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Judge to determine if irregularities were intentional

By **Sandi Dolbee and Mark Sauer**
UNION-TRIBUNE STAFF WRITERS

August 1, 2007

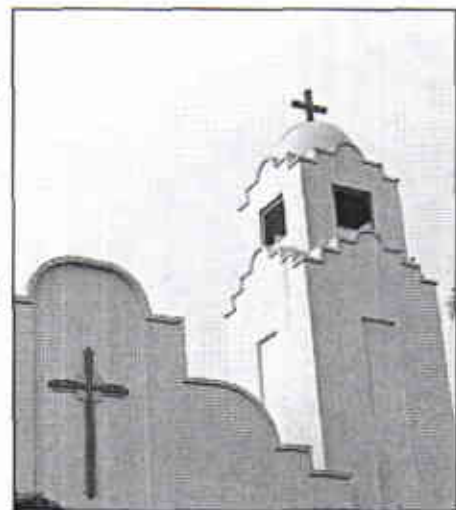
A sweeping financial review has found that the Diocese of San Diego made conflicting statements about its assets, that Catholic parishes withheld millions in surplus funds and that churches hid money in two instances.

Attorneys representing about 150 victims of sexual abuse by priests and other church personnel seized upon the findings by court-appointed financial expert R. Todd Neilson as proof that the diocese is not being honest in its bankruptcy case.

"(Bishop Robert Brom) and his legal advisers have demonstrated their utter contempt for the bankruptcy court and the legal system," said Irwin Zalkin, an attorney representing about 30 percent of those who filed sexual-abuse lawsuits against the diocese here.

"This is in keeping with the contempt for the law they demonstrated by allowing children to be raped and abused for years with impunity," he said yesterday.

But diocese attorney Micheal Webb downplayed the 175-page report



K.C. ALFRED / Union-Tribune
The case involving the Diocese of San Diego marks the first time in the five bankruptcy cases of U.S. dioceses that a judge has ordered such a rigorous outside financial review.

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released late Monday as containing "a small number of problems, all of which have been corrected or are in the process of being corrected."

In a statement, Webb encouraged Catholics and the public "to listen to and rely only on the comments of Mr. Neilson himself."

For a copy of the court-appointed financial expert's report, go to uniontrib.com/more/diocesereport.

Neilson, a former FBI agent and recognized expert in bankruptcy and forensic accounting, was appointed in April by federal bankruptcy Judge Louise DeCarl Adler to examine nearly 1,000 bank accounts held by the diocese and its 98 parishes.

This is the first time in the five bankruptcy cases involving U.S. dioceses that a judge has ordered such a rigorous outside financial review. Legal experts said Adler could respond to Neilson's findings in a range of ways.

If Adler deems the financial irregularities to be mistakes and oversights, she could do nothing. But if she determines there has been intentional deception, she could dismiss the bankruptcy, appoint a trustee to take over diocese finances, ask the U.S. Attorney to open a criminal-fraud investigation or ask the financial expert to expand his review, experts said.

The judge could also decide to start releasing the sexual-abuse lawsuits, which have been put on hold by the bankruptcy, for trial in state court, said Lynn LoPucki, a UCLA law professor specializing in bankruptcy issues. In that case, he said, "the process is the penalty."

Neilson is scheduled to be questioned at an Aug. 23 hearing before Adler.

In his report, Neilson praises church officials, pastors and parish employees for their cooperation. But he cites certain "purposeful attempts" to circumvent federal law and "openly questionable activities" relating to diocese bankruptcy filings and what he calls its "Byzantine" financial system.

The report, which notes that about \$165 million flows through the diocese annually, contains these key findings:

Assertions by diocese officials in bankruptcy court that tens of millions of dollars in assets are held in trust for the various parishes and not owned by the diocese "were in direct contradiction to the assertions" made in recent years to banks and bond-market investors. Under Catholic church law, officials said, the parishes are held in trust by the diocese.

Two parishes in Imperial County tried to conceal nearly \$350,000 from the bankruptcy court.

Many parishes and schools are not following the policy of depositing surplus funds with the diocese's banking system. In the 74 schools and parishes audited in the report, Neilson estimated that nearly \$22 million was not being sent to the diocese.

A \$19 million deduction from main accounts known as the "Diocese

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Bank” just before the Feb. 27 bankruptcy filing appears to be missing from financial statements filed with the court. An additional \$12 million in interest earnings was shifted from the Diocese Bank into an account that cannot be used to settle sexual-abuse claims.

Webb, the diocese attorney, said in a statement he is not surprised that Neilson's report found “some room for improvement.”

“However, on the whole, his report demonstrates that the cash-management system of the diocese is effective and competently processes and monitors the finances of the diocese, parishes and schools,” Webb said. “The report clearly states that all funds are accounted for.”

But Neilson noted that there is “an incredible array” of accounting methods in churches and schools, resulting in the diocese being “woefully unaware” of finances at the parish level.

