3d ed. 1967); see also *In re Koons' Will*, 206 Misc. 856, 858, 135 N.Y.S.2d 733, 735 (Sup. Ct. 1954); *Knickerbocker Hosp. v. Goldstein*, 181 Misc. 540, 543, 41 N.Y.S.2d 32, 35 (Sup. Ct. 1943).

14. "In applying the doctrine of cy pres the courts endeavor to accomplish the general charitable purpose of the testator 'as nearly as it can be conveniently done, consistently with the efficacious promotion of the general design.' . . ." *Town of Brookline v. Barnes*, 327 Mass. 201, 208, 97 N.E.2d 651, 655 (1951), quoting *American Acad. of Arts & Sciences v. President of Harvard College*, 78 Mass. (12 Gray) 582, 589 (1832).

15. See 4 SCOTT ON TRUSTS § 399 (3d ed. 1967).

tent, the gift will be appropriately modified.<sup>16</sup> In *In re Goehring*,<sup>17</sup> the testator left a large bequest to a preparatory school. Six months after the testator's death, the trustees of the school voted to dissolve the charitable corporation and close the school.<sup>18</sup> The court was asked to apply the cy pres doctrine and did so according to the test of intent:<sup>19</sup>

In applying cy pres we must be mindful that courts have no more power to make wills for the dead than contracts for the living. Therefore basic to that determination is the intention of the testator. A broad generality is that the cy pres doctrine . . . will be applied (though impossible to carry out fully the testator's expressed desires) if from the will as a whole there may be discerned a primary intention of the testator to devote his property to a general charitable purpose rather than to give the gift to a particular charity or for a particular purpose. Where the issue arises because of the nonexistence, merger or dissolution of the charitable beneficiary, the test applied is—if a general charitable purpose is primary and the particular beneficiary is only secondary, cy pres will be applied. On the other hand if the particular beneficiary is primary and the general charitable purpose only secondary then cy pres will not be applied.

Applying this test, the court held that the testator's primary motive was a general charitable intent and reformed the trust.<sup>20</sup>

16. In the usual course of affairs, courts tend to find charitable intent frequently. The New York Court of Appeals has recognized the "liberality of the rules which the courts have adopted in order to save charitable gifts by the application of cy pres." *In re Syracuse Univ.*, 3 N.Y.2d 665, 670, 148 N.E.2d 671, 673, 171 N.Y.S.2d 545, 547-48 (1958).

17. 69 Misc. 2d 145, 329 N.Y.S.2d 516 (Sur. Ct. 1972).

18. *Id.* at 146, 329 N.Y.S.2d at 518. While this case technically involved a distribution of assets following dissolution of a charitable corporation, the court indicated that the cy pres doctrine was applicable to the proceeding. *Id.* at 147, 329 N.Y.S.2d at 520.

19. *Id.* at 148, 329 N.Y.S.2d at 520 (citations omitted).

20. *Id.* at 148-49, 329 N.Y.S.2d at 521. The court noted that:

The testator does not perhaps foresee the possible failure of his gift. But when he does, he generally does not look ahead beyond the vesting of the gift. Up to the point of vesting he may very well have an intention to benefit a particular institution. But all institutions must ultimately fail, if not soon after vesting then decades later. Of course, those dispositions which are outright gifts will have then been consumed. Those which are in charitable trust . . . and not consumed will invariably be subjected to cy pres. The reasons — this is what most testators probably intend should the gift fail long after vesting: judicial policy favoring charitable gifts prompts courts to find a general charitable intent.

*Id.* Once a charitable disposition has vested, the cy pres doctrine will invariably be applied, unless the creator has clearly evidenced an intent that a particular gift over has been in the event of the failure of the bequest. *In re Neher*, 279 N.Y. 370, 18 N.E.2d 625 (1939). In *In re Potter*, 307 N.Y. 504, 121 N.E.2d 552 (1954), the trust creator had left an amount in trust to

Two recent cases demonstrate the liberality with which the cy pres doctrine has come to be applied in New York State. *In re Staten Island Hospital*<sup>21</sup> was a proceeding brought by a private hospital, as the income beneficiary of certain trust funds, seeking modification of the trust. The hospital occupied a fifty-year-old building which, due to overcrowded conditions and structural defects, was in violation of health and safety standards promulgated by the United States Department of Health, Education and Welfare. As a result, federal payments to the hospital under Medicare were in jeopardy. The hospital sought to obtain the trust principal and use it to erect a new hospital building.

The court took note of the hospital's plight: failure to correct the overcrowding and structural defects would make the hospital ineligible for Medicare reimbursement, depriving the hospital of 38 percent of its income.<sup>22</sup> Repair of the structural faults would have cost over two million dollars and would not have relieved the overcrowding; in short, "[i]f the new hospital facilities [were] not built, the Staten Island Hospital [would have gone] out of existence."<sup>23</sup> Examining the trust instruments, the court concluded that the testators had expressed a general, rather than specific, charitable intent:<sup>24</sup>

Circumstances have so changed since the execution of these wills that it is no longer practicable to continue to use the income from these funds to maintain the present facility and it will be impossible to use the income for the benefit of the hospital if the hospital ceases to exist. The facts here warrant the application of cy pres to carry out the general charitable intent of the decedents and to prevent the failure of their definite charitable purpose, the continued operations of the Staten Island Hospital.

