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Rejecting Collective Bargaining Agreements Under Section 1113 of the Bankruptcy Code - Judicial Precision or Economic Reality?

Joseph L. Cosetti

Stanley A. Kirshenbaum

REJECTING COLLECTIVE BARGAINING AGREEMENTS UNDER SECTION 1113 OF THE BANKRUPTCY CODE—JUDICIAL PRECISION OR ECONOMIC REALITY?

*The Honorable Joseph L. Cosetti**
*Stanley A. Kirshenbaum***

I. INTRODUCTION

In *NLRB v. Bildisco and Bildisco*,[1] the United States Supreme Court held that a debtor in possession in a Chapter 11 bankruptcy proceeding may unilaterally terminate its collective bargaining agreement.[2] Further, the Supreme Court decided that such actions were not unfair labor practices and set forth the standard a debtor in possession must meet to reject its union contract.[3] Subsequently, a firestorm erupted in the organized labor community. Union officials feared a deluge of Chapter 11 bankruptcies by companies seeking to rid themselves of their obligations under collective bargaining agreements.[4] On that same day, Congressman Rodino of New Jersey proposed legislation "to clarify the circumstances under which collective bargaining agreements may be rejected."[5] Even prior to the Courts decision in the *Bildisco* case, organized labor sought relief from Congress in response to unilateral contract rejections following Chapter 11 filings by such recognized companies as Braniff Airlines, Continental Airlines, Wilson Foods Corp. and Rath Packing Com-

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* B.S, 1951, M.B.A., 1953, Ohio State University; J.D., 1975, Duquesne University School of Law; Currently Chief Judge, United States Bankruptcy Court for the Western District of Pennsylvania.

** B.A., 1977, University of Pittsburgh; J.D., 1985, University of Pittsburgh School of Law; Currently Law Clerk to Judge Cosetti.

1. 465 U.S. 513 (1984).
2. *Id.* at 527-34.
3. *Id.*
4. Comment, *From Legislation to Consternation: Has Section 1113 Really Changed Bildisco,* 12 DEL. J. CORP. L. 167, (1987); Gibson, *The New Law of Rejection of Collective Bargaining in Chapter 11: An Analysis of 11 U.S.C. § 1113,* 58 AMER. BANKR. L.J. 325, 326 (1984).
5. H.R. 4908, 98th Cong., 2d Sess., 130 Cong. Rec. H809 (daily ed. Feb. 22, 1984).

pany, and the threatened bankruptcy rejection by Eastern Airlines.[6] Following the *Bildisco* decision, organized labor intensified its lobbying efforts, while business and creditor interests vigorously lobbied Congress to sustain the *Bildisco* decision.[7]

The legislative battle to reshape the law of the rejection of collective bargaining agreements occurred during an uncertain and eventful period of bankruptcy jurisprudence. Two years earlier, in June 1982, the Supreme Court had declared the system of bankruptcy court jurisdiction unconstitutional and gave Congress an opportunity to redesign it.[8] Thus, the attempt to overrule *Bildisco* by legislation became emeshed with the legislation designed to resolve the constitutionality of the jurisdiction of bankruptcy courts. All of the resultant 1984 legislation lacks skillful draftsmanship. Section 1113 is no exception.

Section 1113 created the procedure by which a debtor[9] must first propose modifications in the collective bargaining agreement to the authorized representative of the debtor's employees. The proposal must be based upon "the most complete and reliable information available"[10] and must contain only "necessary modifications" which treat "all creditors, the debtor and all of the affected parties ... fairly and equitably."[11] The debtor must provide "relevant information" to enable the employees' representative to evaluate the proposal.[12] Section 1113 also provides for an expedited hearing

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6. Rosenberg, *Bankruptcy and the Collective Bargaining Agreement—A Brief Lesson in the Constitutional System of Checks and Balances*, 58 AMER. BANKR. L.J. 293, 305-06, 312 (1984). On February 9, 1984, 15 days before the *Bildisco* decision was issued, Congressman Simon introduced H.R. 4858 to "amend the National Labor Relations Act and the Railway Labor Act to modify the circumstances under which certain collective bargaining agreements ... may be rejected in a case under Chapter 11 of Title 11 of the United States Code." H.R. 4858, 98th Cong., 2d Sess., 130 Cong. Rec. H707 (daily ed. Feb 9, 1984).

7. Rasnic, *Labor's Return from Waterloo: Congressional Response to NLRB v. Bildisco*, 23 AM. BUS. L.J. 633, 645-46 (1986); Rosenberg, *supra* note 6, at 312.

8. Northern Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50 (1982); *see infra* notes 68-69 and accompanying text.

9. The technically correct term for a debtor in a Chapter 11 bankruptcy proceeding is "debtor in possession." 11 U.S.C. § 1101(1)(1982) provides that "'debtor in possession' means debtor except when a person that is qualified under § 322 of this title is serving as trustee in the case." For purposes of brevity, "debtor" will be used for "debtor in possession" throughout this article unless it becomes necessary to use the technically correct term.

10. 11 U.S.C. § 1113(b)(1)(A) (Supp. IV 1986).

11. *Id.*

12. 11 U.S.C. § 1113(b)(1)(A) (Supp. IV 1986). The court may enter protective orders to protect the debtor's trade secrets. 11 U.S.C. § 1113(d)(3) (Supp. IV 1986).

process[13] if the parties are unable to agree on modifications after "confer[ring] in good faith."[14] The court may approve rejection of the agreement if the debtor's proposal satisfies the above requirements, the representative of the employees has rejected the proposal "without good cause,"[15] and the "balance of equities clearly favors rejection of such agreement."[16]

Section 1113 of the Bankruptcy Code embodies a compromise between the desires of organized labor and those of the business and creditor community. Because it is a compromise, it is loaded with terms of compromise. Interpretation of terms such as "necessary," "fairly and equitably," "good faith," and "good cause" naturally falls to the courts. Given the ambiguity of the statute, and the tension inherent in situations where the debtor must seek rejection of its collective bargaining agreement, the potential for frequent, complex litigation seems great. In fact, these compromise words and factors came together in the first case to reach the United States Court of Appeals, *Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of America, AFL-CIO-CLC.*[17]

However, in the real business world, section 1113 may be a non-issue. There has not been a flood of litigation. The fear by organized labor that employers would rush to bankruptcy courts to rid themselves of unions has not materialized. One of the few such cases, prior to the enactment of section 1113, was *In re Continental Airlines Corp.*[18] Continental Airlines unilaterally rejected its collective bargaining agreements and laid off all of its employees immediately after it filed bankruptcy.[19] Shortly thereafter, it resumed operations with less than one-half of its employees who were paid at less than one-half their prior wage rates.[20] The pilots and flight attendants struck, but the airline survived.[21]

When labor is not well organized, as may have been the case in *Continental*, such an outcome is possible. However, when a company is organized by a strong union, such as the United Steelworkers of America, the union can force a damaging strike. A debtor struggling

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13. 11 U.S.C. § 1113(d)(1) (Supp. IV 1986).
14. 11 U.S.C. § 1113(b)(2) (Supp. IV 1986).
15. 11 U.S.C. § 1113(c)(2) (Supp. IV 1986).
16. 11 U.S.C. § 1113(c)(3) (Supp. IV 1986).
17. 791 F.2d 1074 (3d Cir. 1986); *see infra* text accompanying notes 173-276.
18. 50 Bankr. 342 (S.D. Tex. 1985), *aff'd* 790 F.2d 35 (5th Cir. 1986).
19. Continental, 50 Bankr. at 349.
20. *Id.*
21. *Id.*

for survival cannot risk a strike and the resultant loss of business. That was the case in *Wheeling-Pittsburgh*. Although the case ultimately reached the court of appeals, the real economic issues were decided at the bargaining table.

This article will examine the implications of section 1113 of the Bankruptcy Code. First, the article will briefly discuss section 1113 and the events which led to its enactment. Second, the article will analyze trends in recent cases, suggest parameters for courts to follow in future cases, and discuss how those parameters will not interfere with the debtor's ability to reorganize. Finally, although the authors believe that section 1113 has not been a significant issue in bankruptcy jurisprudence, the article will propose courses of action for debtors and employee representatives facing the prospect of rejection of a collective bargaining agreement.

II. The Evolution of Section 1113

A. *NLRB v. Bildisco and Bildisco*

Much has been written about *NLRB v. Bildisco and Bildisco*.[22] However, a brief discussion of the case is appropriate at this juncture to provide the context in which section 1113 was enacted.

Bildisco and Bildisco ("Bildisco"), a New Jersey partnership, filed for relief under Chapter 11 of the Bankruptcy Code[23] on April 1, 1980.[24] Bildisco was subsequently authorized to operate the business as debtor in possession.[25] At the time Bildisco filed for bankruptcy, it was subject to a three-year collective bargaining agreement with Local 408 of the International Brotherhood of Teamsters, Chauffeurs, Warehousemen and Helpers of America (the "Union").[26] In January 1980, Bildisco breached the collective bargaining agreement by failing to pay certain health and pension benefits and by failing to remit union dues withheld from employees.[27] In May 1980, Bildisco also failed to pay contractually mandated wage increases. In December 1980, Bildisco sought permission to reject the collective bargaining

22. 465 U.S. 513.
23. 11 U.S.C. § 1101 *et seq.* (1982).
24. 465 U.S. at 517.
25. 11 U.S.C. § 1107 (1982).
26. Approximately 40-45% of Bildisco's employees were members of the bargaining unit.
27. 465 U.S. at 518.

agreement pursuant to section 365(a) of the Bankruptcy Code.[28] The bankruptcy court granted Bildisco's request,[29] and the district court affirmed the bankruptcy court's decision. The Union appealed to the Court of Appeals for the Third Circuit.[30]

Following Bildisco's breach of the collective bargaining agreement, but prior to Bildisco's attempt to reject the agreement, the Union filed unfair labor practice charges with the National Labor Relations Board ("NLRB").[31] The NLRB ultimately found "that Bildisco had violated section 8(a)(5) and section 8(a)(1) of the [National Labor Relations Act] by unilaterally changing the terms of the collective bargaining agreement and by refusing to negotiate with the Union," and ordered Bildisco to take appropriate remedial action.[32]

The NLRB petitioned the Court of Appeals for the Third Circuit to enforce its order.[33] The Union's appeal of the bankruptcy order was consolidated with the NLRB's petition for enforcement.[34] The court of appeals declared that a collective bargaining agreement is an executory contract which may be rejected through section 365(a) of the Bankruptcy Code.[35] However, the court recognized that collective bargaining agreements are afforded special status, even though the Bankruptcy Code does not explicitly treat them differently.[36] Consequently, the court declined to utilize the normal test for rejection of an executory contract, the business judgment test.[37] Rather, the court adopted the standard set forth in *Shopmen's Local Union No. 455 v. Kevin Steel Products, Inc.*[38] In that case, the court stated

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28. 11 U.S.C. § 365(a) (1982). This section states, in pertinent part, that "the trustee, subject to the court's approval, may assume or reject any executory contract ... of the debtor."

29. The Union was given 30 days to file a claim for damages resulting from the breach of contract.

30. 465 U.S. at 518.

31. *Id.*

32. 465 U.S. at 519. Section (8)(a) of the National Labor Relations Act ("NLRA"), 29 U.S.C. § 158(a) (1982), provides, *inter alia*, that "[i]t shall be an unfair labor practice for an employer—(1) to interfere with, restrain, or coerce employees in the exercise of the rights guaranteed in § 157 of this title; ... (5) to refuse to bargain collectively with the representatives of his employees...."

33. The NLRB lacks enforcement powers; it must petition the appropriate United States Court of Appeals to enforce its orders. 29 U.S.C. § 160(e) (1982).

34. NLRB v. Bildisco and Bildisco (*In re* Bildisco), 682 F.2d 72 (3d Cir. 1982).

35. *Id.* at 78.

36. *Id.* at 79.

37. *Id.*

38. 519 F.2d 698 (2d Cir. 1975).

that a debtor may reject a collective bargaining agreement "only after thorough scrutiny, and a careful balancing of the equities on both sides...."[39] The Union and the NLRB unsuccessfully argued that a union contract could be rejected only upon "a showing 'that an onerous and burdensome executory collective bargaining agreement will thwart efforts the save a [debtor] ... from collapse.'"[40]

The *Bildisco* court of appeals refused to enforce the NLRB's order,[41] criticizing the NLRB's contention that the debtor in possession was bound by the collective bargaining agreement because it was an alter ego of the pre-petition employer.[42] Rather, the court stated that "as a matter of law, a debtor in possession is '[a] new entity ... created with its own rights and duties, subject to the supervision of the bankruptcy court.'"[43] As a new entity, similar to a successor employer of a profitable business, Bildisco was not subject to the collective bargaining agreement and thus "had the ability to reject the agreement without following the procedures outlined in section 8(d)."[44]

The United States Supreme Court granted certiorari because of the conflict between the Court of Appeals for the Second Circuit in *REA Express*[45] and the Third Circuit in *Bildisco*.[46] The Supreme Court first recited that none of the parties disputed that a collective bargaining agreement is an executory contract, as that term is used in section 365(a) of the Bankruptcy Code.[47] Since such agreements were not expressly exempted from the scope of section 365(a), the Court

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39. *Id.* at 707 (quoting In re Overseas National Airways, 238 F. Supp. 359, 361 (E.D.N.Y. 1965)).

