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Rejection of Collective Bargaining Agreements in Bankruptcy: Finding a Balance in 11 U.S.C. §

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REJECTION OF COLLECTIVE BARGAINING AGREEMENTS IN BANKRUPTCY: FINDING A BALANCE IN 11 U.S.C. § 1113

INTRODUCTION

Traditionally, the common law and all versions of United States corporate reorganization law[1] have enabled bankruptcy trustees[2] to reject executory contracts.[3] In the 1970's, debtors began using this fundamen-

1. The Constitution provides Congress with the power "[t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States." U.S. Const. art. I, § 8, cl. 4. Congress first enacted uniform bankruptcy laws in 1898. *See* Bankruptcy Act of 1898, ch. 541, 30 Stat. 544. The first major enactment of corporate reorganization laws was the Chandler Act. *See* Act of June 22, 1938 (Chandler Act), ch. 575, 52 Stat. 840 (repealed 1978). This Act remained in effect until it was superceded by the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified as amended at 11 U.S.C. §§ 101-1330 (1982 & Supp. IV 1986)) (hereinafter the Bankruptcy Code).

2. For the purposes of this Note, the term "debtor" refers either to a trustee or a debtor-in-possession. Traditionally, when a person filed for bankruptcy or was declared a bankrupt, a trustee either was elected by the debtor's creditors or appointed by the court and was responsible for collection and distribution of the debtor's property. *See* 1 Norton Bankruptcy Law and Practice § 1.03 (W. Norton ed. 1981). Modern business reorganization contains no provision for automatic appointment of a trustee. *See* M. Bienenstock, Bankruptcy Reorganization 288 (1987). Rather, the bankruptcy court can appoint a trustee under § 1104(a) of the Bankruptcy Code, *see* 11 U.S.C. § 1104(a) (1982 & Supp. IV 1986), either "for cause, including fraud, dishonesty, incompetence, or gross mismanagement" of the debtor's affairs by the current management, 11 U.S.C. § 1104(a)(1) (1982), or if "appointment [of a trustee] is in the interests of creditors, any equity security holders, and other interests of the estate." *Id.* at § 1104(a)(2). A strong presumption exists against appointment of a trustee in chapter 11 reorganizations. *See In re* Garland Corp., 6 Bankr. 456, 460 (Bankr. 1st Cir. 1980); *In re* Cole, 66 Bankr. 75, 76 (Bankr. E.D. Pa. 1986); *In re* St. Louis Globe-Democrat, Inc., 63 Bankr. 131, 138 (Bankr. E.D. Mo. 1985).

In cases where a trustee has not been appointed, the debtor remains in possession of the estate and exercises the powers and duties of a trustee with the exception of the trustee's investigatory duties. *See* 11 U.S.C. § 1107(a) (Supp. IV 1986). Such a debtor is referred to as a "debtor in possession." *See* 11 U.S.C. § 1101(1) (1982). The duties of the trustee are set out in § 1106 of the Bankruptcy Code, which provides that the trustee shall be accountable for all property received; examine proofs of claims and object to improper claims; furnish information concerning the estate and its administration if requested by a party in interest; make periodic reports and summaries of the operation of the business; make a final report and file an accounting with the court; file a list of creditors, schedules of assets and liabilities, current income and expenditures, and statements of the debtor's affairs; investigate acts, conduct, assets, liabilities and financial condition of the debtor; file a plan of reorganization or otherwise dispose of the case; provide information for the payment of back taxes; and after confirmation of a plan of reorganization, file such reports as are necessary. *See* 11 U.S.C. §§ 704, 1106 (1982 & Supp. IV 1986). When a debtor-in-possession acts as trustee, § 1104(b) provides that an examiner may be appointed to investigate the debtor. *See* 11 U.S.C. § 1104(b) (Supp. IV 1986).