Thus, the court preserved the specific beneficiary by carrying out the testators' general intent, though not their specific instructions.

Public policy considerations can have a considerable influence on

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a private school to be used for educating "the children of the poor." *Id.* at 509, 121 N.E.2d at 523. More than a century after the gift vested, the school was merged into the public school system. The trustee brought an action to compel a reverter of the funds, pursuant to a provision of the trust. The court denied the application and applied the cy pres doctrine, on the theory that the fund could still be used for the general purpose of educating the children of the poor. *Id.* at 518, 121 N.E.2d at 529.

21. N.Y.L.J., April 26, 1976, at 9, col. 4 (Sur. Ct. 1976).

22. *Id.* at col. 5.

23. *Id.*

24. *Id.*



cy pres proceedings, as is shown by *In re Samaritan Fund for the Aged*.<sup>25</sup> In *Samaritan Fund*, a not-for-profit corporation petitioned the New York Supreme Court for judicial approval of a plan of dissolution. The fund was the beneficiary of certain trust assets which were used to maintain and operate a home for indigent, aged members of the Protestant faith; the restrictions on these assets apparently were continued in the proposed plan of dissolution.

The court was dissatisfied with the proposed plan and appointed a referee to develop a new distribution scheme. Under the referee's proposal, adopted by the court, the trust funds specifically intended to aid members of a particular religious group became available for the care of the indigent aged in general.<sup>26</sup>

Cy pres proceedings are fairly complex. In New York, the nature of the trust determines the forum which will interpret and administer it. Proper venue for testamentary trusts lies in the surrogate's court that admitted the will to probate,<sup>27</sup> while petitions regarding inter vivos trusts are heard by the supreme court.<sup>28</sup> Necessary parties to all such proceedings include the State Attorney General,<sup>29</sup> the trustees<sup>30</sup> (if they are not the petitioning parties), the creator of the trust<sup>31</sup> (if he is still alive), and in the case of real property, the

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25. N.Y.L.J., May 5, 1976, at 7, col. 2 (Sup. Ct. 1976).

26. *Id.* The court in *Samaritan Fund* was obviously concerned with overcoming a restriction it found repugnant and noted some of the factors it considered in deciding the disposition of the trust principal:

In accordance with the original mandate, special attention as directed by the referee to the admissions and employment policies and history of the proposed donee, in the context of its geographic locale and surrounding population composition. An in-depth study and review of relevant legal precedents and memoranda was necessarily undertaken by him on this issue. Past and current records of the proposed donee were meticulously examined. Among those heard on this question was the Supervising Compliance Officer for the Civil Rights Compliance Unit of the New York State Department of Health, the agency which is responsible for surveying skilled nursing and health related facilities in the state for purposes of verifying compliance with state and federal civil rights legislation.

*Id.* Public policies must therefore be considered significant factors in the application of the cy pres doctrine.

27. N.Y. EST., POWERS & TRUSTS LAW § 8-1.1(c) (McKinney 1967) (concurrently with the supreme court).

28. *Id.*

29. *Id.* § 8-1.1(f) provides that "The attorney general shall represent the beneficiaries of such dispositions for religious, charitable, educational or benevolent purposes and it shall be his duty to enforce the rights of such beneficiaries by appropriate proceedings in the courts."

30. *Id.* § 8-1.1(c).

31. *Id.*

owners of any future estates.<sup>32</sup> Thus, when a charity is faced with a need to reallocate endowment funds, it may be required to submit a number of multiparty petitions to various tribunals. As a result, a comprehensive plan respecting these funds rarely could be presented to a single state judge or court.<sup>33</sup>

### III. Reorganization Under the Bankruptcy Act

The Constitution grants Congress the power "[to] establish . . . uniform laws on the subject of Bankruptcies throughout the United States."<sup>34</sup> This power is exercised through the current Bankruptcy Act,<sup>35</sup> which preempts state provisions regarding debtor-creditor relations.<sup>36</sup> Chapter XI of the Act<sup>37</sup> provides a workable method for modifying a debtor's entire financial structure in a single forum;<sup>38</sup> a

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32. *Id.* § 8-1.1(h).

33. The consolidation and removal provisions of New York Civil Practice Law and Rules in no way obviate the need for multiple petitions. See N.Y.C.P.L.R. § 325 (McKinney 1972); *Id.* § 5602 (McKinney 1976). In any event, consolidation is discretionary and not mandatory. *Id.* § 602.

34. U.S. CONST. art. 1, § 8.

35. 11 U.S.C. §§ 1-1103 (1970), as amended, (Supp. V, 1975).

36. See 1 COLLIER, BANKRUPTCY ¶ 0.02 (14th ed. 1974).

37. 11 U.S.C. §§ 701-99 (1970). Proceedings under Chapter XI of the Bankruptcy Act are directed toward formulating an arrangement under which the creditors voluntarily release the debtor in exchange for a portion of the sums actually owed them. The benefits to the debtor of such an arrangement are obvious; it maintains operations and avoids the complete liquidation of assets which is a necessary condition to relief under the so-called "straight bankruptcy" provisions of the Act. *Id.* §§ 1-112 (1970), as amended, (Supp. V, 1975). Similarly, a Chapter XI arrangement is often more beneficial to creditors. While they receive only a portion of sums actually owed them, a Chapter XI plan will often yield a higher return than liquidation; in addition, creditors will usually derive future business from the reorganized debtor. See LEVIN AND WEINTRAUB, PRACTICAL GUIDE TO CHAPTER XI OF THE BANKRUPTCY ACT 3 (1975).