Also coming under criticism was the accounting firm Ernst & Young, which certified for bankers and bond investors that the diocese owned ample parish assets required to secure loans for the construction of new high schools. Officials for the accounting firm declined to comment yesterday about the report.

Perhaps the harshest language was reserved for two Imperial County churches.

Our Lady of Guadalupe in Calexico “deliberately concealed” nearly \$50,000 at the time of the bankruptcy petition, Neilson's report said. St. Mary in El Centro withdrew and converted \$290,000 into cashiers checks that were kept in a church safe. In both cases, the funds have been re-deposited.

Even a May directive from the diocese's vicar general, Monsignor Steven Callahan, didn't persuade parishes to follow the policy of depositing surplus funds with the diocese. “Most parishes continued to ignore the diocesan policy, the direction of this memo and their commitment to the court,” Neilson wrote.

One in particular, Our Lady of Mt. Carmel in San Ysidro, drew attention because the relatively modest church had \$1.2 million in its bank accounts when the diocese bankruptcy was filed. Neilson said this demonstrated “a willful disregard” for the diocese's procedures.

Priests at those parishes did not return phone calls. Susan Boswell, lead bankruptcy attorney for the diocese, would not comment on the particulars of the findings, saying, “I really think the report speaks for itself.”

Frederick Naffziger, a business law professor at Indiana University South Bend, was taken aback by the two parishes caught concealing money from the bankruptcy court. “I'm a little surprised at the magnitude.”

He suggested that the judge could order priests and others from those churches to appear in court and explain why they shouldn't be held in contempt.

“Those kind of stand out as sore thumbs of defiance of the court and the creditors,” Naffziger said. The court will want “a pretty thorough

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explanation.”

UCLA's LoPucki called Neilson's conclusions regarding the pastors' actions, “a finding of concealment, a finding of a crime.”

Also disturbing, Naffziger said, was the degree to which parishes are not complying with the diocese's surplus-funds policy.

“One explanation is kind of nefarious – that the parishes knowing bankruptcy is coming are trying to hide assets and cheat the creditors,” Naffziger said. “A more innocent explanation may be that that practice has gone on for years.”

LoPucki said Neilson's “most important finding” was that the bishop and other church officials switched positions regarding ownership of parish assets depending upon its needs at the time.

“The bishop treated parish money as belonging to the diocese when he wanted to borrow against these assets,” LoPucki said. “But when the diocese filed for bankruptcy, suddenly he claims the parish assets are separate.”

Naffziger is less bothered by the the diocese's mixed messages about whether parishes are assets.

The diocese characterizes them as assets for loans and audits, he said. However, in court, the diocese insists they are not assets because under church law the diocese is only holding them in trust for the parishes.

“It isn't deceptive,” he added. “It's just two different systems with two different rules. Ultimately, if they do not settle this, the bankruptcy court is going to have to decide which set of rules is applicable.”

A spokesman for a newly formed group of Catholic churchgoers said he sees this report as proving that “all the money comes from the parishioners.” Patrick Hazel, a representative of the Parishioners for the Churches and Schools, said the report also shows “these parishes tended to act very independently.”

He added: “I didn't see anything in the report saying the diocese directed the parishes to act that way.”

The million-member diocese has offered to settle victims' lawsuits for \$95 million, about half of what the plaintiffs' attorneys are seeking for their clients.

At a news conference yesterday for victims and supporters, Victoria Martin criticized the bishop for filing for Chapter 11 bankruptcy protection and putting the trials on hold.

“He's not wearing me down,” said Martin, 60, who says she was raped by a diocesan priest on her 13th birthday. “The only thing he's doing is spending more money that belongs to faithful Catholics.”

Naffziger suggested Bishop Brom may suffer the most damage from Neilson's findings.

“It (has) given the bishop a credibility problem,” he said. “Not that the

bishop himself has lied, but a credibility problem from the point of view that the bishop may not be relied upon because his inferiors may be lying to the court."

Neilson and his team of accountants have billed more than \$750,000 so far, which the diocese must pay. He said his investigation is not yet complete.

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By Abuse Survivor on 08/01/2007

Never thought it would be so difficult to seek justice from a religious institution that professes high moral character as an essential part of being a member of the hierarchy.

A religious institution should provide guidance, in how to be a integral part of society, and abide by the same laws, that give religions their freedom.

To pick and choose which rules apply, and provide the best outcome is disingenuous. This is the constantly how the Diocese runs its operations.

They pick and choose which laws to follow - Cannon or Civil,

re: Parish Ownership

In Pauma Valley Parish litigation the Diocese states "we own the parishes"

In Banckruptcy Court, "We don't own the Parishes"

re: Diocesan Bank

In loan documents, it's used as collateral, and stated as Diocese money.

In Bankruptcy, it's not our money, it belongs to the parishes.

re: Childhood Sexual Abuse

at one parish, Fr. Robier has been raping children, keep him away from children