3. At common law, a bankruptcy trustee had the power to reject an executory contract if, in his opinion, it would be profitable or desirable to do so. *See* United States Trust Co. v. Wabash W. Ry., 150 U.S. 287, 299-300 (1893); *In re* Frazin, 183 F. 28, 29-31 (2d Cir. 1910). *See generally* Silverstein, *Rejection of Executory Contracts in Bankruptcy and Reorganization*, 31 U. Chi. L. Rev. 467, 468-72 (1964). Although the term "executory contract" is not defined in the Bankruptcy Code, *see* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 522 n.6 (1984), the legislative history to 11 U.S.C. § 365 (1982 & Supp. IV

tal bankruptcy power[4] to reject collective bargaining agreements ("CBA's").[5] Certain courts held that this use of the bankruptcy power was acceptable,[6] while others concluded that it implicated the national labor policy of encouraging collective bargaining.[7] In *NLRB v. Bildisco & Bildisco*,[8] the Supreme Court authorized rejection of CBA's under section 365(a) of the Bankruptcy Code,[9] holding that rejection was not an

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1986) indicates that an executory contract is one "on which performance remains due to some extent on both sides." *See Bildisco*, 465 U.S. at 522 n.6 (quoting H.R. Rep. No. 595, 95th Cong., 1st Sess. 347, *reprinted in* 1978 U.S. Code Cong. & Admin. News 5963, 6303); *see also* Countryman, *Executory Contracts in Bankruptcy: Part I*, 57 Minn. L. Rev. 439, 460 (1973) (stating that an executory contract is one "under which the obligation of both the bankrupt and the other party to the contract are so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other"). *See generally* M. Bienenstock, *supra* note 2, at 441-45.

The ability to reject executory contracts was codified first in the 1930's, spurred by the advent of corporate reorganization. *See* Bankruptcy Act of June 7, 1934, ch. 424, § 77(B)(b)(6), 48 Stat. 911, 914 (amending the Bankruptcy Act of 1898, ch. 541, 30 Stat. 544) (repealed 1938). Section 77(B)(b)(6) provided that "[a] plan of reorganization within the meaning of this section . . . may reject contracts of the debtor which are executory in whole or in part, including unexpired leases except contracts in the public authority." *Id.* Less than five years later, the Chandler Act, Pub. L. No. 75-696, 52 Stat. 840 (1938), superceded this section with two separate sections, § 116 for corporate reorganizations, and § 313 for arrangements of unsecured debts. *See* Silverstein, *supra*, at 467 n.4. Section 116 provided that "[u]pon the approval of a petition, the judge may . . . permit the rejection of executory contracts of the debtor . . . upon notice to the parties to such contracts and to such other parties in interest as the judge may designate." Act of June 22, 1938 (Chandler Act), ch. 575, § 116, 52 Stat. 840, 884-85 (codified as amended at 11 U.S.C. § 516 (1976)) (repealed 1978). Section 313 provided that "[u]pon the filing of a petition, the court may . . . permit the rejection of executory contracts of the debtor, upon notice to the parties to such contracts and to such other parties in interest as the court may designate." Act of June 22, 1938 (Chandler Act), ch. 575, § 313(1), 52 Stat. 840, 906 (codified as amended at 11 U.S.C. § 713(1) (1976)) (repealed 1978). This language remained in effect until the enactment of the Bankruptcy Code in 1978. *See* 11 U.S.C. §§ 516, 713 (1976) (repealed 1978). Under the Bankruptcy Code these two sections are combined in § 365(a), providing that "the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor." 11 U.S.C. § 365(a) (Supp. IV 1986). The debtor has a duty to reject executory contracts that do not benefit the estate. *See* Butterworth v. Degnon Contracting Co., 214 F. 772, 773 (2d Cir. 1914); Investors Dev. Co. v. Forum Homes, Inc. (*In re* Investors Dev. Co.), 7 Bankr. 772, 774 (Bankr. D.N.J. 1980); M. Bienenstock, *supra* note 2, at 456-57.

4. *See supra* note 3.

5. *See, e.g.*, NLRB v. Bildisco & Bildisco, 465 U.S. 513, 518 (1984); Local Unions 20 v. Brada Miller Freight Sys., Inc. (*In re* Brada Miller Freight Sys., Inc.), 702 F.2d 890, 892 (11th Cir. 1983); *see also* Brotherhood of Railway, Airline and Steamship Clerks v. REA Express, Inc., 523 F.2d 164, 167 (2d Cir.) (using § 365's predecessor, § 313(1) of the Bankruptcy Act), *cert. denied*, 423 U.S. 1017 (1975); Shopmen's Local Union No. 455 v. Kevin Steel Prods., Inc., 519 F.2d 698, 700 (2d Cir. 1975) (same).