It should be noted that all provisions of the Bankruptcy Act pertaining to stays of creditor actions against the debtor apply to Chapter XI cases. See BANKR. R. 11-44(a). Proposed arrangements must be accepted by a majority of creditors (or where creditors are classified, a majority of each class), holding a majority in amount of all claims. 11 U.S.C. § 762 (1970). Upon acceptance and subsequent confirmation of the plan by the court, the case is dismissed, *Id.* § 767; but upon the debtor's failure to comply with the terms of the plan, the court may adjudicate the debtor a bankrupt and order liquidation of the debtor's assets. *Id.* § 277; BANKR. R. 11-42(b).

Chapter XI is essentially a "relief and rehabilitation statute. It is founded upon the principle that preservation of a business is good for the national economy and that its liquidation is not." Herzog, *Mechanics of Chapter XI*, in PROCEEDINGS OF SEMINAR FOR NEWLY APPOINTED REFEREES IN BANKRUPTCY 283 (1964).

38. Chapter XI has generally been recognized as a more successful reorganization scheme than Chapter X, which deals strictly with corporate reorganization. One authority notes:

charitable entity<sup>39</sup> seeking to maintain operations would seek relief under this Chapter.

### A. Jurisdiction Over the Debtor's Assets

Upon the filing of a Chapter XI petition, the bankruptcy court in which the petition is filed obtains exclusive jurisdiction over the debtor and his assets, wherever located.<sup>40</sup> Once a trustee has been appointed and qualified,<sup>41</sup> he is vested by operation of law with the debtor's title to all nonexempt property.<sup>42</sup> Exemptions are normally determined by reference to state law,<sup>43</sup> unless state law impairs the

[A] practical evaluation suggests greater benefits by a composition or extension under Chapter XI than the doubtful values under Chapter X of a long proceeding, new management getting on-the-job training and new interests acquiring control of the business.

LEVIN AND WEINTRAUB, PRACTICAL GUIDES TO CHAPTER XI OF THE BANKRUPTCY ACT 4 (1975).

39. Cursory inspection of the Act might yield the conclusion that charitable corporations are not covered by its provisions; yet this is clearly not the case. 11 U.S.C. § 22 (1970) applies to all "persons," with specified exclusions. No exception is made for charitable corporations or trusts. The word "persons," as defined by the Act, clearly embrace a charitable entity:

"Persons" shall include corporations, except where otherwise specified, and officers, partnerships, and women, and when used with reference to the commission of acts which are forbidden under this title shall include persons who are participants in the forbidden acts, and the agents, officers, and members of the board of directors or trustees or of other similar controlling bodies of corporations.

*Id.* § 1(23).

40. *Id.* § 110(a).

41. In Chapter XI proceedings, the court may decline to appoint a trustee and permit the debtor to remain in possession of his property and to have all the title and exercise all the powers of a duly-appointed trustee. *Id.* § 742. The debtor in possession is at all times subject to the control of the bankruptcy court. *Id.* He may be required to furnish a bond or other security. BANKR. R. 11-20(a), 11-20(f). For the advantages of allowing the debtor to continue in possession, see note 38 *supra*. In the United States District Courts for the Southern and Eastern Districts of New York, the customary practice is to allow the debtor to continue in possession and operate his business. However, receivers are appointed in other districts. See LEVIN AND WEINTRAUB, PRACTICAL GUIDE TO CHAPTER XI OF THE BANKRUPTCY ACT 5 (1975).

42. 11 U.S.C. § 110 (1970).

43. The Act describes the assets of the bankrupt's estate to which the trustee takes title. *Id.* § 110(a). In its most general statement, this section provides that the trustee is vested with the bankrupt's title to "property, including rights of action, which prior to the filing of the petition he could by any means have transferred or which might have been levied upon and sold under judicial process against him, or otherwise seized, impounded or sequestered . . . ." *Id.* § 110(a)(5).

The question of what property the debtor could transfer is usually determined by reference to state law. *Hewitt v. Berlin Machine Works*, 194 U.S. 296, 303 (1904). *But cf.* *Chicago Board of Trade v. Johnson*, 264 U.S. 1, 10 (1924). See generally Countryman, *The Use of State Law in Bankruptcy Cases*, 47 N.Y.U. L. Rev. 407 (1972).

efficacy of the bankruptcy power.<sup>44</sup> In evaluating the bankruptcy court's power to grant *cy pres* relief, two issues must be confronted: (1) when, under state law, does a gift actually vest in the charitable organization; and (2) does the trustee in bankruptcy take title to trust assets?

In New York, assets left in trust for the use of a charitable corporation are deemed to be the outright property of the corporation; the corporation holds the property on its own behalf and not as trustee. The New York Not-For-Profit Corporation Law provides:<sup>45</sup>

A corporation . . . classified as a Type B corporation shall hold full ownership rights in any assets consisting of funds or other real or personal property of any kind, that may be given, granted, bequeathed or devised to or otherwise vested in such corporation in trust for, or with a direction to apply the same to, any purpose specified in its certificate of corporation, and shall not be deemed a trustee of an express trust of such assets. Any other corporation subject to this chapter may similarly hold assets so received, unless otherwise provided by law or in the certificate of incorporation.