40. *In re* Bildisco, 682 F.2d at 79 (quoting Brotherhood of Railway, Airline and Steamship Clerks v. REA Express, Inc., 523 F.2d 164, 169 (2d Cir. 1975), *cert. denied,* 423 U.S. 1017 (1975), *cert. denied*, 423 U.S. 1073 (1976)).

41. *Bildisco*, 682 F.2d at 85.

42. *Id.* at 82.

43. *Id.* (quoting *Kevin Steel*, 519 F.2d at 704).

44. *Id.* at 83.

45. 523 F.2d 164.

46. 465 U.S. at 521.

47. 11 U.S.C. § 365(a) (1982). This generally had not been a disputed issue. *See* West, *Life After Bildisco: § 1113 and the Duty to Bargain*, 47 OHIO ST. L.J. 65, 88 (1986).

However, as *amicus curiae*, the United Mine Workers of America argued that a collective bargaining agreement is not an executory contract within the context of § 365(a). The Court noted that the Bankruptcy Code does not define "executory contract," but that "Congress intended the term to mean a contract 'on which performance remains due to some extent on both sides.'" 465 U.S. at 522 n.6 (quoting H.R. Rep. No. 95-595, 95th Cong., 1st Sess. (1977)).

concluded "that Congress intended that section 365(a) apply to all collective bargaining agreements covered by the NLRA."[48]

The Supreme Court, however, agreed with the Third Circuit that "the business judgement" test is an insufficient standard for rejecting collective bargaining agreements.[49] However, like the Third Circuit, the Supreme Court rejected the *REA Express* standard which requires adoption of the prior collective bargaining agreement, unless rejection provides the only means for preventing the failure of the reorganization.[50] Such a standard, the Court stated, is "fundamentally at odds with the policies of flexibility and equity built into Chapter 11 of the Bankruptcy Code."[51] Rather, the debtor should be allowed to reject its collective bargaining agreement upon a "show[ing] that the collective bargaining agreement burdens the estate, and that after careful scrutiny, the equities balance in favor of rejecting the labor contract."[52] This was the standard adopted by the Third Circuit in *Bildisco*, and by the Eleventh Circuit in *In re Brada Miller Freight System, Inc.*[53] The Court added that the bankruptcy court should be satisfied that the debtor and the employees' representative have made reasonable efforts to negotiate voluntary modifications, but the bankruptcy court need not determine that the parties have bargained to impasse.[54] If the parties are unable to agree on modifications, the court may allow rejection.[55] At that time, the court must make a reasoned finding on the record as to whether rejection should be permitted and should consider the following factors:

> [The] likelihood and consequences of liquidation for the debtor absent rejection, the reduced value of the creditors' claims that would follow from affirmance and the hardship that would impose on them, and the impact of rejection on the employees. In striking the balance, the Bankruptcy Court must consider not only the degree of hardship faced by each party, but also any qualitative differences between the types of hardship each may face.[56]

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48. 465 U.S. at 522-23. Section 1167(a) of the Bankruptcy Code, 11 U.S.C. § 1167(a) (1982), exempts collective bargaining agreements subject to the Railway Labor Act from rejection pursuant to § 365. The Court reasoned that Congress knew how to draft an exemption to § 365(a) if it so chose. *Id.*

49. 465 U.S. at 523.

50. *Id.* at 524-25. *See supra* note 40 and accompanying text.

51. 465 U.S. at 525.

52. *Id.* at 526.

53. 702 F.2d 890 (11th Cir. 1983).

54. 465 U.S. 526.

55. *Id.* At that stage of the proceedings, the Court noted, the policies of the National Labor Relations Act have been adequately served.

56. *Id.* at 527.

In considering these factors, the court must focus on reorganization, "the ultimate goal of Chapter 11."[57]

The Supreme Court then considered whether a debtor commits an unfair labor practice by unilaterally rejecting or modifying a collective bargaining agreement.[58] The Supreme Court discounted the "new entity" analysis used by the court of appeals,[59] but ruled that a debtor does not violate sections 8(a)(5) and 8(d) of the NLRA by failing to honor any term of the contract, from the date of filing the bankruptcy petition until formal acceptance of the contract.[60] In a Chapter 11 bankruptcy, the debtor has until confirmation of the reorganization to decide whether to accept or reject an executory contract.[61] Rejection of an unassumed contract relates back to the date immediately preceding the filing of the petition.[62] The automatic stay[63] prevents an action for breach of contract. Therefore, the Supreme Court reasoned that the filing of a petition in bankruptcy means that the agreement is "no longer immediately enforceable, and may never be enforceable again."[64] Consequently, the NLRB "is precluded from ... enforcing the terms of the collective bargaining agreement by filing unfair labor practice charges ... for violating section 8(d) of the NLRA .... [T]he practical effect of the enforcement action would be to require adherence to the terms of the collective bargaining agreement."[65]

Four justices dissented from the Court's holding that the debtor does not commit an unfair labor practice by unilaterally modifying the labor contract before it has been authorized to do so by the bankruptcy court.[66] The first part of the decision, which established

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57. *Id.*
58. *Id.*
59. *Id.* at 528.
60. *Id.* at 532.
61. 11 U.S.C. § 365(d)(2) (1982).
62. 11 U.S.C. § 365(g)(1) (1982). Claims arising from a breach of a collective bargaining agreement are dealt with through the normal bankruptcy process for determining claims. 11 U.S.C. § 502 (Supp. 1986).
63. 11 U.S.C. § 362 (1982).
64. 465 U.S. at 532.
65. *Id.* The Court stated that such a result would run directly counter to the express provisions of the Bankruptcy Code and the Code's overall effort to give a debtor in possession some flexibility and breathing space. For the same reasons, the Court also refused to require the debtor to satisfy the requirements for mid-term contract modifications of § 8(d) of the NRLA.
66. *Id.* at 539 (Brennan, J. dissenting). The dissent pointed out that "no provision of [the] Code ... purports to render § 8(d) inapplicable ..." notwithstanding the majority's assertion that "enforcement of ... § 8(d) ... in the post-filing period 'would run directly counter to the express provisions of the Bankruptcy Code.'"

the standard for rejecting collective bargaining agreements, was a unanimous decision. It was not thought to be as controversial as the second part,[67] dealing with the question of unfair labor practices, which was the main impetus for the enactment of section 1113.

B. *The Constitutional Crisis in the Bankruptcy System and the Enactment of Section 1113*

The enactment of section 1113 was a major skirmish within the larger campaign to create a bankruptcy system that would pass constitutional muster. Two years earlier, in *Marathon Pipe Line*,[68] the United States Supreme Court held that the jurisdiction of the bankruptcy courts was unconstitutional. To avoid impairing the administration of the bankruptcy laws, the Court declined to apply the decision retroactively, and stayed its judgment until October 4, 1982 to "afford Congress an opportunity to reconstitute the bankruptcy courts or to adopt other valid means of adjudication ...."[69] Although the Senate Judiciary Committee held hearings on the bankruptcy system in July 1982, Congress was unable to meet the Court's deadline. The Supreme Court then extended its stay until December 24, 1982, but Congress still did not act. The Court refused to grant an additional continuance.

Following the expiration of the stay in *Marathon Pipe Line*, the Judicial Conference of the United States promulgated an interim

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67. Gibson, *supra* note 4, at 326; West, *supra* note 47, at 90.

68. 458 U.S. 50. Prior to 1978, bankruptcy courts were endowed with limited jurisdiction. In 1978, Congress enacted the Bankruptcy Code, which *inter alia*, expanded the jurisdiction of the bankruptcy courts. 28 U.S.C. § 1471(b) and (c) gave the bankruptcy courts "the jurisdiction of all civil proceedings arising under Title 11 or arising in or related to cases under Title 11." In effect, Congress gave bankruptcy court judges many of the powers of Article III judges, but none of the protections (lifetime tenure, removal only through impeachment by Congress, and salaries which may not be reduced). Article I of the Constitution empowers Congress to create other inferior tribunals such as the bankruptcy courts. These courts lack the protections of Article III courts.

In *Marathon*, Northern Pipeline, a Chapter 11 debtor, brought an action in bankruptcy court against Marathon for various state law causes of action. Marathon moved for dismissal, asserting that 28 U.S.C. § 1471 unconstitutionally conferred Article III powers on bankruptcy judges. The bankruptcy court denied the motion to dismiss, but the district court reversed the bankruptcy court. The debtor and the United States appealed to the Supreme Court. In a plurality opinion, the Supreme Court concluded that the broad grant of jurisdiction to the bankruptcy courts was unconstitutional because it gave Article III responsibilities to judges lacking the constitutional safeguards of Article III.

69. 458 U.S. at 88.

rule, which was adopted by the judicial council for each circuit and ultimately by the district courts.[70] Following the *Bildisco* decision, organized labor renewed its efforts to have Congress address the issue of the rejection of collective bargaining agreements during Chapter 11 proceedings. The business and creditor community lobbied Congress to maintain the salutary effects of *Bildisco*. Concurrently, the March 31, 1984 expiration of the interim rule was approaching.

The initial attempts to address the problem, as perceived by organized labor, were naturally very restrictive. To preclude employers from filing Chapter 11 for the purpose of rejecting union contracts, H.R. 4858[71] imposed a solvency test on debtors. The Rodino measure, H.R. 4908,[72] imposed substantially the same requirements as those imposed by the Court of Appeals for the Second Circuit in *REA Express*.[73] Additionally, the collective bargaining agreement rejection provision of H.R. 4908 was retroactive.

Congressman Rodino subsequently introduced another measure to reconstitute the bankruptcy system, H.R. 5174.[74] H.R. 5174 contained a proposed section 1113, dealing with the rejection of collective bargaining agreements. Procedurally, that section was substantially similar to the measure which was ultimately enacted. Substantively, however, the proposed section 1113 contained the *REA Express* standard for rejection, but was not retroactive.

On March 31, 1984, the interim rule on jurisdiction was to expire. Until Congress ultimately enacted corrective legislation, on June 28, 1984, it was required to extend the transition period and interim rule several times.[75] In May 1984, two proposals dealing with collective

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70. Rosenberg, *supra* note 6, at 312. The interim rule was to expire March 31, 1984. The interim rule provided that all cases under Title 11,arising under Title 11, or arising in or related to cases under Title 11 were automatically referred to bankruptcy judges, but the reference could be withdrawn. In related proceedings, absent consent of the parties, the bankruptcy court could not enter final orders; the bankruptcy court could only submit findings of fact, conclusions of law and a proposed order to the district court. All orders entered by the bankruptcy court were subject to *de novo* review by the district court.

71. *See supra* note 6 and accompanying text.

72. *See supra* note 5 and accompanying text.

73. 523 F.2d 164; *see supra* note 40 and accompanying text.

74. H.R. 5174, 98th Cong., 2d Sess., 130 Cong. Rec. H1727 (1984). This proposed legislation sought to grant Article III status to bankruptcy judges. Previously Congressman Rodino had introduced similar legislation. *See* H.R. 3, 98th Cong., 1st Sess., 129 Cong. Rec. H40 (1983).

75. For a detailed description of the atmosphere and activity in Congress surrounding the enactment of the Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, *see* Rosenberg, *supra* note 6, at 312-21.

bargaining agreements were introduced in the Senate: the "Thurmond substitute" and the "Packwood amendment".[76] The Thurmond substitute,[77] *inter alia*, maintained the *Bildisco* standard of balancing the equities. The proposal required that before a debtor could reject a collective bargaining agreement, the debtor and the employees' representative make reasonable efforts to reach a voluntary agreement, that such efforts be unlikely to produce satisfactory results, and that the inability to reach an agreement threaten the likelihood of successful reorganization.[78] Additionally, the debtor could not unilaterally terminate the contract for thirty days after filing a motion to reject, during which time the bankruptcy court would hold a hearing on rejection.[79] The Thurmond substitute was not retroactive.[80]

The Packwood amendment[81] required the debtor to propose the minimum modifications to enable the reorganization to succeed. Such modifications would be based on the debtor's best estimate of the necessary sacrifices required of creditors and other affected parties.[82] The Packwood amendment would further require the debtor to supply the union with the information necessary to evaluate the proposal.[83] As with the Thurmond substitute, the parties would be required to attempt to agree on modifications.[84] If the debtor made a sufficient proposal which the union unjustifiably refused, then the balance of equities would favor rejection.[85] The Packwood amendment provided for an expedited hearing and decision, and was retroactive.[86]

The Senate was unable to agree on either proposal. The Senate passed the Thurmond substitute on June 19, 1984, but without including its provision on collective bargaining agreements.[87] The House and Senate conferred on the final version of the legislation, but the Conference Committee was unable to agree on legislation by the time the last extension and the 1982 Emergency Rule finally

76. Rosenberg, *supra* note 6, at 316.
77. 130 Cong. Rec. S6081 (daily ed. May 21, 1984).
78. Rosenberg, *supra* note 6, at 317.
79. *Id.*
80. *Id.*
81. 130 Cong. Rec. S6181-82 (daily ed. May 22, 1984).
82. Rosenberg, *supra* note 6, at 317.
83. *Id.*
84. *Id.*
85. *Id.*
86. *Id.* at 317-18.
87. 130 Cong. Rec. S7617 (daily ed. June 19, 1984).

expired on June 27, 1984.[88] On June 28, 1984, at close to 3:00 a.m., the House and Senate Conference Committee agreed on a compromise bill, the Bankruptcy Amendments and Federal Judgeship Act of 1984,[89] which included provisions modifying the *Bildisco* decision. The conference report was approved by the full House of Representatives and Senate,[90] and was ultimately signed by the President.