6. *See, e.g.*, Local Unions 20 v. Brada Miller Freight Sys., Inc. (*In re* Brada Miller Freight Sys., Inc.), 702 F.2d 890, 894 (11th Cir. 1983); NLRB v. Bildisco & Bildisco (*In re* Bildisco), 682 F.2d 72, 84 (3d Cir. 1982), *aff'd*, 465 U.S. 513 (1984).

7. *See, e.g.*, Brotherhood of Railway, Airline and Steamship Clerks v. REA Express, Inc., 523 F.2d 164, 169 (2d Cir.) (decided under § 313(1) of the Bankruptcy Act), *cert. denied*, 423 U.S. 1017 (1975); *In re* Alan Wood Steel Co., 449 F. Supp. 165, 169 (E.D. Pa. 1978) (same), *appeal dismissed*, 595 F.2d 1211 (3d Cir. 1979).

8. 465 U.S. 513 (1984).

9. *See id.* at 522-23.

unfair labor practice.[10]

In response to *Bildisco*, Congress passed section 1113 of the Bankruptcy Code,[11] providing that CBA's can be rejected only if the debtor follows certain procedural steps and meets certain substantive requirements.[12] The procedural steps contained in section 1113(b) require that the debtor propose to the employees' representative modifications in the CBA "necessary to permit reorganization of the debtor"[13] before the bankruptcy court can rule on the debtor's motion to reject. The debtor also must meet with the employees' representative[14] and, in good faith, attempt to reach an agreement.[15] If no compromise is achieved, the substantive requirements of section 1113(c) mandate that the bankruptcy court approve rejection only if the procedural steps of section 1113(b) have been complied with,[16] the representative of the employees has refused to accept the proposal without good cause,[17] and the balance of the

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10. *See id.* at 532-33.

11. 11 U.S.C. § 1113 (Supp. IV 1986).

12. The provision was enacted as part of the Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 390 (codified in scattered sections of 11 U.S.C.). Section 1113 provides in pertinent part:

> (a) The debtor in possession, or the trustee if one has been appointed under the provisions of this chapter . . . may assume or reject a [CBA] only in accordance with the provisions of this section.
>
> (b)(1) Subsequent to filing a petition [for reorganization] and prior to filing an application seeking rejection of a [CBA], the debtor in possession or trustee (hereinafter in this section 'trustee' shall include a debtor in possession), shall—
>
> (A) make a proposal to the authorized representative of the employees covered by such agreement, based on the most complete and reliable information available at the time of such proposal, which provides for those necessary modifications in the employees [sic] benefits and protections that are necessary to permit the reorganization of the debtor and assures that all creditors, the debtor and all of the affected parties are treated fairly and equitably; and
>
> (B) provide . . . the representative of the employees with such relevent information as is necessary to evaluate the proposal.
>
> (2) During the period beginning on the date of the making of a proposal provided for in paragraph (1) and ending on the date of the hearing . . . the trustee shall meet, at reasonable times, with the authorized representative to confer in good faith in attempting to reach mutually satisfactory modifications of such agreement.
>
> (c) The court shall approve an application for rejection of a [CBA] only if the court finds that—
>
> (1) the trustee has, prior to the hearing, made a proposal that fulfills the requirements of subsection (b)(1);
>
> (2) the authorized representative of the employees has refused to accept such proposal without good cause; and
>
> (3) the balance of the equities clearly favors rejection of such agreement.

11 U.S.C. § 1113 (Supp. IV 1986).

13. *See* 11 U.S.C. § 1113(b)(1)(A); *supra* note 12.

14. *See* 11 U.S.C. § 1113(b)(2); *supra* note 12.

15. *See* 11 U.S.C. § 1113(b)(2); *supra* note 12.

16. *See* 11 U.S.C. § 1113(c)(1); *supra* note 12.

17. *See* 11 U.S.C. § 1113(c)(2); *supra* note 12.

equities clearly favors rejection of the contract.[18]

Recently, a conflict has arisen among the United States Courts of Appeals as to how necessary and to what end proposed modifications must be in order to meet the threshold necessity requirement.[19] For example, in *Wheeling-Pittsburgh Steel Corp. v. United Steelworkers*,[20] the Third Circuit held that a debtor will not be allowed to reject a CBA unless the debtor's modifications are essential to prevent immediate liquidation of the business.[21] In contrast, the Second Circuit, in *Truck Drivers Local 807 v. Carey Transportation Inc.*,[22] held that a debtor's modifications need only be necessary for its successful long-term reorganization.[23] Although this specific conflict is new, the clash between the forces that produced it is not. On one side of the issue is the nation's interest in rehabilitating failed businesses, on the other is the nation's policy of ensuring fair employment.