This provision codifies the rule of *Saint Joseph's Hospital v. Bennet*,<sup>46</sup> in which the New York Court of Appeals held that property transferred to a charity upon condition or in trust actually vests in the charity. The basis for the holding in *Saint Joseph's* was the common law doctrine that an entity may not be the trustee of a fund for its own benefit;<sup>47</sup> such mergers of legal and beneficial interest have been consistently held to defeat the existence of a trust.<sup>48</sup> Since property given in trust or upon condition is deemed vested in a charitable corporation, the bankruptcy court could exercise jurisdiction over it when the corporation presents itself in the posture of a Chapter XI debtor.

If a charitable corporation holds property as a trustee for another beneficiary, the trustee in bankruptcy will normally take title to such trust assets, subject of course to the outstanding interest of the beneficiaries.<sup>49</sup> However, "[w]hen it appears that the bankrupt [or

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44. *Local Loan Co. v. Hunt*, 292 U.S. 234 (1934).

45. N.Y. NOT-FOR-PROFIT CORP. LAW § 513(a) (McKinney 1970).

46. 281 N.Y. 115, 22 N.E.2d 305 (1939).

47. *Id.* at 120, 22 N.E.2d at 307, citing *Wetmore v. Parker*, 52 N.Y. 450, 458 (1873).

48. See *Reed v. Browne*, 295 N.Y. 184, 188, 66 N.E.2d 47, 49 (1946); *Rose v. Hatch*, 125 N.Y. 427, 26 N.E. 467 (1891); see also RESTATEMENT (SECOND) OF TRUSTS § 99(5) (1959).

49. 4A COLLIER, BANKRUPTCY ¶ 70.25 (14th ed. 1976).

debtor] was only a trustee and had no beneficial interest in or claim against the property, . . . the court should turn the property over to its true owners when possible."<sup>50</sup>

A different situation exists where the charitable debtor is the beneficiary of trust property held by a separate trustee. Under state law, the property has vested in the trustee, and the debtor has no legal title to it;<sup>51</sup> however, the debtor does have some interest in and rights to the property, over which the bankruptcy court might take jurisdiction.<sup>52</sup>

The rule is that where property is held in trust for one who becomes bankrupt, the bankruptcy trustee, upon his appointment, becomes vested with any interest in the trust estate or fund the bankrupt had, provided that at the time of the filing of the petition such interest was under § 70(a)(5)[11 U.S.C. § 110(a)(5)] capable of being assigned or transferred by the bankrupt or was subject to attachment, seizure or judicial sale.

Whether an interest was assignable or transferable at the time the petition was filed is generally determined by the law of the state where the trust has its situs.<sup>53</sup>

Where a charitable debtor is the sole possible income beneficiary of a charitable trust, an argument might be advanced that the corpus of the trust is in reality property of the debtor and that the trustee occupies the same position as the directors of the corporation. Judicial adoption of such a view might permit the bankruptcy court to exercise jurisdiction over the trust corpus, rather than merely over the debtor's rights to receive income from the trust.

However, it should be noted that not all trusts are subject to the bankruptcy court's jurisdiction. "If the trust is created so as to be inalienable by the [beneficiary] . . . the trustee in bankruptcy generally takes nothing."<sup>54</sup> Thus, the trustee is not entitled to reach the bankrupt beneficiary's interest in a spendthrift trust,<sup>55</sup> if such

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50. *Id.* at 340-41.

51. See text accompanying notes 45-48 *supra*.

52. 4A COLLIER, BANKRUPTCY ¶ 70.26 (14th ed. 1976). See also *Thumess v. Von Hoffman*, 109 F.2d 293 (3d Cir. 1940); *Suskin & Berry, Inc. v. Rumley*, 37 F.2d 304 (4th Cir. 1930); *Sommers v. Timely Toys, Inc.*, 110 F. Supp. 844 (E.D.N.Y. 1953); *In re Skodnick*, 91 F. Supp. 529 (E.D.N.Y. 1950); *Brown v. Barker*, 68 App. Div. 592, 74 N.Y.S. 43 (4th Dept. 1902).

53. See 4A COLLIER, BANKRUPTCY ¶ 70.26 (14th ed. 1976).

54. *Id.*

55. *Danning v. Lederer*, 232 F.2d 610 (7th Cir. 1956); *Ashton v. Sentney*, 145 F.2d 719

trust is valid according to applicable state trust law.<sup>56</sup>

## B. Federal Judicial Authority To Exercise Cy Pres Powers

Once the bankruptcy court obtains jurisdiction over a specific trust interest, the question remains whether it may conduct a cy pres proceeding and modify the conditions upon which the property is held. While the cy pres power has been said to be an inherent power of all courts of equity,<sup>57</sup> this alone cannot be conclusive on the issue of the bankruptcy court's capacity to modify trusts.<sup>58</sup> In New York, jurisdiction over testamentary trusts is by statute vested in the surrogate's court,<sup>59</sup> while inter vivos trusts are administered by the supreme court,<sup>60</sup> yet this grant of jurisdiction to the New York courts cannot determine the jurisdiction of courts of bankruptcy. Even though New York law would likely be applied by the bank-

(9th Cir. 1944); *Jones v. Harrison*, 7 F.2d 461 (8th Cir. 1925), *cert. denied sub nom. Jules v. Ready*, 270 U.S. 652 (1926).