C. *What was Congress' Intent*

Section 1113 corrected what organized labor found to be the most odious portion of the *Bildisco* decision—a debtor's unfettered ability to unilaterally reject a collective bargaining agreement.[91] Although section 1113 does not address the issue as it arose within the *Bildisco* decision, whether unilateral rejection is an unfair labor practice, "[n]o provision of this title shall be construed to permit a trustee to unilaterally terminate or alter any provision of a collective bargaining agreement prior to compliance with the provisions of this section."[92] To avoid its obligations under a collective bargaining agreement, a debtor must now satisfy the following prerequisites:

> (A) [M]ake a proposal to the authorized representative of the employees covered by such agreement, based upon the most complete and reliable information available at the time of such proposal, which provides for those necessary modifications in the employees' benefits and protections that are necessary to permit the reorganization of the debtor and assures that all creditors, the debtor and all the affected parties are treated fairly and equitably; and
> (B) Provide, subject to subsection (d)(3), the representative of the employees with such relevant information as is necessary to evaluate the proposal.[93]

Once the debtor satisfies these requirements, the bankruptcy court "shall" approve rejection[94] if it finds "the authorized representative

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88. Rosenberg, *supra* note 6, at 318. The United States Judicial Conference implemented a second emergency plan to keep the bankruptcy courts operating. Under this plan, the bankruptcy judges were to serve as consultants to the district court.

89. Pub. L. No. 98-353, 98 Stat. 390.

90. 130 Cong. Rec. H7499 (daily ed. June 29, 1984).

91. Ehrenwerth and Lally-Green, *The New Bankruptcy Procedures for Rejection of Collective Bargaining Agreements: Is the Pendulum Swinging Back?*, 23 DUQ. L. REV. 939, 950 (1985).

92. 11 U.S.C. § 1113(f) (Supp. IV 1986).

93. 11 U.S.C. § 1113(b)(1)(A)-(B) (Supp. IV 1986).

94. 11 U.S.C. § 1113(c)(1) (Supp. IV 1986).

of the employees has refused to accept such proposal without good cause"[95] and "the balance of the equities clearly favors rejection of such agreement."[96] The court must hold a hearing within fourteen days of the filing of the application for rejection[97] and must issue a decision within thirty days of the commencement of the hearing.[98] If the court fails to issue a timely decision, only then may the debtor unilaterally reject the contract.[99] Section 1113 also enables the court to authorize the debtor to implement interim changes, notwithstanding a pending application to reject, "if essential to the continuation of the debtor's business," or "to avoid irreparable damage to the estate." [100]

The procedural requirements of section 1113 are straightforward; the substantive requirements, however, are not. Although Congress appears to have codified the *Bildisco* standard for rejection, questions of interpretation naturally remain, because "necessary," "good faith," "fairly and equitably," and "good cause" are not defined by the statute. The legislative history is sparse, and thus is of limited value in determining Congress' intentions. The House and Senate Judiciary Committees did not publish a joint explanatory statement or report. The only legislative history consists of inconsistent statements made to the Congress by some members of the House and Senate Judiciary Committees.[101] In such circumstances, such statements may not "reflect the collective intent or will of Congress."[102]

Thus, we turn to the language of section 1113. We first examine the term "necessary." The litigation which has ensued from section 1113 has frequently involved interpretation of this word.[103] It should

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95. 11 U.S.C. § 1113(c)(2) (Supp. IV 1986).

96. 11 U.S.C. § 1113(c)(3) (Supp. IV 1986).

97. 11 U.S.C. § 1113(d)(1) (Supp. IV 1986). This section also provides that the "court may extend the time for commencement of such hearing for a period not exceeding seven days" or for additional periods of time by agreement between the debtor and the union.

98. 11 U.S.C. § 1113(d)(2) (Supp. IV 1986). By agreement of the parties, the court may extend the time in which it may render a decision.

99. *Id.*

100. 11 U.S.C. § 1113(e) (Supp. IV 1986). The court may allow interim changes only after notice and a hearing.

101. 130 Cong. Rec. H7489-97 and S8897-8900 (daily ed. June 29, 1984), *reprinted in*, 1984 U.S. Code Cong. & Ad. News 576-605.

102. Landmark Hotel & Casino, Inc. v. Local Joint Executive Board of Las Vegas (In re Landmark Hotel & Casino, Inc.), 78 Bankr. 575, 583 (9th Cir. B.A.P. 1987); *see also* Garcia v. United States, 469 U.S. 70 (1984).

103. *See, e.g.*, Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of America, 791 F.2d 1074 (3d Cir. 1986).

be noted that "necessary" appears twice within section 1113(b)(1)(A).[104] The debtor must propose only "necessary modifications" to the collective bargaining agreement "that are necessary to permit the reorganization of the debtor."[105]

Congress did not specify the standard to be used in evaluating whether proposed changes are "necessary." Organized labor favored the stringent standard of *REA Express*,[106] while business and creditor interests favored the *Bildisco* standard.[107] However, the legislative history does not indicate that Congress adopted the *REA Express* standard. The legislation proposed by Congressman Rodino,[108] which incorporated the *REA Express* standard, was not enacted. Nor was Senator Packwood's proposed legislation adopted. That proposal provided that the debtor propose "minimum modifications."[109] Rather, Congress' use of the "necessary" clause, together with its non-use of the language of the Rodino and Packwood proposals indicates that it did not use the *REA Express* standard. Additionally, in the subsection providing for interim relief,[110] Congress deliberately used the term "essential" where it desired to implement the *REA Express* standard.[111] Thus, Congress knew how to adopt the *REA Express* standard if it chose to do so. Congress' failure to use the term "essential" instead of the term "necessary" in section 1113(b)(1)(A) demonstrates that Congress did not adopt the *REA Express* standard.[112]

Clearly, the changes in the contract which the debtor proposes must focus on a successful reorganization.[113] Senator Packwood

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104. 11 U.S.C. § 1113(b)(1)(A) (Supp. IV 1986).

105. *Id.*

106. *See supra* note 40 and accompanying text.

107. *See supra* notes 50-54 and accompanying text.

108. *See supra* notes 5 and 72 and accompanying text.

109. *See supra* text accompanying note 81.

110. 11 U.S.C. § 1113(e) (Supp. IV 1986) states, in pertinent part, that "when the collective bargaining agreement continues in effect, and if essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate, the court, after notice and a hearing, may ... implement interim changes ...."

111. *See* 130 Cong. Rec. H7496 (daily ed. June 29, 1984) (statement of Rep. Morrison); *See also* 130 Cong. Rec. S8898 (daily ed. June 29, 1984) (statement of Sen. Packwood).

112. This argument was rejected as "hyper-technical" by the Third Circuit in Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1088; *see infra* text accompanying note 258.

113. *But see* Wheeling-Pittsburgh v. Steelworkers, 791 F.2d 1074; *infra* text accompanying notes 244-254.

articulated this concept during the debate on the conference committee's report: "The debtor will not be able to exploit the bankruptcy procedure to rid itself of unwanted features of the labor agreement that have no relation to its financial condition and its reorganization which were earlier agreed to by the debtor."[114] Modifications to the collective bargaining agreement which result in easily quantifiable cost savings are more likely to constitute "necessary" modifications. However, a showing by the debtor that the proposed changes will result in cost savings, by itself, is insufficient to meet the requirement of necessity. Such savings must be necessary to the debtor's reorganization.[115] Examples of changes which are likely to be found to be necessary include changes in wages, health insurance, pension fund contributions, vacations, and paid holidays. It is less clear whether changes in the collective bargaining agreement which cannot be measured as easily in dollars, such as changes in seniority and work rules, will be construed as necessary.[116]

In a statement on the conference report, Senator Hatch injected a note of pragmatism into the process envisioned by section 1113. He noted that at the time a debtor would be likely to file an application to reject pursuant to section 1113, the debtor's reorganization plan would still be in the formative stages: "The conference also discussed at length its intent that this provision not become an attempt to devise an entire reorganization plan at a premature stage. We were all aware of the impossibility of even identifying all the creditors and their interests at this early stage of the reorganization effort."[117] Consequently, the term "necessary" must be viewed within this context.

We next consider the meaning of the phrase "fairly and equitably." Section 1113(b)(1)(A) requires that the debtor's proposal treat "all creditors, the debtor, and all of the affected parties ... fairly and equitably." [118] The legislative history reveals that this language was

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114. 130 Cong. Rec. S8898 (daily ed. June 29, 1984) (statement of Sen. Packwood).

115. *See, e.g.*, *In re* American Provision Co., 44 Bankr. 907 (D. Minn. 1984). There, the court denied rejection because the proposed changes would have saved the debtor only 2% of it monthly operating expenses; *see infra* text accompanying notes 140-150.

116. Ehrenwerth and Lally-Green, *supra* note 91, at 953; West, *supra* note 47, at 110.

117. 130 Cong. Rec. S8991 (statement of Sen. Hatch), *reprinted in*, 1984 U.S. Code Cong. & Ad. News at 593.

118. 11 U.S.C. § 1113(b)(1)(A) (Supp. IV 1986).

meant to ensure that the burden does not fall unfairly on a particular group of employees or other parties. Senator Packwood favored this language to assure "that the focus for cost cutting must not be directed exclusively at unionized workers. Rather, the burden of sacrifices ... will be spread among all affected parties."[119] Senator Packwood believed that this provision would make the proposed modifications more palatable to the union employees; they would not feel that only they were making sacrifices to preserve the debtor.

As an example of how the "fairly and equitably" requirement should be applied, Senator Packwood referred approvingly to *In re Blue Ribbon Transportation Co. Inc.*[120] In that case, the bankruptcy court agreed that successful reorganization required a rejection of the collective bargaining agreement. However, the court noted that management wages and benefits were also excessive. The court conditioned rejection of the collective bargaining agreement on commensurate reductions in management costs.[121]

Other members of the conference committee attached a different meaning to this provision. Those who were less sympathetic to labor's position[122] believed that this language would prevent non-union employees from bearing a disproportionate burden of the reorganization. As stated by Senator Thurmond, "[t]his phrase clearly includes, however, all non-union employees of the debtor whose interests should be as carefully considered by the court as those of any union employees."[123]

Between the time the debtor proposes modifications to the collective bargaining agreement and the hearing on the application for rejection, the debtor must "meet, at reasonable times with the authorized representative to confer in good faith ... to reach mutually satisfactory modifications...."[124] The good faith requirement originated in

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119. 130 Cong. Rec. S8898 (daily ed. June 29, 1984) (statement of Sen. Packwood).

120. 30 Bankr. 783 (Bankr. D.R.I. 1983).

121. *Id.* at 786-87. (The court noted that management was overstaffed, as well as overpaid).

122. Senator Thurmond, for example, believed that *Bildisco* was correctly decided. However, he agreed to the enactment of § 1113 because of the "critical need to pass this bankruptcy bill ...." 130 Cong. Rec. S8887 (statement of Sen. Thurmond), *reprinted in*, 1984 U.S. Code Cong. & Ad. News at 582.

123. 130 Cong. Rec. S8888 (statement of Sen. Thurmond), *reprinted in*, 1984 U.S. Code Cong. & Ad. News at 583.

124. 11 U.S.C. § 1113(b)(2) (Supp. IV 1986).

Bildisco[125] and Congress intended to maintain that requirement.[126] A large body of precedent defines "good faith" within labor law jurisprudence. Congress, mindful of the Supreme Court's admonition in *Bildisco* that bankruptcy courts should avoid areas outside their expertise,[127] has proscribed the bankruptcy courts from using such precedents,[128] but has not provided an alternate definition. One commentator has suggested that Congress intended the courts to interpret the "good faith" requirement in a non-technical fashion limited to a determination of whether the debtor seriously attempted to reach an agreement with the union.[129] This suggested interpretation is consistent with *Bildisco's* requirement that the parties bargain, but not to impasse.