This Note examines the requirements of section 1113 and how it can be used to resolve these competing interests. Part I looks at the procedural and substantive requirements of section 1113, examining the *Bildisco* case and section 1113's legislative history. Part II examines the case law interpreting section 1113's necessity requirement and concludes that allowing the debtor to make proposals that are necessary to the successful long-term reorganization of the enterprise best effectuates the fundamental purpose of the procedural aspect of section 1113. Last, the Note concludes that if the necessity requirement is properly construed, the balancing-of-the-equities requirement must then be reexamined to reflect proper concern for the hardship of employees faced with losing their contractual rights.

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18. *See* 11 U.S.C. § 1113(c)(3); *supra* note 12.

19. *See* 11 U.S.C. § 1113(b)(1)(A); *supra* note 12; *supra* note 13 and accompanying text.

20. 791 F.2d 1074 (3d Cir. 1986).

21. Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1088-89 (3d Cir. 1986).

22. 816 F.2d 82 (2d Cir. 1987).

23. *See id.* at 90. Despite the fact that Webster's dictionary indicates that the words "necessary" and "essential" have the same meaning, *compare* Webster's New Universal Unabridged Dictionary 1200 (2d ed. 1983) (stating that necessary means that which "cannot be dispensed with; essential") *with id.* at 624 (stating essential means "necessary to make a thing what it is"), the word "necessary," as a legal term at least, has a more flexible meaning. *See* McCulloch v. Maryland, 17 U.S. (4 Wheat.) 316, 414 (1819) ("necessary" "has not a fixed character, peculiar to itself[, but] admits of all degrees of comparison; and is often connected with other words, which increase or diminish the impression the mind receives of the urgency it imports"); Black's Law Dictionary 928 (5th ed. 1979) (necessary "must be considered in the connection in which it is used, as it is a word susceptible of various meanings [and] may import absolute physical necessity . . . or it may import that which is only convenient"). Essential, on the other hand, means "[i]ndispensibly necessary." *See id.* at 490.

I. REJECTION OF COLLECTIVE BARGAINING AGREEMENTS UNDER 11 U.S.C. SECTION 1113

Chapter 11 of the Bankruptcy Code[24] provides a debtor corporation with the opportunity to reorganize[25] while keeping its creditors at bay.[26] The rationale underlying reorganization is that a successful reorganization is preferable to liquidation:[27] a reorganized debtor will be in a better position to repay its creditors, provide a dividend for its shareholders, and supply uninterrupted employment for its workers.[28] Thus, Chapter

24. 11 U.S.C. §§ 1101-1174 (1982 & Supp. IV 1986). Chapter 11 was enacted as part of the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (1978) (superceding the Bankruptcy Act of 1898).

25. *See* 11 U.S.C. § 301 (1982). In a typical Chapter 11 scenario, a debtor, *see* 11 U.S.C. § 109 (1982 & Supp. IV 1986) (determining what entities can qualify for Chapter 11 relief), files a petition for reorganization, *see* 11 U.S.C. § 301 (1982), whereupon an estate is created, *see* 11 U.S.C. § 541(a) (1982 & Supp. IV 1986), comprised of all the debtor's property, wherever located and by whomever held, *see id.*, unless exempted by § 541(b) of the Bankruptcy Code, *see* 11 U.S.C. § 541(b) (Supp. IV 1986). At the time of filing, all actions to recover claims against the debtor automatically are stayed, *see* 11 U.S.C. § 362 (1982 & Supp. IV 1986). The debtor usually remains in possession of the estate, *see* 11 U.S.C. § 1101 (1982); 11 U.S.C. § 1107 (1982 & Supp. IV 1986), unless a trustee is appointed, *see id.* at § 1104(a); *supra* note 2. The debtor continues the business, *see* 11 U.S.C. § 1108 (Supp. IV 1986), and sifts through his assets and liabilities, *see* 11 U.S.C. §§ 541, 1106, 1107 (1982 & Supp. IV 1986). It is during this period that a debtor can elect to accept or reject executory contracts, *see id.* at § 365, and to reject a CBA, *see* 11 U.S.C. § 1113 (Supp. IV 1986). After a reasonable period for the debtor to get his affairs in order, *see* 11 U.S.C. § 1121 (1982 & Supp. IV 1986), the debtor files a plan of reorganization, *see id.*, designating the claims against the estate and the proposed treatment of such claims, *see id.* at § 1123. Claims are divided by type, *see id.* at § 507, and whether they accrued before the filing of the petition ("prepetition"), *see* 11 U.S.C. § 365(g) (Supp. IV 1986), or after ("postpetition"), *see* 11 U.S.C. § 503 (1982 & Supp. IV 1986). Claims accruing after filing receive priority over prepetition claims. *See id.* at § 507. The debtor's creditors vote on the plan, *see id.* at § 1126, and a hearing is held on its confirmation, *see* 11 U.S.C. § 1128 (1982). The bankruptcy court can confirm the plan only if it meets the statutory requirements of § 1129. *See* 11 U.S.C. § 1129 (1982 & Supp. IV 1986). The debtor's handling of executory contracts and CBA's does not require confirmation as part of the overall plan of reorganization, *see id.*, but does require court approval pursuant to either § 365 or § 1113, *see id.* at § 365; 11 U.S.C. § 1113 (Supp. IV 1986).