56. New York provides by statute that all trusts to receive the rents and profits from real property or the income from personal property are spendthrift in nature. N.Y. EST., POWERS & TRUSTS LAW § 7-1.5(a)(1) (McKinney 1967). However, the creator may provide for the transferability or assignability of income in the instrument creating the trust. *Id.*

57. See *Fontain v. Ravenal*, 58 U.S. (17 How.) 369, 386 (1854); 4 SCOTT ON TRUSTS § 399 (3d ed. 1967).

58. Section 2(a) of the Bankruptcy Act indicates that the bankruptcy court has jurisdiction both in law and in equity. 11 U.S.C. § 11(a) (1970). The Supreme Court has acknowledged this fact, stating that the bankruptcy court is "essentially [a court] of equity, and [its] proceedings [are] inherently proceedings in equity." *Local Loan Co. v. Hunt*, 292 U.S. 234, 240 (1934). Furthermore the court has noted that "[p]roceedings in bankruptcy generally are in the nature of proceedings in equity . . ." *Bardes v. Hawarden Bank*, 178 U.S. 524, 535 (1900). See also *In re Lahongrais*, 5 F.2d 899, 901 (1st Cir. 1925); *In re Rochford*, 124 F. 182, 187 (8th Cir. 1903); *Swarts v. Siegal*, 117 F. 13, 16 (8th Cir. 1902); *Guariglia v. Community Nat'l Bank & Trust Co.*, 382 F. Supp. 758, 761 (E.D.N.Y. 1974), *aff'd*, 516 F. 2d 896 (2d Cir. 1975); *Inland Security Co. v. Estate of Kirshner*, 382 F. Supp. 338, 349 (W.D. Mo. 1974); *In re Swofford Bros. Dry Goods Co.*, 180 F. 549, 553 (W.D. Mo. 1910).

59. N.Y. EST., POWERS & TRUSTS LAW § 8-1.1(c) (McKinney 1967). This jurisdiction is exercised concurrently with the supreme court. *Id.*

Federal courts are said to have no jurisdiction in matters of probate; this stems in part from the common law treatment of decedents' estates. Probate matters were not considered matters of "law" or "equity" at the time of the ratification of the Constitution, and were traditionally in the province of the English ecclesiastical courts. *In re Broderick's Will*, 88 U.S. (21 Wall.) 503, 509-10 (1874). However, since cy pres in many states is not solely a function of probate courts, it would be unreasonable to deny summarily the power of federal courts to act upon funds created by will as opposed to those created by inter vivos agreement.

60. N.Y. Est., Powers & Trusts Law § 8-1.1(c) (McKinney 1967).

ruptcy court in applying cy pres relief,<sup>61</sup> a federal court could hardly look to state law in order to establish its own jurisdiction.

Federal courts presented with applications for cy pres relief have reached different conclusions regarding both their authority to grant such relief and the proper body of law to be used in making such a determination.

The foremost case, *Pennsylvania v. Brown*,<sup>62</sup> was an action brought pursuant to the Civil Rights Act of 1866.<sup>63</sup> Plaintiffs sought to eliminate racial restrictions governing admission to Philadelphia's Girard College, a charitable educational institution established and maintained by a testamentary trust. Referring to Pennsylvania law, the district court held that it had pendent jurisdiction of the plaintiff's state claim and could exercise cy pres power over the trust.<sup>64</sup>

Judicial *cy pres* is part of the "regular and inherent jurisdiction [of] a court of equity in relation to trusts . . ." If [the complaint] were to state a valid *cy pres* claim—and on what we presently intimate no view—this court would have jurisdiction to grant relief.

While this result has not been seriously attacked, the cases upon which the court relied for its holding do not form the strong precedential underpinning suggested by the firmness of the court's language. Two of the cases relied on in *Brown* were mid-nineteenth century decisions of the Supreme Court—*Fontain v. Ravenel*<sup>65</sup> and

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61. Since the interpretation of wills and trusts and the resultant discernment of the donor's intent is largely a function of state law, a federal court would undoubtedly look to state law for decisional precedents. See *Evans v. Abney*, 396 U.S. 435, 437, 444 (1970) (noting that the construction of wills is essentially a state question and that the determination of whether to apply the doctrine of cy pres is traditionally a state function).

It may well be that state law looks solely to the conscience of the court on the issue of cy pres. But since the creation and governance of trusts is so generally a creature of state law, it might be appropriate to look to that source. Such a decision would be sensibly grounded in the principles of comity underlying *Erie v. Tompkins*, 304 U.S. 64 (1938). See generally Friendly, *In Praise of Erie—and of the New Federal Common Law*, 39 N.Y.U. L. REV. 383, 392-98 (1964). Examination of the tenth amendment to the Constitution suggests a similar view. U.S. CONST. amend. X.

62. 260 F. Supp. 323 (E.D. Pa. 1966), *vacated in part on other grounds*, 373 F.2d 771 (3d Cir. 1967).

63. 42 U.S.C. § 1981 (1970).

64. 260 F. Supp. at 337.

65. 58 U.S. (17 How.) 369 (1854).