If an agreement cannot be reached rejection will be allowed, but the court must first find that the union has refused to accept the debtor's proposal "without good cause."[130] The statute fails to define the phrase "without good cause," nor is it defined in the NLRA or anywhere else in bankruptcy law.[131] It is logical to assume that "without good cause" somehow parallels "in bad faith."[132] Senator Packwood's comments support this position: "The 'without good cause' langauge provides an incentive or pressure on the debtor to negotiate in good faith .... [The] language serves to prohibit any bad faith conduct by the employer, while at the same time protecting the employer from a union's rejection of the proposal without good cause."[133] Thus, the "without good cause" requirement is an indirect

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125. 465 U.S. at 526 ("[T]he Bankruptcy Court should be persuaded that reasonable efforts to negotiate a voluntary modification have been made and are not likely to produce a prompt and satisfactory solution.")

126. 130 Cong. Rec. S8892 (statement of Sen. Hatch), *reprinted in*, 1984 U.S. Code Cong. & Ad. News at 593.

127. *Bildisco*, 465 U.S. at 526-27.

128. *See infra* note 131.

129. Gibson, *supra* note 4, at 330.

130. 11 U.S.C. § 1113(c)(2) (Supp. IV 1986).

131. *See* Ehrenwerth and Lally-Green, supra note 91, at 974; West, *supra* note 47, at 133. Senator Thurmond feared that the requirement that the "union refusal to accept the proposal be 'without good cause' would import traditional labor law concepts into a bankruptcy forum or turn the bankruptcy courts into a version of the National Labor Relations Board." 130 Cong. Rec. S8888 (statement of Sen. Thurmond), *reprinted in,* 1984 U.S. Code Cong. & Ad. News at 583.

132. Perhaps the drafters meant to say "in bad faith" instead of "without good cause," but inadvertently used the wrong terminology. It should be remembered that the conferees reached agreement at 3:00 a.m.

133. 230 Cong. Rec. S8898 (daily ed. June 29, 1984) (statement of Sen. Packwood).

and somewhat redundant demand that the parties bargain in good faith.

In addition to requiring that the union bargain in good faith, some commentators have suggested that the phrase "without good cause" imposes substantive requirements on the union's bargaining posture. For example, if the debtor, in good faith, makes a proposal which it believes contains only "necessary" modifications, but the union, in good faith, makes a counterproposal containing what it believes to be only "necessary" modifications, does this constitute rejection"without good cause"?[134] If the debtor's proposal satisfies section 1113(b)(1), must the union compromise its position?[135]

Even if the union has not shown good cause the court must also find that the "balance of equities clearly favors rejection."[136] Congress made it clear that it was adopting the standard for rejection set forth in *Bildisco*.[137] However, Congress modified the *Bildisco* standard by mandating that the balance of equities "clearly" favors rejection. This is to ensure that rejection is not allowed when the balance of the equities does not favor one side or the other: "The word 'clearly' is merely intended to assure that rejection is not warranted where the equities balance exactly equally on each side ...."[138] Other than those comments, Congress failed to further elucidate the concept of "balance of equities."[139]

III. Judicial Interpretation of Section 1113

A. *Initial Interpretation by the Bankruptcy Courts*

The first reported decision interpreting section 1113 was *In re American Provision Company*.[140] There, the court determined that section 1113 creates nine requirements for rejection:

1. The debtor in possession must make a proposal to the union to modify the collective bargaining agreement.

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134. *See* Gibson, *supra* note 4, at 341; West, *supra* note 47, at 131.

135. Ehrenwerth and Lally-Green, *supra* note 91, at 964.

136. 11 U.S.C. § 1113(c)(3) (Supp. IV 1986).

137. 130 Cong. Rec. S8892 (statement of Sen. Hatch), *reprinted in,* 1984 U.S. Code Cong. & Ad. News at 594; 130 Cong. Rec. S8890 (statement of Sen. Dole), *reprinted in,* 1984 U.S. Code Cong. & Ad. News at 588. For a list of the factors to be considered in "balancing the equities," *see supra* text accompanying note 56.

138. 130 Cong. Rec. S8992 (statement of Sen. Hatch), *reprinted in,* 1984 U.S. Code Cong. & Ad. News at 594.

139. Ehrenwerth and Lally-Green, *supra* note 91, at 965.

140. 44 Bankr. 907 (Bankr. D. Minn. 1984).

2. The proposal must be based on the most complete and reliable information available at the time of the proposal.
3. The proposed modifications must be necessary to permit the reorganization of the debtor.
4. The proposed modifications must assure that all creditors, the debtor and all of the affected parties are treated fairly and equitably.
5. The debtor must provide to the union such relevant information as is necessary to evaluate the proposal.
6. Between the time of the making of the proposal and the time of the hearing on approval of the rejection of the existing collective bargaining agreement, the debtor must meet at reasonable times with the union.
7. At the meetings the debtor must confer in good faith in attempting to reach mutually satisfactory modifications of the collective bargaining agreement.
8. The union must have refused to accept the proposal without good cause.
9. The balance of the equities must clearly favor rejection of the collective bargaining agreement.[141]

The court also noted that the debtor bears the initial burden of persuasion, by a preponderance of the evidence, on all nine elements.[142] However, the court stated that after an initial showing of the nine factors by the debtor, the burden of producing evidence shifts to the union with respect to three of the nine elements.[143] First, after the debtor shows what information it has provided to the union, the union must then produce evidence that the information provided "was not the relevant information which was necessary for it to evaluate the proposal."[144] Second, after the debtor shows that it has met with the union's representatives, the union must "produce evidence that the debtor did not confer in good faith."[145] Finally, once the debtor shows that the union refused to accept its proposal, "the union must produce evidence that it was not without good cause."[146]

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141. *Id.* at 909. Several other cases have adopted, or referred to, the nine-step analysis of this case. *See, e.g.*, Wheeling-Pittsburgh v. Steelworkers, 791 F.2d 1074; *In re* K & B Mounting, Inc., 50 Bankr. 460 (Bankr. N.D. Ind. 1985); *In re* Cook United, 50 Bankr. 561 (Bankr. N.D. Ohio 1985). *But see In re* Royal Composing Room, Inc., 62 Bankr. 403, 406 (Bankr. S.D.N.Y. 1986), *aff'd* 78 Bankr. 671 (S.D.N.Y. 1987) ("This court eschews the talismanic nine-step analysis ... first used in *In re* American Provision Co....").

142. *Id.*

143. *Id.*

144. *Id.* at 909-10.

145. *Id.* at 910.

146. *Id.*

Although *American Provision* is frequently cited for its statement of the nine requirements for rejecting a collective bargaining agreement, it is also an important case because it represents the first attempt to define "necessary" within the context of section 1113.[147] At the time of its application to reject, the debtor employed only two union employees.[148] The court stated that the proposed savings to the debtor, as a result of rejection, would equal 2% of the debtor's monthly operating expenses.[149] Consequently, the court stated that it could not find such *de minimis* savings were necessary to permit the reorganization of the debtor.[150]

In re K & B Mounting, Inc.[151] is another case in which the bankruptcy court refused to find that the debtor's proposed modifications were necessary.[152] There, pre-petition, the debtor began an austerity program, which included purchasing equipment for cash rather than on credit.[153] Consequently, the debtor had no secured debt; its only major obligations were to the union's health, welfare and pension plans.[154] The debtor's proposed modifications to the collective bargaining agreement included wage reductions and suspension of payments under the welfare and pension plans.[155] In those circumstances, the court could not conclude that the proposed modifications were necessary, since the debtor failed to "substantiate its proposal with 'relevant' information selected from 'the most complete and reliable information available' ...."[156] Rather, the court criticized the debtor for attempting to modify the collective bargaining agreement with nothing more than unsupported allegations of serious cash flow problems.[157] The court also found that the debtor's unique financial situation, in which its only obligations were to the union's pension, health, and welfare funds, could not constitute fair and equitable treatment of all the affected parties.[158] Thus, the union had

147. *Id.*
148. *Id.*
149. *Id.*
150. *Id.* The court also disallowed rejection because the debtor failed to meet its burden of proving that it had bargained in good faith. *See infra* text accompanying note 321.
151. 50 Bankr. 460 (Bankr. N.D. Ind. 1985).
152. *Id.* at 467.
153. *Id.* at 468.
154. *Id.*
155. *Id.* at 467.
156. *Id.* (quoting 11 U.S.C. § 1113(b)(1)(A)).
157. 50 Bankr. at 467-68.
158. *Id.* at 468.

good cause to reject the debtor's proposal.[159] The court indicated that although a debtor may not like its collective bargaining agreement, such reasons are clearly insufficient grounds for rejection: "[T]he test, in justifying ... the proposed modifications, is necessity, not convenience or desirability."[160]

Similarly, in *In re Cook United, Inc.*,[161] the court refused to find that the debtor's proposed modifications were necessary, in light of positive cash flow of $1.9 million in the debtor's plan of reorganization, even without the proposed changes in the contract.[162] The court also found that the proposed changes did not treat all of the affected parties fairly and equitably since the proposed changes had a disproportionate impact on the lowest paid union employees.[163] The debtor, creditors, and other unionized employees were not subjected to the same level of sacrifices as were the lowest paid employees.[164] The court also noted that the debtor's management failed to take any pay cuts.[165]

The first reported decision in which a bankruptcy court examined the term "necessary" and allowed rejection was *In re Allied Delivery System Co.*[166] In determining that the debtor's proposed modifications were necessary, the court addressed an argument that would later be raised in *Wheeling-Pittsburgh*[167] — whether "necessary" means "essential." The court emphasized that section 1113(b)(1)(A) differed significantly from the original proposal in the House of Representatives, which would have required a finding by the bankruptcy court that the reorganization would fail and the employees would lose their jobs unless the contract was rejected.[168] The court added that subsection (e) of section 1113 "requires that the debtor show that the requested relief is 'essential to the continuation of the debtor's business' or is needed 'to avoid irreparable damage to the estate

159. *Id.*
160. *Id.*
161. 50 Bankr. 561 (Bankr. N.D. Ohio 1985).
162. *Id.* at 563.
163. *Id.* at 564.
164. *Id.* The employees, who the court found would be the most burdened by the modifications, were members of various locals of the United Food and Commercial Workers Union. The debtor's other unionized employees, who were subjected to less severe cuts, were members of one Teamsters local.
165. *Id.* at 565.
166. 49 Bankr. 700 (Bankr. E.D. Ohio 1985).
167. 791 F.2d 1074.
168. 49 Bankr. at 702.

...'."[169] *A fortiori*, the court reasoned that if Congress intended to adopt a stricter test, it knew how to do so.[170]

The court also analyzed the term "necessary" in connection with the requirement of good faith negotiations. If the debtor proposed modifications which were limited to those that were essential to its survival, and then moderated its demands as part of the negotiating process, it would be "subject to a finding that any substantial lessening of the demands made in the original proposal proves that the original proposal's modifications were not 'necessary.'"[171] It is not difficult to see how the court found that the debtor's proposed modifications were necessary. The union contract provided for labor costs which constituted 87% of the debtor's gross revenues.[172]

B. *The Third Circuit Explores the Issue—Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of America*

Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of America, AFL-CIO-CLC,[173] was the first case in which a court of appeals considered section 1113. The Third Circuit reversed the bankruptcy court's allowance of rejection, and the district court's affirmance, holding that the debtor's proposal was not limited to necessary modifications.[174] In doing so, the court of appeals concluded, *inter alia*, that "necessary" within the context of section 1113 is tantamount to "essential."[175] The court also found that the debtor's proposal did not treat all parties "fairly and equitably," because it failed to contain a "snap back" provision.[176] The Third Circuit's opinion has not been followed outside that circuit.

