4th Circ. Nixes Release Approvals In Charity's Ch. 11

By **Roxanne Palmer**

Law360, New York (December 12, 2011, 7:16 PM ET) -- The Fourth Circuit on Friday ruled that a Virginia federal court erred in affirming National Heritage Foundation Inc.'s reorganization plan, saying a bankruptcy court had not justified its approval of provisions releasing certain third parties from liability.

The nondebtor release, injunction and exculpation provisions in question prevented potential claimants from asserting claims against the NHF and certain officers and directors, as well as the official committee of unsecured creditors. Plaintiffs-appellants and former NHF donors John R. Behrmann and Nancy Behrmann challenged the reorganization plan, but U.S. District Judge Claude M. Hilton affirmed the provisions in August 2010.

Release provisions such as those in the NHF plan are sometimes permissible, but the bankruptcy court must find sufficient enough facts to support them, a three-judge panel for the Fourth Circuit found Friday.

"Because the bankruptcy court in this case failed to make such findings, the district court erred in affirming the bankruptcy court's confirmation order," the opinion said.

The bankruptcy court had found that the release provisions were essential to the NHF's reorganization and appropriate to the foundation's unique circumstances, but provided no factual findings to support its conclusion, according to the panel.

Without such information, "the court's conclusions could apply just as well to any number of reorganizing debtors," the opinion said.

The panel vacated the district court's judgment and remanded the case in order to allow the bankruptcy court to produce specific factual findings supporting its ruling on the release provisions, according to the opinion.

Erika L. Morabito of Foley & Lardner LLP, an attorney for the NHF, said the Fourth Circuit's decision was consistent with the foundation's legal position.

"We also feel strongly that on remand the bankruptcy court will be able to set forth specific factual findings supporting its initial conclusions that are fully supported by the existing record," Morabito told Law360 on Monday.

Representatives for the Behrmanns could not immediately be reached for comment Monday.

The NHF was set up in 1994 to centralize administrative activities and make it easier for individual donors to set up their own charitable funds.

The foundation and its CEO John T. Houk II solicited the Behrmanns to set up such a fund, which they did in 1996. They ultimately donated $1.09 million to set up the Highbourne Foundation, the stated purpose of which was to prevent cruelty to children and animals, through one of the NHF's donor-advised funds, according to court documents and tax records collected by the National Center for Charitable Statistics.

But in 2009, the foundation filed for Chapter 11 bankruptcy and seized money in the donor-advised funds, including $650,000 from Highbourne, to pay off creditors, according to the plaintiffs.

The Behrmanns objected to these moves in the bankruptcy proceeding, but the NHF "resisted" them, arguing that the Behrmanns had given up all their rights to their donations when they set up their fund with the foundation, the plaintiffs said.

In addition to challenging the release provisions of the reorganization plan, the Behrmanns also sued McGuireWoods LLP in Virginia federal court in April, alleging the firm threw unsecured creditors like them under the bus when it drafted the foundation's reorganization plan.

Judges William B. Traxler, G. Steven Agee and Albert Diaz sat on the panel for the Fourth Circuit.

The Behrmanns are represented by Glenn W. Merrick of G.W. Merrick & Associates LLC and Gregory H. Counts of Tyler Bartl Ramsdell & Counts PLC.

The NHF is represented by Erika L. Morabito of Foley & Lardner LLP.

The case is Behrmann et al. v. National Heritage Foundation Inc. et al., case number 10-02015, in the U.S. Court of Appeals for the Fourth Circuit.

--Additional reporting by Eric Hornbeck. Editing by Andrew Park.