*Vidal v. Girard's Executors*<sup>66</sup>—while third case, *Smith v. Moore*,<sup>67</sup> was decided by the Fourth Circuit Court of Appeals in 1965.

*Vidal v. Girard's Executors*<sup>68</sup> involved the same trust before the court in *Brown*. The testator bequeathed a fund to the City of Philadelphia to establish a school for indigent male youths. Plaintiffs attacked the validity of the trust, claiming that the law could not recognize trusts established for the benefit of an indefinite class of beneficiaries.<sup>69</sup> The critical issue before the court was whether the repeal of the English Statute of Charitable Uses,<sup>70</sup> which had been repealed in Pennsylvania, divested the courts of that state of cy pres powers. One Pennsylvania Supreme Court decision seemed to indicate that it had, at least with respect to "prerogative" cy pres.<sup>71</sup> Mr. Justice Story, writing for the Court, examined the statute's history and noted that prerogative cy pres powers—used to cure flaw in charitable trusts—had been exercised by English Courts of Chancery long before and independent of the statute.<sup>72</sup> He concluded that the statute merely codified the common law concept of cy pres and that the repeal did not affect the court's power to remove abhorrent trust provisions. To this extent, he indicated that cy pres was an inherent power of courts of equity.<sup>73</sup>

The bequest in *Fontain v. Ravenel*<sup>74</sup> involved a life estate, with a remainder to be paid over "[to] such charitable institutions in Pennsylvania . . . as [my executors] may deem most beneficial to mankind . . ." <sup>75</sup> The executors failed to exercise their power of appointment over the fund, and the holder of the life estate (the last surviving executrix) made no reference to the power in her will. The Attorney General of Pennsylvania petitioned a federal court to apply the cy pres doctrine in order to maintain the charitable pur-

66. 43 U.S. (2 How.) 126 (1844).

67. 343 F.2d 594 (4th Cir. 1965).

68. 43 U.S. (2 How.) 127 (1844).

69. While the beneficiaries of a trust must be identified with reasonable certainty, an opposite rule obtains in the case of charitable trusts. Such trusts are said to be for the benefit of all mankind, and so the beneficiaries *must* be an identifiable class of persons. *In re Syracuse Univ.*, 3 N.Y.2d 665, 148 N.E.2d 671, 171 N.Y.S.2d 545 (1958).

70. 43 Eliz. I, c. 2 (1601).

71. *Methodist Church v. Remington*, 1 Watts (Pa.) 218 (1833).

72. 43 U.S. (2 How.) at 196.

73. *Id.*

74. 58 U.S. (17 How.) 269 (1854).

75. *Id.* at 382.



pose of the gift. The Supreme Court, in denying the requested remedy on appeal, reached a conclusion seemingly contradictory to its earlier decision in *Vidal*.<sup>76</sup> But the court founded on the distinction between cy pres as a judicial power and cy pres as a prerogative function of the Chancellor:<sup>77</sup>

The courts of the United States cannot exercise any equity powers, except those conferred by acts of congress, and those judicial powers which the high court of chancery in England, acting under its judicial capacity as a court of equity, possessed and exercised, at the time of the formation of the Constitution of the United States. Powers not judicial, exercised by the chancellor merely as the representative of the sovereign, and by virtue of the king's prerogative as *parens patriae* are not possessed by the circuit courts.

Noting that "[c]hancery will not compel the execution of a mere naked power,"<sup>78</sup> the court held the bequest to be unenforceable; to carry out the testator's charitable intent would require the exercise of prerogative cy pres, which was not within the ambit of ordinary and inherent equity powers.<sup>79</sup> In reaching its decision, the court also considered Pennsylvania state law, which denied the existence of the cy pres doctrine in that state.<sup>80</sup>

Two concurring opinions in *Fontain* further confuse the jurisdictional issue. Mr. Chief Justice Taney was of the opinion that state law should not have been consulted, since it could only increase the authority of federal court within the boundaries of that state's judicial power.<sup>81</sup> By this reasoning, prerogative cy pres, if available as a remedy, belonged to the state as a sovereign entity, and no state could confer its executive power on the federal judiciary. Mr. Justice Daniel, in his concurrence, expressed the view that jurisdiction to administer cy pres relief was inherent in the equitable jurisdiction of the federal courts.<sup>82</sup> Yet he concurred in the majority opinion for

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76. See text accompanying notes 68-73 *supra*. It should be noted that the Court in *Fontain* did not reach the issue of whether the federal courts could exercise cy pres functions which were traditionally considered judicial in nature.

77. 58 U.S. (17 How.) at 384.

78. *Id.* at 385.

79. *Id.* at 389.

80. In *Methodist Church v. Remington*, 1 Watts (Pa.) 218 (1833), the court held that the English Statute of Charitable Uses, of which the doctrine of cy pres is a function, did not codify the common law with the result that the blanket repeal of English statutes in Pennsylvania left the doctrine without force there.

81. 58 U.S. (17 How.) at 391 (Taney, C.J., concurring).