In contrast, Chapter 7 of the Bankruptcy Code, 11 U.S.C. §§ 701-766 (1982 & Supp. IV 1986), provides for the collection, liquidation and distribution of a debtor's property. *See* 3 Collier Bankruptcy Manual ¶ 700.01 (L. King ed. 1987). Chapter 7 can be used as an alternative to filing under Chapter 11, *see* 3 Norton Bankruptcy Law and Practice § 50.02 (W. Norton ed. 1981), or may be utilized by a Chapter 11 debtor whose attempt to rehabilitate fails. *See* 11 U.S.C. §§ 1112, 1129 (1982 & Supp. IV 1986). A plan of reorganization may also include liquidation. *See* 11 U.S.C. § 1129(a)(11) (1982).

26. *See* 11 U.S.C. § 362 (1982 & Supp. IV 1986).

27. In one study of Chapter 7 liquidations, secured creditors recovered less than 33% of their claims, and unsecured creditors received an average of 8%, whereas in successful Chapter 11 reorganizations, secured creditors almost always received their claims in full, while unsecured creditors recovered an average of 19% of their claims under lump sum payment plans and 10% of their claims under deferred payment plans. *See* D. Stanley & M. Girth, Bankruptcy 129-30, 142-43 (1971). Although a plan of reorganization can provide for liquidation of the debtor, *see* 11 U.S.C. § 1129(a)(11) (1982), successful reorganization as used in this Note means rehabilitation of the debtor.

28. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 528 (1984); United States v.

11 is intended to achieve not mere short-term relief, but successful, long-term restructuring of the debtor's affairs.[29] Accordingly, in order to confirm a plan of reorganization the debtor must prove that confirmation is "not likely to be followed by the [debtor's] liquidation, or the need for further financial reorganization . . . unless such liquidation or reorganization is proposed in the plan."[30]

The debtor's ability to reject executory contracts under section 365(a) of the Bankruptcy Code forms an essential part of the mechanism of Chapter 11.[31] Section 365(a) of the Bankruptcy Code provides that "the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor."[32] The scope of section 365 is broad. The trustee may reject an executory contract if he perceives any business advantage in doing so.[33] Accordingly, the bankruptcy court's standard of review is one of business judgment: "the rule . . . requires that the decision be accepted by courts unless it is shown that the bankrupt's decision was one taken in bad faith or in gross abuse of the bankrupt's retained business discretion."[34] Rejection causes the contract to be deemed breached immediately prior to the debtor's filing of its petition for Chapter 11 protection, and the promisee has a prepetition claim against the estate.[35]

Whiting Pools, Inc., 462 U.S. 198, 203 (1983); H.R. Rep. No. 595, 95th Cong., 1st Sess. 220, *reprinted in* 1978 U.S. Code Cong. & Admin. News 5963, 6179.