Wheeling-Pittsburgh exemplifies the legal maxim "hard cases make bad law." At the time of the bankruptcy, Wheeling-Pittsburgh was the largest debtor ever to utilize section 1113. The debtor and union had particularly rancorous labor-management relations.[177] At the time that it filed for relief under Chapter 11, Wheeling-Pittsburgh was

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169. *Id.*
170. *Id.*
171. *Id.*
172. *Id.* The court added that labor costs and current pension and welfare obligations potentially exceeded the debtor's gross revenues. *Id.*
173. 791 F.2d 1074.
174. *Id.* at 1085.
175. *Id.* at 1088.
176. *Id.* at 1090.
177. *Id.* at 1077-78.

the seventh largest steelmaker in the country.[178] During the late 1970's, Wheeling-Pittsburgh extensively modernized its facilities. Some of its facilities were modern and efficient, but as a result it became heavily indebted.[179] The company lost money in 1982, 1983, and 1984. Wheeling-Pittsburgh's losses, coupled with the need to make payments on the modernization loans, severely impaired the company's financial condition.[180]

Twice in 1982, Wheeling-Pittsburgh asked for concessions from its union, the United Steelworkers of America, AFL-CIO-CLC ("Steelworkers").[181] At the time that it asked for the initial concessions, Wheeling-Pittsburgh's average gross labor costs were near the industry average of approximately $25 per hour.[182] In April of 1982, the Steelworkers granted Wheeling-Pittsburgh a reduction in labor costs of $1.65 per hour. As a *quid pro quo*, the employees were entitled to preferred stock.[183]

In December 1982, the Steelworkers again granted concessions, as part of a new three-and-one-half year collective bargaining agreement.[184] Labor costs were reduced again. In return, Wheeling-Pittsburgh created a profit-sharing plan.[185] This new agreement provided for recovery of the concessions, so that the average labor costs would be $25 per hour at the end of the contract term.[186] At the end of 1984, Wheeling-Pittsburgh again asked for concessions—the cancellation of all scheduled restorations. The Steelworkers agreed to defer restoration, pending review by its accountants of Wheeling-Pittsburgh's financial reports. After consulting with its accountants, the Steelworkers agreed to defer concessions indefinitely.[187]

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178. *Id.* at 1076.

179. *Id.* The court noted that Wheeling-Pittsburgh's long term debts grew from $170 million at the end of 1979 to $527 million at the end of 1984. *Id.*

180. *Id.*

181. *Id.* at 1077.

182. *Id.* at 1076-77. Gross labor costs include wages, benefits, current pension costs and other retiree benefits, and payroll taxes. Traditionally, Wheeling-Pittsburgh and the other major steel producers bargained as a group with the Steelworkers. Thus, Wheeling-Pittsburgh's average gross labor costs were substantially the same as the other major steel producers. *Id.* at 1076.

183. *Id.* at 1077.

184. *Id.*

185. *Id.*

186. *Id.* Labor costs were reduced to a minimum of $18.60, although the exact amount was disputed. The gradual restorations provided, for example, that the average labor costs would be restored to $21.40 per hour by the end of 1984. *Id.*

187. *Id.*

In January 1985, Wheeling-Pittsburgh requested concessions for the fourth time.[188] This time, however, the Steelworkers refused to grant further concessions until Wheeling-Pittsburgh obtained concessions from its lenders, a very astute reaction from a bankruptcy point of view. Previously, the lenders had not made any concessions. Thereafter, Wheeling-Pittsburgh issued a restructuring proposal, which sought to obtain concessions from the lenders[189] and shareholders[190] as well as the Steelworkers.[191] Wheeling-Pittsburgh had not proposed to pledge its current assets as collateral for past debts. The Steelworkers considered this crucial to the company's survival.[192] It feared that if Wheeling-Pittsburgh "pledged the current assets, the company would have no 'life preserver' and thus go under (taking the employees' jobs with it) in the event of an economic downturn."[193] In fact, the Steelworkers' counterproposal insisted that Wheeling-Pittsburgh promise not to pledge its current assets to the banks.[194] This was prudent bankruptcy bargaining prior to the bankruptcy filing. The lenders counterproposed that Wheeling-Pittsburgh pledge its current assets, in return for deferring present indebtedness and providing additional credit.[195] Wheeling-Pittsburgh was ready to concede to the lenders![196] The attempted restructuring outside of bankruptcy failed.[197] The Steelworkers and the lenders would not retreat from

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188. *Id.*

189. *Id.* Wheeling-Pittsburgh asked all of its lenders for a moratorium on principal payments in 1985 and 1986. It also asked some of its lenders for an additional moratorium of 50% for 1987 through 1989 and/or reductions in interest payments. In return, the lenders were to receive common stock. *Id.*

190. *Id.* Wheeling-Pittsburgh proposed continuing the suspension of preferred stock dividends, eliminating pre-emptive rights, and diluting the stockholders' present holdings. *Id.*

191. *Id.* Wheeling-Pittsburgh asked the Steelworkers for a labor cost of approximately $19 per hour for three years and cancellation of the scheduled restorations. In return, the employees were to receive preferred or common stock. *Id.*

192. *Id.*

193. Brief for Appellant at 7, Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1074.

194. Wheeling-Pittsburgh v. Steelworkers, 791 F. 2d at 1077. The Steelworkers' counterproposal offered a two year contract with labor costs of $19.50 the first year and $20 the second year and cancellation of scheduled restorations. In return, the employees were to receive common stock and the right to appoint a member to Wheeling-Pittsburgh's Board of Directors. *Id.*

195. *Id.* Current assets consisted of accounts receivable and inventory, then worth $300,000 million. The lenders proposed to defer $210 million and lend an additional $40 million. *Id.*

196. *Id.*

197. *Id.*

their respective positions on the current assets.[198] The Steelworkers lost confidence in management's good faith and ability to protect their interests. Wheeling-Pittsburgh filed for relief under Chapter 11 on April 16, 1985.[199]

On May 9, 1985 Wheeling-Pittsburgh proposed to the Steelworkers the following modifications of the collective bargaining agreement: a five-year contract term; a maximum average labor cost of $15.20; elimination of the profit-sharing plan; reduction in medical and insurance benefits; elimination of supplemental and insurance benefits; and, elimination of various obligations including payments of the pension plan, redemption fund, and cash dividends on preferred stock.[200] Wheeling-Pittsburgh's projected business scenario for the next five years was becoming more pessimistic.[201]

The Steelworkers' financial consultants unsuccessfully sought certain financial data from Wheeling-Pittsburgh.[202] Notwithstanding Wheeling-Pittsburgh's ultimatum to either accept or reject the proposal, the Steelworkers maintained that they could not respond until their financial consultants received the information that they desired.[203] Wheeling-Pittsburgh moved to reject the collective bargaining agreement.[204]

The bankruptcy court used the nine-step analysis from *American Provision* for rejection.[205] First, the court recited that the debtor submitted a proposal and negotiated with the Steelworkers, pursuant to section 1113.[206] The court then rejected the Steelworkers' contentions that the debtor failed to confer in good faith to reach mutually satisfactory modifications. The Steelworkers asserted that Wheeling Pittsburgh "waited only three weeks after submitting the ... proposal to the Union before filing its section 1113 motion; and 2) that the Company refused to cooperate with the Union's financial experts with regard to the provision of information the Union needed to bargain...."[207] The Steelworkers averred that such behavior could not

198. *Id.*
199. *Id.*
200. *Id.* at 1077-78.
201. *Id.* at 1078.
202. *Id.*
203. *Id.*
204. *In re* Wheeling-Pittsburgh Steel Corp., 50 Bankr. 969 (Bankr. W.D. Pa. 1985).
205. 44 Bankr. 907; *see supra* text accompanying note 140.
206. *In re* Wheeling-Pittsburgh, 50 Bankr. at 975. The testimony on these points was unrebutted.
207. *Id.* at 976.

evidence good faith.[208] In response, the court noted that section 1113 "permits the debtor to file its application to reject any time after it submits its proposal."[209] The court also found the Steelworkers' contentions regarding the alleged failure to provide information unpersuasive.[210]

The court found, based on uncontradicted testimony, that Wheeling-Pittsburgh used the most complete and reliable information available to formulate its proposal.[211] The court then considered whether the proposed modifications were necessary for reorganization, and found that the $15.20 per hour labor cost and the five-year contract term were necessary because of the severity of Wheeling-Pittsburgh's financial difficulties and the "critical state of the United States steel industry."[212] The Steelworkers argued that lack of a clause raising the labor rate if Wheeling-Pittsburgh recovered, the "snap-back" clause, prevented all parties from being treated fairly and equitably.[213] The bankruptcy court disagreed.[214] It found that all parties were treated fairly and equitably under Wheeling-Pittsburgh's proposal because creditors and salaried employees also made sacrifices for the reorganization.[215] The bankruptcy court also found that Wheeling-Pittsburgh had given the Steelworkers sufficient information to evaluate the proposal.[216] Because the bankruptcy court believed that Wheeling-Pittsburgh satisfied the first seven factors of *American Provision*,[217] it found that the Steelworkers refused to accept the debtor's proposal without good cause.[218] Lastly, the court found that the balance of equities clearly favored rejection because

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208. *Id.*
209. *Id.*
210. *Id.* at 976-77. The Steelworkers contended that Wheeling-Pittsburgh failed to provide their financial consultants with a requested plant tour and review the explanation of its wage and cost system. The court stated that Wheeling-Pittsburgh, for reasons of convenience, only delayed, and did not deny, the plant tour. With respect to the explanation of the wage and cost system, the court found that the Steelworkers had obtained substantially similar information when Wheeling-Pittsburgh sought concessions in late 1984 and early 1985. *Id.*
211. *Id.* at 977.
212. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1080.
213. *Id.*
214. *Id.*
215. *Id.* at 1081.
216. *Id.* The court stated that the Steelworkers' financial experts already possessed a wealth of information from previous concession. *Id.*
217. *In Re* Wheeling-Pittsburgh, 50 Bankr. at 975-83.
218. *Id.* at 983.

"[r]ejection ... will have a significant and positive effect on Wheeling-Pittsburgh's prospects for reorganization."[219]

On July 17, 1985, the bankruptcy court issued an opinion authorizing Wheeling-Pittsburgh to reject the contract.[220] Shortly thereafter, Wheeling-Pittsburgh rejected the agreement, cutting the labor cost to $17.50 and implementing several other changes.[221] On July 21, 1985, the Steelworkers struck Wheeling-Pittsburgh.[222]

During the strike, the Steelworkers appealed the decision of the bankruptcy court.[223] The district court emphasized three issues in affirming the bankruptcy court.[224] First, the district court agreed with the bankruptcy court that "necessary" does not mean "absolutely essential".[225] Second, the district court upheld the bankruptcy court's conclusion that all parties would be treated "fairly and equitably,"[226] and third, the district court let stand the bankruptcy court's finding that Wheeling-Pittsburgh conferred in good faith, although it noted that there was evidence of record to refute bankruptcy court's finding.[227] The court also commented that the twenty-two day period between the proposal to modify the collective bargaining agreement and the motion to reject, which the Steelworkers found so objectionable, was not "inherently unreasonable since section 1113 has no time restraint relative to when the debtor, following the submission of a proposal, may file its rejection application."[228] The Steelworkers then filed a timely appeal to the United States Court of Appeals for the Third Circuit.[229]

On October 15, 1985, after an eighty-seven day strike, while the appeal to the Third Circuit was still pending, the parties reached a tentative agreement.[230] The agreement provided for hourly labor costs

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219. *Id.*
220. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1078.
221. *Id.*
222. *Id.*
223. *In re* Wheeling-Pittsburgh Steel Corp., 52 Bankr. 997 (W.D. Pa. 1985).
224. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1081.
225. *In re* Wheeling-Pittsburgh, 52 Bankr. at 1003. The court stated that Congress envisioned the "necessary" standard as a "more practical long range test of a less stringent nature." *Id.*
226. *Id.* at 1005.
227. *Id.* at 1005-06. The district court did not indicate the evidence to which it was referring.
228. *Id.* at 1006.
229. Wheeling-Pittsburgh Steel v. Steelworkers, 791 F.2d 1074.
230. *Id.* at 1078.

of $18 per hour.[231] During the strike, the plant guards at the various Wheeling-Pittsburgh facilities, who were also represented by the Steelworkers, remained on the job, as required by the former collective bargaining agreement. During this time, Wheeling-Pittsburgh paid them at the unilaterally imposed wage scale of $17.50 per hour. The company and the Steelworkers did not resolve this dispute. It involved approximately forty-five employees and approximately $146,000. However, the parties agreed that if rejection of the contract was reversed on appeal, the Steelworkers would assert administrative expense claims[232] on behalf of the employees who worked during the strike.

It is an understatement that the strike was acrimonious[233] and involved a strong personality clash. The strike was not settled until Wheeling-Pittsburgh chairman and chief executive officer, Dennis J. Carney, the antagonist to the Steelworkers, was removed.[234] The atmosphere surrounding the strike is relevant. During the early months, the animosity between the parties prevented productive bargaining. The circumstances were inflammatory. The company perceived that the court, by rejecting the contract, would resolve the company's problem. The history of American labor relations does not support that thesis. Labor negotiations occur at the bargaining table. Courts clearly do not settle labor disputes by judicial process. The bankruptcy court did not resolve the economic dispute in *Wheeling-Pittsburgh*. At best, a motion to reject the contract is an invitation to bargain. The court of appeals' opinion set the standard for rejection, but it was a moot issue. The parties had agreed to a new interim contract seven months before the court of appeals issued its decision.

Because the strike was settled before the court of appeals heard the case, the bank creditors actually argued that the issue was moot.[235]

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231. Wall St. J., October 15, 1985, at 8, col. 1. The agreement contained an escalator clause which would raise labor rates to $19 per hour based on steel prices and the company's cash flow.