82. *Id.* at 396 (Daniel, J., concurring).

the reason that a naked power does not create an enforceable trust.<sup>83</sup>

In *Smith v. Moore*,<sup>84</sup> the district court was faced with a bequest made for the purpose of constructing a hospital. However, the amount of the gift was insufficient for that purpose. The court, whose jurisdiction over the parties was based on diversity of citizenship, assessed its power to administer *cy pres* by looking to the law of the state in which it sat. The court concluded that the state would avoid frustration of the bequest by granting *cy pres* relief.<sup>85</sup>

Once having determined the validity of the trusts and the application of *cy pres*, it is the opinion of this court that the state court, on appropriate petition by the fiduciary, should resolve the remaining issues and allocate the trusts under *cy pres* [since] [s]uch action would permit parties in interest to be heard.

The Court of Appeals for the Fourth Circuit reversed the district court's decision.<sup>86</sup> Without exploring the question of subject matter jurisdiction, the court directed the trustees to divert the funds to the creation of a wing for an already existing hospital.<sup>87</sup>

In reaching its decision, the court of appeals employed an analysis based on the doctrine of "equitable approximation."<sup>88</sup> The distinction between this novel "doctrine" and judicial *cy pres* in the context of a charitable trust is thus not easy to comprehend. Nevertheless, to the court of appeals, the distinction was vital.

Reference was first made to the Virginia rules concerning *cy pres* and it was stated that it "is in the main stream of the confusion, contradiction and equivocation attaching to the history of the doctrine."<sup>89</sup> The court then avoided this morass by seizing on the concept of equitable appropriation and, without further reference to Virginia law, this concept was found to be inherent in courts of equity and applied to the case at bar. Although the proper body of decisional authority was never identified, the court's reference to the Virginia law of *cy pres* supports the contention that it considered itself bound by state law.<sup>90</sup>

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83. *Id.* at 398. See text accompanying note 78 *supra*.

84. 343 F.2d 594 (4th Cir. 1965).

85. 225 F. Supp. 434, 449 (E.D. Va. 1963).

86. 343 F.2d 594, 604 (4th Cir. 1965).

87. *Id.*

88. *Id.* at 602.

89. *Id.* at 599.

90. *Id.* at 604.

An approximation of prerogative cy pres had developed in federal courts with respect to racial and religious discrimination in charitable trusts. Courts using a "state action" rationale<sup>91</sup> have excised discriminatory trust features on the grounds that they violate the equal protection clause of the fourteenth amendment.<sup>92</sup> One commentator has noted:<sup>93</sup>

The state action concept is not wielded sparingly; peripheral governmental involvement is often enough to necessitate the dismantling of exclusionary trust instructions. Generally, the trust property will then be preserved for charitable purposes through application of the doctrines of *cy pres* or deviation, unless the testator has unmistakably manifested an intention that a gift-over or lapse occur in the event the discrimination is disallowed.

Two modes of state action have been articulated with respect to trusts: first, judicial state action, based on the actions of the judiciary in enforcing a discriminatory trust;<sup>94</sup> and second, a "significance" test, determined by evaluating the extent of obvious state participation<sup>95</sup> in the operation of a discriminatory trust. Exclusionary trust provisions may be stricken from a charitable trust when either form of state action is found, but all nondiscriminatory features of the trust remain in operation.

*Pennsylvania v. Brown*<sup>96</sup> furnishes a prime example of discriminatory trust modification. The trust in that case provided for the establishment of a school for white males.<sup>97</sup> Seven blacks brought suit

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91. Racially discriminatory provisions in a trust are almost invariably invalidated and rendered inoperative. However, provisions which discriminate in favor of religious groups may be allowed to stand under certain circumstances.

Trusts directly in support of religion, such as a fund to maintain a parish church, are unanimously accepted as charitable and apparently immune from constitutional attack. On the other hand, when religious restrictions are affixed to a trust providing a service or benefit ordinarily available to the general public, the fourteenth amendment may be offended. Adams, *Racial and Religious Discrimination in Charitable Trusts: A Current Analysis of Constitutional and Trust Law Solutions*, 25 CLEV. ST. L. REV. 1, 20 (1976).

92. U.S. CONST. amend. XIV.

93. Adams, *supra* note 91, at 1.

94. See *Shelley v. Kraemer*, 334 U.S. 1 (1948).

95. See *Burton v. Wilmington Parking Auth.*, 365 U.S. 715 (1961). See also Nelkin, *Cy Pres and the Fourteenth Amendment: A Discriminating Look at Very Private Schools and Not So Charitable Trusts*, 56 GEO. L.J. 2722 (1967).

96. 260 F. Supp. 358 (E.D. Pa. 1966), *vacated in part and remanded*, 373 F.2d 771 (3d Cir. 1967), 270 F. Supp. 782 (E.D. Pa. 1967), *aff'd*, 392 F.2d 120 (3d Cir.), *cert. denied*, 391 U.S. 921 (1968).

97. 392 F.2d at 120.

seeking admission to the school and asking the district court to remove the racial restrictions by imposing cy pres modification on the trust.<sup>98</sup> The district court deferred consideration of the cy pres claim, although indicating that it had authority to impose cy pres.<sup>99</sup> On appeal from a later remand, the Court of Appeals for the Third Circuit found that state court enforcement<sup>100</sup> of the exclusionary trust provisions constituted judicial and significant state action in contravention of the fourteenth amendment, and ordered elimination of the exclusionary trust features.<sup>101</sup>

Thus, two grounds for federal exercise of cy pres may be articulated. Some courts have recognized the power as inherent in a court of equity; civil rights decisions have indicated that federal courts may alter trusts afflicted with discriminatory state action. It should be noted that excising discriminatory trust provisions on the basis of prerogative cy pres may require the court to consider its authority to administer judicial cy pres.