232. 11 U.S.C. § 503(a)(1)(A) (1982). These expenses include "the actual necessary costs and expenses of preserving the estate, including wages, salaries, or commissions for various services rendered after the commencement of the case...." *Id.*

233. One of the co-authors had the opportunity to observe portions of the settlement efforts. At times, representatives of Wheeling-Pittsburgh management and the Steelworkers would not agree to be in the same room. Such conditions are hardly conducive to a rapid settlement.

234. Wall St. J., September 23, 1985 at 3, col. 3.

235. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1079.

The court disagreed.[236] First, the court remarked that settling a controversy does not render moot an unresolved sub-issue of the controversy."[237] The court dismissed the bank's contention that the issue of the wage differential of the plant guards was deliberately left open by the company and the union as a "mere contrivance."[238] The banks argued that the Steelworkers had "an interest in securing a ruling on the merits of the appeal above and beyond the satisfaction of the plant guards' claims...."[239] However, the Steelworkers indicated that they would accept settlement that paid the full amount of the plant guards' claim, even if it meant withdrawal of the appeal.[240] The court emphatically refused to believe the banks' assertion that if the parties were able to negotiate a labor contract estimated at $360 million dollars, they should have been able to compromise on $146,000.[241]

The court placed a greater emphasis on the $146,000 than the banks did: "That sum is not *de minimis* for any company, and particularly not for a bankrupt one."[242] In this context, the authors disagree with the court of appeals' characterization of the disputed $146,000. Although $146,000 is not *de minimis* in absolute terms, it was a *de minimis* part of the substantive dispute over rejection of Wheeling-Pittsburgh's plans for a reorganization. The legal resources required to prosecute the appeal were significant. The appeal squandered time and resources, which could have been used to formulate a plan of reorganization.[243]

Turning to substantive issues, the Third Circuit Court of Appeals held that the bankruptcy court used the incorrect standard of necessity.[244] The court of appeals equated "necessary" with "essential". The court did find that the bankruptcy court and district court used the correct standard for determining whether Wheeling-Pittsburgh's

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236. *Id.* at 1079-80.

237. *Id.* As support, the court cited Powell v. McCormack, 395 U.S. 486 (1969) (seating of a member does not render moot his suit against the House of Representatives for failure to seat him). *Id.*

238. *Id.* at 1079.

239. *Id.* at 1080. The Steelworkers admitted that they desired a favorable ruling for its precedential value.

240. *Id.* at 1079. This fact was developed through discovery.

241. *Id.*

242. *Id.*

243. As of February 29, 1988, Wheeling-Pittsburgh had not filed a plan of reorganization; it had been granted several extensions for filing its plan.

244. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1088, 1090-91.

proposal treated all of the parties "fairly and equitably," but that they misapplied the standard.[245]

In determining that "necessary" is synonymous with "essential", the court reviewed the legislative history of section 1113 and discussed the three proposals that it perceived: the Rodino proposal,[246] the Thurmond substitute,[247] and the Packwood amendment.[248] The court focused on the language of the Packwood amendment, which "provided that the debtor's proposal should contain 'the minimum modifications in such employees' benefits and protections that would permit the reorganization'."[249] The court found that the language of section 1113 as it was adopted, ("that the debtor's provide for those necessary modifications in the employees' benefits and protections that are necessary to permit the reorganization of the debtor")[250] was "a substitute"for the aforementioned clause of the Packwood amendment.[251] The court found support for its position in "[t]he contemporaneous remarks of the conferees [which] made it clear that the provision was based on the substance of Senator Packwood's proposal."[252] The remarks of various other members of Congress, as well as Senator Packwood, satisfied the court that Congress intended that "the substantive standard of *Bildisco* be overturned and that the *REA Express* standard, or something similar, be reinstated."[253] The *REA Express* standard, it should be remembered, provided for rejection only as a last resort if the debtor is in imminent danger of collapse and the employees are threatened with a loss of their jobs.[254] Thus, the court believed "necessary", as it was used in section 1113, meant "essential".[255]

The court of appeals' decision, in large part, relied upon legislative history. There is an absence of the traditional explanatory statements or reports associated with such legislative history, and thus the legislative history is unreliable. Other courts have not found that the

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245. *Id.* at 1091-93.
246. *See supra* note 5 and accompanying text.
247. *See supra* text accompanying notes 77-79.
248. *See supra* text accompanying note 81.
249. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1087.
250. *Id.* at 1087 (quoting 11 U.S.C. § 1113(b)(1)(A) (Supp. IV 1986)).
251. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1087.
252. *Id.*
253. *Id.* at 1088 (citing Ehrenwerth & Lally-Green, *supra* note 91, at 953-54, Gibson, *supra* note 4, at 337-30).
254. *See supra* text accompanying note 40.
255. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1088.

legislative history demonstrates an intent to adopt the *REA Express* standard.[256]

The court noted that "essential" appeared in another subsection of section 1113[257] but did not attach any significance to this. The court stated that to argue that "necessary" and "essential" have different meanings because they appeared in different subsections of section 1113 was a "hyper-technical argument."[258] The court also discounted the importance of the statement of Senator Hatch, who viewed section 1113 as a return to the *Bildisco* decision.[259]

After the court defined "necessary", it asked "necessary" to what? Although the statute says "necessary to permit the reorganization of the debtor",[260] the court believed that the long term rehabilitation of the debtor was not the concern of the conferees.[261] Rather, the court of appeals determined that Congress was concerned with "a somewhat shorter term goal of preventing the debtor's liquidation."[262] Congress' use of the phrase "permit the reorganization" indicated to the court of appeals that Congress intended to emphasize the immediate future, rather than the long term future of the debtor.

The court also remarked "that the requirement that the debtor's proposal contain only 'necessary' modifications ... is conjunctive with the requirement that the proposal treat 'all the affected parties ... fairly and equitably'."[263] Such language and the legislative history, the court found, would prevent a court from allowing rejection merely out of equity to the parties.[264]

The court of appeals then applied its definition of "necessary" to those items in Wheeling-Pittsburgh's proposal which the Steelworkers found to be objectionable: the five-year contract term; the "worst case" scenario underlying Wheeling-Pittsburgh's projections; and, the lack of a "snap back" clause.[265] With respect to the five-year

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256. *See supra* text accompanying notes 108-112; *see also* Note, *The Standard for Rejection of Collective Bargaining Agreements by Chapter 11 Debtors—Wheeling-Pittsburgh Steel Corp. v. United Steelworkers*, 60 TEMP. L.Q. 757, 786 (1987).

257. 11 U.S.C. § 1113(e) (Supp. IV 1986).

258. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1089.

259. *Id.*

260. 11 U.S.C. § 1113(b)(1)(A) (Supp. IV 1986).

261. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1089.

262. *Id.* at 1090. The district court opinion discussed necessity in the context of "prevention of the debtor going into liquidation." *In re* Wheeling-Pittsburgh, 52 Bankr. at 1003. Nevertheless, the court of appeals criticized the district court for approving the standard of "necessity" used by the bankruptcy court.

263. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1089.

264. *Id.*

265. *Id.*

contract term, the Steelworkers presented uncontradicted evidence in the proceedings before the bankruptcy court that neither Wheeling-Pittsburgh nor the American steel industry generally used a five-year contract term.[266] Nevertheless, the bankruptcy court found the five-year term necessary because it anticipated that the reorganization of Wheeling-Pittsburgh would take at least five years, and that labor stability would be crucial during that time.[267] On the basis of the record, the court of appeals was unable to agree that the five-year term was necessary.[268]

The court of appeals was less critical of the bankruptcy court's use of Wheeling-Pittsburgh's pessimistic five-year projection, rather than the more optimistic projection offered by the Steelworkers.[269] As support for Wheeling-Pittsburgh's position, the bankruptcy court found that the domestic steel industry was in poor condition.[270] The court of appeals agreed with the bankruptcy court's characterization of the American steel industry.[271]

The court of appeals was most critical of the bankruptcy court for its failure to consider a "snap back" provision in its analysis of necessity, although the court of appeals noted that the bankruptcy court discussed the absence of a "snap back" provision in its analysis of fair and equitable treatment.[272] Considering the lack of a "snap back" clause together with a five-year contract term and the pessimistic five-year projection of Wheeling-Pittsburgh, the court was unable to accept the bankruptcy court's finding of necessity and therefore remanded the case to the bankruptcy court.[273]

The court of appeals then changed the emphasis of its analysis of the lack of a "snap back" clause.[274] It determined that the lack of such clause in conjunction with a five-year agreement, based on pessimistic projections, meant that the employees would not be

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266. *Id.*

267. *In re* Wheeling-Pittsburgh, 50 Bankr. 979. The bankruptcy court stated that "there is no evidence as to how labor stability can be achieved with a contract of less that five years' duration."

268. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1092.

269. *Id.*

270. *In re* Wheeling-Pittsburgh, 50 Bankr. at 978. The bankruptcy court recited a list of the problems then facing the domestic steel industry. *Id.*

271. Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1090.

272. *Id.*

273. *Id.* at 1090-91. The court of appeals also held that the district court erred by treating the bankruptcy court's findings of necessity as merely findings of fact, subject to the "clearly erroneous" standard of review. *Id.* at 1091.

274. *Id.*

treated "fairly and equitably" if Wheeling-Pittsburgh's performance improved during the contract term. Although the bankruptcy court used the correct standard for fair and equitable treatment, whether Wheeling-Pittsburgh's proposal would impose a disproportionate burden on the employees, the court of appeals agreed with the Steelworkers' assertion that the bankruptcy court incorrectly applied that standard.[275] According to the court of appeals, the bankruptcy court erroneously found that Wheeling-Pittsburgh's proposal was fair and equitable, even though the employees would not share in any improvement in the company's position.[276]

It is interesting to note that the actual negotiated agreement which the company and the Steelworkers adopted was an interim type agreement.[277] It required renegotiation at the time of the adoption of a reorganization plan. It permited the Steelworkers to bargain again when the company presented a plan. At that time, the union would be able to recover previous concessions. The court of appeals' argument for a "snap back" fails to take into consideration the claim a union can file for rejection and the short term of most labor agreements.

C. *The Second Circuit Differs—Truck Drivers Local 807 v. Carey Transportation*

The Second Circuit is the only other court of appeals to apply section 1113. In *Truck Drivers Local 807 v. Carey Transportation (In re Carey Transportation)*,[278] the Court of Appeals for the Second Circuit unequivocally differed with the Third Circuit's interpretation of "necessary" and "fairly and equitably".[279] In that case, Carey Transportation ("Carey") operated a bus service between New York

275. *Id.* at 1092.

276. *Id.* The bankruptcy court dismissed such concerns by noting the proposal did not provide for adjusting labor costs downward if Wheeling-Pittsburgh performed worse than it projected. The district court failed to independently evaluate the fair and equitable nature of Wheeling-Pittsburgh's proposal. *In re* Wheeling-Pittsburgh, 50 Bankr. at 980.

277. *Id.*

278. 816 F.2d 82 (2d Cir. 1987).

279. Previously, in Century Brass Products, Inc. v. International Union, United Automobile, Aerospace and Agricultural Implement Workers of America (In re Century Brass), 795 F.2d 265 (2d Cir. 1986), the Second Circuit discussed § 1113, without reaching the merits of the debtor's application for rejection. The court stated that the Third Circuit, in *Wheeling-Pittsburgh*, misconstrued the nature of § 1113 as favoring labor law principles over bankruptcy principles. *Id* at 276.

City and the major New York airports.[280] In the years preceding 1985, when it filed for relief under Chapter 11, Carey suffered increasing operating losses.[281] Carey obtained concessions from the union representing its mechanics and from other creditors, but was unable to obtain significant concessions from Local 807.[282] Shortly after Carey filed its Chapter 11 petition, it proposed to modify the collective bargaining agreement with Local 807.[283] The membership of Local 807 opposed the proposed changes, and refused to negotiate despite the urgings of union officials.[284] Thereafter, Carey filed a petition to reject the contract under section 1113.[285] The bankruptcy court granted the petition and was affirmed by the district court.[286] Local 807 appealed.[287]

After briefly discussing the scope of review,[288] the Second Circuit Court of Appeals noted that the debtor must make three substantive showings before rejection can be allowed: (1) the proposal is limited to "those necessary modifications ... that are necessary to permit the reorganization" and treats "creditors, the debtor and all affected parties ... fairly and equitably,"[289] (2) "[t]he union has rejected this proposal without good cause,"[290] and (3) "the balance of the equities clearly favors rejection...."[291]

Turning to the issue of necessity, the court asked the same questions that the Third Circuit did in *Wheeling-Pittsburgh*: "[H]ow necessary must the proposed modifications be, and ... to what goal must those alterations be necessary?"[292] The Second Circuit's answer differed

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280. Local 807 v. Carey Transp., 816 F.2d at 85.

281. *Id.*

282. *Id.* The Teamsters represented Carey's drivers and station employees. In 1984, the Teamsters agreed to a two-tier wage system, allowing for reduced wages and benefits to employees hired after July 1, 1984, but these concessions yielded insignificant savings. *Id.*

283. *Id.* at 86.