### C. The Bankruptcy Court, Cy Pres, and Public Policy Considerations

Although the cases do not enunciate a clear and consistent rationale for the assumption of such jurisdiction, some federal courts have acknowledged cy pres as one of their inherent equity powers.<sup>102</sup> In addition, they have of their own authority modified exclusionary trust provisions.<sup>103</sup> While the states and their judiciaries are said to have a special interest in the administration of trust properties located within their borders,<sup>104</sup> this interest may not be violated so

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98. *Pennsylvania v. Brown*, 373 F.2d 771 (3d Cir. 1968).

99. 260 F. Supp 323, 357-58 (E.D. Pa. 1966).

100. The racially discriminatory provisions of the trust had been invalidated more than a decade earlier by the Supreme Court. *Pennsylvania v. Board of Directors*, 353 U.S. 230 (1957). The Court found state action in the fact that the trust executors were city officials and held that the trust violated the fourteenth amendment's equal protection clause. *Id.* at 231. On remand the Pennsylvania Supreme Court did not remove the exclusionary provisions from the trust, but instead referred the matter to the Orphan's Court of the County of Philadelphia which removed the municipal executors and replaced them with private citizens. 392 F.2d at 122-23. On appeal, the actions of the Pennsylvania courts in enforcing the discriminatory trust were held to be judicial and significant "state action." 392 F.2d at 125.

101. 392 F.2d at 125.

102. See text accompanying notes 62-85 *supra*.

103. See text accompanying notes 86-96. *supra*.

104. See *Hutchinson v. Ross*, 262 N.Y. 381 (1933).

long as the federal courts apply state trust law.<sup>105</sup> However, before the bankruptcy court may be permitted to employ *cy pres* as an instrument of reorganization, some policy problems must be considered.

Alteration of trust terms by the bankruptcy court may be viewed by some as subverting the purposes of charitable trusts. Such trusts are created in order to benefit indigent or needy individuals; but in a reorganization the bankruptcy court's prime concerns are to apply the debtor's assets for the optimum benefit of creditors.<sup>106</sup> There is perhaps justified fear that in a Chapter XI proceeding the interests of the trust beneficiaries might be subordinated to creditor demands. However, two countervailing factors exist. First, the *cy pres* doctrine may not be applied unless the terms of the trust have become impossible or impractical to enforce. Absent alteration of the trust, the charitable nature of the gift (and the creator's intention) may be lost, along with the general charitable intent of the donor. Thus, trust law provides a check on unbridled application of the *cy pres* doctrine. Secondly, a failure of a Chapter XI debtor to propose a plan of composition acceptable to his creditors may result in a court ordered liquidation of the debtor's operations.<sup>107</sup> From a policy standpoint, the continued existence of a hospital, orphanage, or similar institution is of greater public benefit than the elimination of such facilities or shifting their burdens to municipal agencies.

Judicial economy is a second consideration supporting the use of *cy pres* by bankruptcy courts. At present, a charitable corporation may find it difficult to present a comprehensive plan for the shifting of restricted trust funds to any single forum. Allowing the bank-

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105. See, e.g., *Smith v. Moore*, 343 F.2d 594 (4th Cir. 1965), where a federal district court applied state law in determining whether the *cy pres* doctrine should be applied to a Virginia trust.

106. One authority noted that:

Chapter XI gives an honest debtor the opportunity to restudy his problems and a second chance to remedy his difficulties so that his business man can be put on a sound financial basis. For the creditor, it means that a higher dividend may be possible. . . .

LEVIN AND WEINTRAUB, PRACTICAL GUIDE TO CHAPTER XI OF THE BANKRUPTCY ACT 3 (1975). However, it should be remembered that if a creditor's demands are not met, the bankruptcy court can and will order liquidation of the debtor's assets. 11 U.S.C. § 277 (1970); BANKR. R. 11-42(b).

107. See note 101 *supra*.

ruptcy court to modify an entire endowment would achieve two advantages—first, there would be an obvious saving of time and expense to the judicial system, the trustee, and the debtor's estate; and second, the bankruptcy court, in deciding in what fashion each component of the endowment should be altered, would do so with a view toward developing a comprehensive plan of reorganization.

#### IV. Conclusion

Despite the absence of direct statutory authority or clear judicial precedent, it would appear that a federal bankruptcy court may administer *cy pres* relief. Of course, the court must satisfy the other elements of its jurisdiction before this authority may become operative. But once a charitable organization comes under the bankruptcy court's jurisdiction, judicial *cy pres* seems a reasonable weapon to find in the arsenal of equity.

Restructuring a debtor's financial posture with the aid of endowment funds is likely to benefit all parties concerned. By completing a full-scale reorganization in a single forum, significant savings of time and expense will be achieved, and much needed institutions will not be forced to close, causing hardships to those who rely on them and subverting the intent of those who supported them. In addition, by affording more comprehensive relief, the bankruptcy court will enhance the success and efficacy of Chapter XI reorganizations, and encourage financially distressed charities to reform their operations at an earlier stage. Assuming jurisdiction over charitable trusts would entail considerable work for the bankruptcy court; but under the right circumstances the potential for social good may more than justify the added labor.