284. *Id.*

285. *Id.*

286. *In re* Carey Transp., 50 Bankr. 203 (Bankr. S.D.N.Y. 1985). The district court did not publish an opinion.

287. Local 807 v. Carey Transp., 816 F.2d at 87.

288. *Id.* at 88. The court disagreed with Local 807 that the matter was subject to *de novo* review because it involved mixed questions of law and fact. The court of appeals held that the bankruptcy court's interpretation of § 1113 was subject to plenary review, but any findings of fact were subject to the clearly erroneous standard. *Id.*

289. *Id.* (quoting 11 U.S.C. § 1113(b)(1) (Supp. IV 1986)).

290. *Id.*

291. *Id.* (quoting 11 U.S.C. § 1113(c)(3) (Supp. IV 1986)).

292. *Id.*; *See also* Wheeling-Pittsburgh v. Steelworkers, 791 F.2d at 1088.

sharply from that of the Third Circuit. First, the Second Circuit refused to equate "necessary" with "essential".[293] Local 807 argued that the proposed changes were not "necessary" because they resulted in savings that exceeded the debtor's break even point, because of the length of the contract, and because of the failure to include a "snap back" clause.[294] The court of appeals interpreted the legislative history to find that Congress did not adopt the Packwood amendment[295] which provided for "minimum modifications." Rather, the court believed that Congress adopted the "necessary" language as a substitute for the "minimum modifications" language of the Packwood proposal.[296]

The court of appeals also approved of the additional reason the bankruptcy court used to find that "necessary" and "essential" were not synonymous.[297] Bankruptcy Judge Lifland declared that section 1113 required the debtor to bargain in good faith.[298] If the debtor proposed absolute minimal changes, as Local 807 urged, it would not have had room to bargain or negotiate. However, if it agreed to significant changes during the bargaining process, it would be unable to prove that its initial proposal was limited to essential changes.[299]

The Court of Appeals for the Second Circuit also found the Third Circuit's answer to the question of "'necessary to what'... troubling."[300] The court criticized the Third Circuit's failure to distinguish interim relief from other post-petition modification attempts. Totally departing from the position of the Third Circuit in *Wheeling-Pittsburgh*, the court held that the proper consideration, in situations not involving interim relief, is "whether rejection would increase the likelihood of reorganization."[301] Such an inquiry requires "looking into the debtor's ultimate future and estimating what the debtor needs to attain financial health,"[302] and necessarily will not be limited to minimal changes.

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293. Local 807 v. Carey Transp., 816 F.2d at 89.

294. *Id.* The debtor requested a three-year contract extension. The existing agreement was to expire in eight months. The length of the contract term and the lack of a "snap back" proposal were not raised in the lower courts, and thus could not be raised on appeal. *Id.* at 90.

295. *See supra* text accompanying note 81.

296. Local 807 v. Carey Transp., 816 F.2d at 89.

297. *Id.*

298. *In Re* Carey Transp., 50 Bankr. at 209.

299. *Id.*

300. Local 807 v. Carey Transp., 816 F.2d at 89.

301. *Id.*

302. *Id.* As an example, the debtor's proposed modifications provided for

In assessing whether the debtor's proposal treated Local 807's employees "fairly and equitably", the court noted that the debtor need not show that managers and non-union employees underwent the same diminution of wages and benefits as experienced by the union employees.[303] Although such a comparison would be easy, it would be unnecessary when the debtor could make other showings that the union members were being treated fairly and equitably.[304] In *Carey*, non-union employees had their responsibilities increased as a result of staff cuts, without a commensurate salary increase.[305] Carey's union employees were paid significantly more than the equivalent employees of Carey's competitors, while the salaries of Carey's managers and supervisors were barely competitive.[306] The court of appeals also viewed the pre-petition concessions by other parties as an indicator that those other parties had contributed fairly and equitably. Thus, the court of appeals could not hold that the bankruptcy court erred in evaluating the burdens imposed on all of the parties.[307]

The Court of Appeals for the Second Circuit agreed with the bankruptcy court that Local 807 rejected Carey's proposal without good cause.[308] The bankruptcy court concluded that Local 807 lacked good cause because the debtor's proposal was necessary and fair and equitable.[309] The court of appeals expanded on the bankruptcy court's reasoning, noting that Local 807 refused to participate in meaningful post-petition negotiations and offered no reason for rejection other than it believed that the debtor's proposals were excessive.[310] If such conduct was held to be good cause, the union would be able to

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savings which greatly exceeded the debtor's break even point. Nevertheless, the court recognized that such rejections were necessary, so that the debtor could modernize its fleet and facilities. Query whether debtors should be able to make capital improvements while in bankruptcy?

303. *Id.* at 90.

304. *Id.*

305. *Id.* at 91.

306. *Id.*

307. *Id.* Local 807 also had objected that the treatment of the debtor's parent corporation was unfair to the other creditors. The court ruled that a creditor who was also an owner of the debtor need not take a smaller percentage dividend than the other creditors: "The mere fact that there have been intercompany transactions between a debtor and its owner is not a source of unfairness to other creditors unless the transactions themselves were financially unfair to the debtor." *Id.*

308. *Id.* at 92.

309. *Id.*

310. *Id.*

"stonewall" post-petition negotiations with the hope that the court would later find the debtor's proposal more than "necessary" or not "fair and equitable".[311] This tactic was not what Congress envisioned when it included the "good cause" requirement.[312]

Finally, the Second Circuit Court of Appeals agreed with the bankruptcy court's finding that the balance of equities favored rejection.[313] The court noted that since section 1113 codified the requirement of *Bildisco* that the equities balance, the factors identified in *Bildisco* and in other cases preceding the enactment of section 1113 were still applicable.[314] The court did, however, disagree with the bankruptcy court's holding that allegations of the debtor's bad faith were inappropriate to an objection to a section 1113 application.[315]

D. *Trends in the Application of Section 1113*

Although the case law of section 1113 is not fully developed, it has suggested some trends. The courts generally have been unsympathetic to unions who have refused to participate in meaningful pre-application negotiations. For example, in *In re Royal composing Room, Inc.*,[316] the court granted the debtor's application to reject because it was dissatisfied with the union's attempt to reach voluntary modifications. The Court disapproved of the frequency and duration of the bargaining sessions, which it attributed to the union and considered the union's position "essentially a stonewall ..." which "favors the grant of the debtor's motion for rejection."[317] Not only

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311. *Id.*

312. *Id. But see* Gibson, *supra* note 4, at 34.

313. Local 807 v. Carey Transp., 816 F.2d at 92-93.

314. *Id.* at 92. The court listed six equitable considerations:

> (1) [T]he likelihood and consequences of liquidation if rejection is not permitted; (2) the likely reduction in the value of creditor's claims if the bargaining agreement remains in force; (3) the likelihood and consequences of a strike if the bargaining agreement is voided; (4) the possibility and likely effect of any employee claims for breach of contract if rejection is approved; (5) the cost-spreading abilities of the various parties, taking into account the number of employees covered by the bargaining agreement and how various employees' wages and benefits compare to those of others in the industry; and, (6) the good or bad faith of the parties in dealing with the debtor's financial dilemma.

Id. at 93.

315. *Id. See infra* note 342 and accompanying text.

316. 62 Bankr. 403 (Bankr. S.D.N.Y. 1986).

317. *Id.* at 408; *see also* Local 807 v. Carey Transp., 816 F.2d at 91-92; *supra* text accompanying notes 311-12.

did the union refuse to participate in meaningful negotiations, but it did not "articulate and discuss in detail ... its reasons for declining ... the debtor's proposal in whole or in part."[318] The court equated such behavior with lack of good cause for refusing the debtor's proposal. Similarly in *In re Kentucky Truck Sales, Inc.*,[319] the union's refusal to negotiate away medical coverage, as a matter of policy, was not good cause for rejecting the debtor's proposal.[320] As was the case in *Royal Composing Room*, the union in *Kentucky Truck Sales* also did not make a pre-hearing counteroffer.

On the other hand, rejection has not been permitted when the debtor has been lax in fulfilling its bargaining obligations. In *In re American Provision*,[321] the court refused to allow rejection when, *inter alia*, it found that the debtor engaged in only perfunctory bargaining efforts which were not within the spirit of section 1113.[322] The court noted that the debtor and the union met only once, although the union had indicated a willingness to continue discussions.[323] In *In re K & B Mounting*,[324] the court refused to grant the debtor's application to reject when the debtor and the union had not negotiated face-to-face. Just as some courts have held that a union must articulate specific reasons why it is rejecting the debtor's proposal, the debtor must also be specific.[325] The debtor cannot rely "on a simplistic presentation of a need to reduce labor costs to become more competitive."[326]

Courts have allowed rejection when faced with easily quantifiable economic data which indicates that labor costs are excessive either in relation to the debtor's revenues or in comparison to other employers within the industry.[327] In *In re Amherst Sparkle Market*,[328] the court allowed rejection when the debtor's labor costs equalled

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318. 62 Bankr. at 407.
319. 52 Bankr. 797 (Bankr. W.D. Ky. 1985).
320. *Id.* at 805.
321. 44 Bankr. 907.
322. *Id.* at 911.
323. *Id.*
324. 50 Bankr. 460.
325. *Id.*
326. Sheet Metal Workers International Association, Local No. 9 v. Mile Hi Metal Systems, Inc. (In re Mile Hi Metal Systems, Inc.), 67 Bankr. 114, 118 (D. Col. 1986); *see also In re* K & B Mounting, 50 Bankr. 464-67; *supra* text accompanying notes 156-160.
327. *See, e.g., In re* Allied Delivery, 49 Bankr. at 702; *supra* text accompanying note 172.
328. 75 Bankr. 847 (Bankr. N.D. Ohio 1987).

13.08% of sales versus an industry average of 8.6%.[329] In *In re Royal Composing Room*,[330] the court allowed rejection when the debtor's labor costs were excessive when compared to the industry.[331] The debtor was unable to compete because it was one of the few remaining union shops in that particular industry. Even when labor costs may be average for an industry, rejection may be allowed when they comprise a disproportionate percentage of the debtor's fixed overhead.[332] However, when labor costs under the collective bargaining agreements are minimal, the court may find that the debtor's proposal is not necessary to its reorganization.[333]

Numerous courts have allowed rejection when the debtor has cut all other possible costs before seeking rejection.[334] Indeed, one court has commented that rejection of a collective bargaining agreement, in light of the "history of the collective bargaining agreement and its special treatment and protection,"[335] should be considered a last resort. Generally, by the time the debtor seeks rejection of the collective bargaining agreement, all of the other employees will have been subjected to reductions in wages and benefits.[336] This showing will often be crucial if the court is to find that the debtor's proposal treats all parties fairly and equitably. However, this does not always need to be the case.[337]

Inclusion of a "snap back" clause is one method of ensuring that the debtor's proposal treats all parties "fairly and equitably." However, except for the Third Circuit, other courts have not required

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329. *Id.* at 851.

330. 62 Bankr. 403.

331. *Id.* at 412.

332. *In re* Kentucky Truck Sales, 52 Bankr. at 803 n.16.

333. *See American Provision*, 44 Bankr. at 910; *supra* text accompanying note 150.

334. *In re* Kentucky Truck Sales, 52 Bankr. 797, 802 ("[P]roposed concessions were critical if the company wished to survive as a viable business entity."); *In re Royal Composing Room*, 62 Bankr. at 412 ("Union labor cost ... is the only expense that has not been cut in the last four years."); *In re* Walway Co., 69 Bankr. 967, 973 (Bankr. E.D. Mich. 1987) ("[T]he debtor has shown that cost-saving cuts have been made in other areas, and that these measures did not increase the company's chances of survival. The last measure sought by the debtor was the modification of the labor contract.").

335. *In re* Walway, 69 Bankr. 973 n.15.

336. *See, e.g., In re* Amherst Sparkle Market, 75 Bankr. 847; *In re* Kentucky Truck Sales, 52 Bankr. 797.

337. *In re* Royal Composing Room, 62 Bankr. 403 (Executives' compensation was justified because of their indispensability to the corporation and the availability of more lucrative opportunities).

this result. One court has observed that there is no authority mandating a "snap back" clause.[338] The Third Circuit in *Wheeling-Pittsburgh* was concerned that the Steelworkers receive a *quid pro quo* in exchange for the concessions sought by the company. A bankruptcy reorganization plan most often requires concessions from many creditors. Labor agreements are usually two-three years in terms, providing an opportunity to redress an unfavorable contract. Retention of the employees' jobs, even at a reduced wage, has a high priority for the employees. Retention of the employees' jobs becomes their *quid pro quo*.

The actual experience indicates that rejection of the collective bargaining agreement has not been used as an offensive tactic in labor relations. The various equitable requirements of section 1113 reinforce that experience and prevent employers from using it in this manner. This result was clearly intended by Congress. The debtor who files an application to reject the collective bargaining agreement with an anti-union animus, faces the prospect of having its bankruptcy petition dismissed and its application for rejection denied. Section 1112(b) of the Bankruptcy Code[339] empowers a party in interest to seek conversion to Chapter 7 or dismissal for cause. Although the Bankruptcy Code does not specifically empower courts to dismiss cases filed in bad faith, there is precedent for this course of action[340] and such an interpretation is consistent with the legislative history.[341] To date, there are no reported decisions in which a union has successfully moved for dismissal because of a bad faith filing. However, courts have recognized that a bankruptcy filing for the purpose of eliminating a union may be a bad faith filing subject to dismissal.[342]

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338. *In re* Walway, 69 Bankr. at 974.

339. 11 U.S.C. § 1112(b) (1982 & Supp. IV 1986).

340. *See, e.g.*, *In re* Little Creek Development Co., 779 F.2d 1068 (5th Cir. 1986); *In re* Southern California Sound Systems, Inc., 69 Bankr. 893 (Bankr. S.D. Cal. 1987).

341. 130 Cong. Rec. H7496 (daily ed. June 29, 1984) (statement of Rep. Morrison). "[I]t was also our understanding that a Chapter 11 reorganization case that is brought for the sole purpose or (sic) repudiating or modifying a collective bargaining agreement is a case brought in bad faith." *Id.*

342. *See, e.g.*, *In re* Continental Airlines Corp., 38 Bankr. 67, 71 (Bankr. S.D. Tex. 1984). "That one of the intentions of the debtor was to seek rejection of their collective bargaining agreements insofar as that may be allowed under the provisions of Title 11, does not, under these facts, result in the filing being 'in bad faith....'"; *In re* Carey Transp., 50 Bankr. 203, 212 (Bankr. S.D.N.Y. 1985). ("[T]he ... claim that the case was filed solely to jettison [the] union contract ... is

IV. THE NECESSITY OF BARGAINING—LABOR PEACE REQUIRES GOOD FAITH NEGOTIATIONS, NOT LEGAL PROCESS

In the United States, judicial process has not proved salutary in resolving labor management matters. It is unreal to expect precise results when the judicial process is involuntarily applied to labor management negotiations. It is not clear that the drafters of section 1113 expected it to be so used. This same economic unreality is also present when non-labor bargaining is forced into the courtroom. The reorganization process envisions that the parties will negotiate most matters in good faith. Reliance on the judicial process may actually delay the inevitable bargaining process if it encourages the parties to think that they need not bargain and that the courts will provide an answer.

The ultimate economic answer lies in the market place. Well-informed, good faith bargaining should approximate the market place. Although the judicial process can also approximate the market place, it is clumsy and restrictive and enforcement is not possible when labor is the creditor.

When this bargaining process has been unsuccessful, bringing the dispute to the courtroom in the form of a section 1113 rejection does not resolve much. It can harden positions and waste valuable time.

In enterprises which are labor intensive, the employees tend to be represented by a strong union. In such enterprises labor leaders should become major participants in the economic bargaining that must occur among all the creditors. Without labor's broad participation, a successful reorganization is unlikely. The consequences of a failure to bargain and reorganize are great. Failure means that secured creditors will receive poor value for their collateral, active employees will lose their jobs, retired employees will lose part of their pensions, and unsecured creditors will lose everything. Chapter 11 reorganization procedures consist of a series of guidelines, backed by legal authority, designed to encourage *voluntary* modification by creditors of their previous "legal" rights. It is intended to maximize

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more appropriate fodder for dismissal considerations under § 1112(b) of the Code, or for a motion by a party in interest such as the Union here ... to appoint a trustee or examiner under Code § 1104.", *aff'd*, Truck Drivers Local 807 v. Carey Transp., Inc., 816 F.2d 82. The court of appeals did note that allegations of bad faith were appropriate to an objection to a § 1113 application as well as the basis for a motion to dismiss or to appoint a trustee or examiner.

over the longer term the actual return to be received by all creditors. It is based on realistic self interest. Each creditor group must analyze their prospects under the plan and vote yes or no.[343]

However, labor is a unique creditor. Labor creditors are not completely subject to a two-thirds majority vote[344] and the cram down[345] provisions because of their strike power. Rejection of the labor contract does not change the designated bargaining agent or unit. The union continues to exist and is free to strike. An active and strong union will require a new contract.

Further, rejection of the pre-petition labor contract does not determine the actual economic provisions to be adopted in the post-petition labor contracts. Most labor contracts are limited to relatively short periods of time, such as one, two, or three years. Success of the reorganized enterprise offers new opportunities to renegotiate contracts in the future. This is not the case for other creditors.

It should be obvious (but it has not been) that unless a new labor agreement is negotiated, a strong labor organization will strike when their contract is rejected. In an ongoing business, a strike is likely even if the courts determine by strict standards that rejection is appropriate. Strongly represented employees are conditioned to work only when a contract is in place. The Bankruptcy Code does not provide the court with unique ability to prevent such a strike.

This may not be the condition when the union is disorganized. A weak or disorganized union may be forced to accede to rejection and to the debtor's proposal. Obviously, in these situations, the court should proceed carefully so as to maintain the needed equity balance. The early cases, which provoked labor leaders, involved relatively disorganized responses by the labor organizations. It is not really accurate to attribute those concessions to the bankruptcy contract rejection power alone. A union that cannot maintain an effective

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343. 11 U.S.C. § 1126(a) (1982).

344. 11 U.S.C. § 1126(c) (1982). This section provides that a class of claims has accepted a Chapter 11 plan of reorganization if "at least two-thirds in amount and more than one-half in number of the allowed claims of such class," which actually vote, accept the plan.

345. 11 U.S.C. § 1126(b)(1) (1982 and Supp. IV 1986). This section provides that the bankruptcy court shall confirm the plan, even if all classes of creditors have not voted for confirmation, if at least one impaired class of claims has voted to accept the plan, "the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan. This section is commonly referred to as the "cram down" provision.

strike as a last resort has lost its ultimate bargaining weapon. Other economic factors should be examined to explain the union's disorganized response in the early cases. By itself, the bankruptcy power to reject the labor contract does not explain the result.

In industries with strong union traditions, such as the steel industry, attempts to reject the contract without a concurrent renegotiation are sterile exercises. In *Wheeling-Pittsburgh*, after rejection and a long strike, a new interim contract was negotiated.[346] Without a renegotiated contract, the company had little hope of developing the plan of reorganization.

In *Wheeling-Pittsburgh*, the need for a new labor contract became an economic necessity and an actual fact before the court of appeals determined that the rejection of the contract had occurred without the required standard of legal precision. Surely in an economic sense the court of appeals decided an economic issue that was moot. If the strike continued and the parties waited seven months until the court of appeals decided the standard for rejection, the most likely result would have been liquidation. Conversely, if the bankruptcy court had not rejected the contract and the union not renegotiated the contract, the result would also have been liquidation. These economic facts provide the legal result with an unreal quality. This is likely to be so in many other cases, because reorganization is essentially an economic process.

In the LTV bankruptcy, the parties may have learned from the Wheeling-Pittsburgh experience.[347] The contract was amicably renegotiated. In LTV, labor and management avoided the pitfalls of the legal process.[348] Whether the labor contract which was renegotiated avoided the economic problems faced by LTV is yet to be determined.

It is important to observe that these renegotiated contracts are also of an interim nature. The contracts are limited to a time near the

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346. *See supra* text accompanying notes 219-231.

347. LTV Corp., a conglomerate which includes the nation's second largest steel manufacturer, filed for relief under Chapter 11 on July 17, 1986.

348. Query how much has LTV learned? Although it was able to renegotiate its collective bargaining agreement, it caused labor unrest and litigation by unilaterally terminating the life insurance and health benefits of its retirees. *See* United Steelworkers of America v. LTV Corp. (*In re* Chateaugay Corp.), 76 Bankr. 937 (Bankr. S.D.N.Y. 1987). In response, Congress passed stop-gap legislation to reinstate the benefits. Congress is currently considering legislation to limit the ability of a debtor in possession to terminate insurance benefits to retirees. *See* H.R. 2969, 100th Cong., 1st Sess., 133 Cong. Rec. H8552 (daily ed. Oct. 13, 1987); 133 Cong. Rec. S15590 (daily ed. Oct. 30, 1987).

confirmation of the plan. *Therein lies the rub.* This practical result is an economic admission of the need to balance all the economic forces through the process of a plan. In *Wheeling-Pittsburgh*, the pre-petition dispute between the management and the union over pledging the current assets as collateral reflected the union's early understanding that an asset crucial to the debtor's restructuring was being negotiated away without the union's participation. That issue is usually not a labor-management dispute, but it became so as a part of the total plan of reorganization. The company was about to collateralize an important asset and was asking the union concurrently to reduce its contract wages. Those economically related acts needed to be legally coordinated or tied together by a plan of reorganization.

For all creditors, voluntary negotiation is the essence of the Chapter 11 plan process. Debtors in possession may need more than the 120 days provided in the statute in order to prepare a plan.[349] Judges should consider using the exclusivity period to encourage such bargaining at every level. Frequently the bargaining is slow to get started, and is not realistic. Judges have tended to extend the 120 day limit easily. Easy extensions do not encourage the needed bargaining. Once protected by the automatic stay, debtors do not want to leave that safe harbor. The parties sometimes attempt to solve every conceivable debtor/creditor problem before the plan is presented. The professionals, attorneys, accountants, etc. often do not act to hasten the reorganization. A quick and prompt plan does not maximize their fees, but delay does. This is a matter Congress should address. Courts and creditors have been reluctant to force the issue. When judges easily extend the exclusivity period without conditions, and creditors do not oppose the extension or file their own plan of reorganization, the debtor in possession gets comfortable and refuses to leave the safe harbor with a negotiated plan. To encourage the bargaining process, judges should not extend the exclusivity period.

Labor creditors are different than other creditors. When non-labor creditors do not voluntarily accept the plan, the court can take evidence, cram down or deny the plan. When dealing with personal property and capital, the court's determination of these matters can be enforced by legal process. However, when dealing with labor, rejection may be ineffective if employees choose to strike. Only voluntary negotiations produce the desired result.

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349. 11 U.S.C. § 1121(b) (1982). This section provides that "only the debtor may file a plan until after 120 days after the date of the order for relief ...."

The bankruptcy legal process should not enable the parties to receive more than the market place permits them to obtain at the bargaining table. Section 1113 encourages the debtor and labor to bargain. It encourages a complete exchange of the relevant information. If by hard bargaining labor creditors achieve more than the market place can support, labor will have achieved a pyrrhic victory. If the terms do not permit the enterprise to prosper after reorganization, the debtor will fail. If the debtor obtains too many concessions from labor, in two to three years when the contract expires, labor can correct the situation and adjust the balance again.

V. CONCLUSION

Before the *Bildisco* decision, courts used varying standards to allow Chapter 11 debtors to reject collective bargaining agreements. The Second Circuit followed the *REA Express* standard, which permitted rejection as a last resort to save a debtor in imminent danger of collapse. Other courts, such as the Third and Eleventh Circuits, used a relaxed standard, allowing rejection if the collective bargaining agreement burdens the estate and the equities balance in favor of rejection. In *Bildisco* the United States Supreme Court resolved the conflict by adopting the latter standard. The Court also held that unilateral rejection of a collective bargaining agreement is not an unfair labor practice. That aspect of the decision particularly incensed organized labor.

Organized labor mounted an intense effort to legislatively overrule *Bildisco*, while business and creditor interests lobbied to retain *Bildisco*'s beneficial effect. The resultant legislation, section 1113 of the Bankruptcy Code, is an accommodation to both of those interests. On one hand, it recognizes the most serious concerns of organized labor by prohibiting a debtor from unilaterally rejecting a collective bargaining agreement. Instead, debtors must now seek the permission of the bankruptcy court to reject. Before doing so, the debtor must bargain with the union over the proposed changes to the collective bargaining agreement, and must provide the union with sufficient information to evaluate the proposed changes.

On the other hand, section 1113 adopts the equitable, subjective standard for rejection set forth in *Bildisco*. The statute utilizes numerous terms of compromise, which have generated some litigation. In the cases reported to date, courts have generally interpreted section 1113 in a common sense manner. Both the debtor and the union must participate in meaningful negotiations. The proposed

modifications, or the union's rejection of them, must be easily quantifiable with respect to the debtor's reorganization.

The better course of action, however, is to avoid rejection litigation. This is accomplished through bargaining. The courts can use their considerable equitable power to require earnest bargaining. The courts should not allow the judicial process to be used to tilt the power balance. Nor should the courts allow the judicial process to be used as a substitute for bargaining. The union and the debtor must focus on the economic realities of their situation, rather than the strength of their respective legal positions. Rejection of the contract may decide technical matters related to claims on liquidation. It will be a waste of time if it does not result in a new economic bargain.