29. For example, under § 1112 of the Bankruptcy Code, 11 U.S.C. § 1112 (1982 & Supp. IV 1986), the Chapter 11 proceeding may be converted to a liquidation proceeding under Chapter 7 of the Bankruptcy Code, 11 U.S.C. §§ 701-766 (1982 & Supp. IV 1986) (providing for collection, liquidation and distribution of a debtor's property), *see supra* note 25, or may be dismissed for cause, on the application of either the debtor, *see* 11 U.S.C. § 1112(a) (Supp. IV 1986), or a party in interest, *see id.* at § 1112(b). One such cause for dismissal or conversion exists when the bankruptcy court finds that the debtor's financial condition is such that there is "no reasonable likelihood that the debtor will be rehabilitated." 3 Collier Bankruptcy Manual, *supra* note 25, ¶ 1112.04[2](d)(i), at 1112-19-20; *see In re* Kors, Inc., 13 Bankr. 676, 681 (Bankr. D. Vt. 1981).

30. 11 U.S.C. § 1129(a)(11) (1982). *See* Teamsters Nat'l Freight Indus. Negotiating Comm. v. U.S. Truck Co. (*In re* U.S. Truck Co.), 800 F.2d 581, 589 (6th Cir. 1986); Travelers Ins. Co. v. Pikes Peak Water Co. (*In re* Pikes Peak Water Co.), 779 F.2d 1456, 1460 (10th Cir. 1985).

31. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 528 (1984); Gibson, *The New Law on Rejection of Collective Bargaining Agreements in Chapter 11: An Analysis of 11 U.S.C. 1113, 58 Am. Bankr. L.J. 325, 325-26 (1984); supra* note 3. If the debtor rejects an executory contract, the Bankruptcy Code treats the contract as if it had been breached immediately before the date the debtor sought Chapter 11 protection, *see* 11 U.S.C. § 365 (g)(1) (1982 & Supp. IV 1986), and, thus, the breach gives rise to a prepetition claim for damages against the estate, *see id.* at § 502(g).

32. 11 U.S.C. § 365(a) (Supp. IV 1986).

33. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 523 (1984); Group of Inst. Investors v. Chicago, M., St. P. & P.R.R., 318 U.S. 523, 549-50 (1943); Lubrizol Enter., Inc. v. Richmond Metal Finishers, Inc. (*In re* Richmond Metal Finishers, Inc.), 756 F.2d 1043, 1047 (4th Cir. 1985), *cert. denied*, 475 U.S. 1057 (1986); Control Data Corp. v. Zelman (*In re* Minges), 602 F.2d 38, 42-43 (2d Cir. 1979); *supra* note 3.

34. Lubrizol Enter., Inc. v. Richmond Metal Finishers, Inc. (*In re* Richmond Metal Finishers, Inc.), 756 F.2d 1043, 1047 (4th Cir. 1985), *cert. denied*, 475 U.S. 1057 (1986).

35. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 530 (1984); *supra* note 31.

In the 1970's, debtors began using section 313 of the Bankruptcy Act,[36] and then its successor, section 365(a), to reject CBA's.[37] This tactic brought the rehabilitative policy of the Bankruptcy Code[38] into conflict with the national labor policy of encouraging collective bargaining to ensure industrial peace.[39] In addressing this conflict, appellate courts agreed that CBA's were executory contracts within section 365(a),[40] but disagreed whether rejection should proceed under the business judgment test or under some stricter test.[41] Moreover, the courts disagreed whether a debtor's rejection of a CBA constituted a unilateral modification, made without collective bargaining, banned by the National Labor Relations Act[42] as an unfair labor practice.[43] In *NLRB v. Bildisco &*

36. *See* Act of June 22, 1938 (Chandler Act), ch. 575, § 313(1), 52 Stat. 840, 906 (codified as amended at 11 U.S.C. § 313(1)(1976)) (repealed 1978); *supra* note 1.

37. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 518 (1984); Local Unions 20 v. Brada Miller Freight Sys., Inc. (*In re* Brada Miller Freight Sys., Inc.), 702 F.2d 890, 892 (11th Cir. 1983); Brotherhood of Railway, Airline and Steamship Clerks v. REA Express, Inc., 523 F.2d 164, 167 (2d Cir.), *cert. denied*, 423 U.S. 1017 (1975); Shopmen's Local Union No. 455 v. Kevin Steel Prods., Inc., 519 F.2d 698, 700 (2d Cir. 1975).

38. *See* United States v. Whiting Pools, Inc., 462 U.S. 198, 203 (1983); *supra* notes 25-30 and accompanying text.

39. *See* National Labor Relations Act, § 1, 29 U.S.C. § 151 (1982). The Supreme Court has recognized that "[e]nforcement of the obligation to bargain collectively is crucial to the statutory scheme" of the National Labor Relations Act. NLRB v. American Nat'l Ins. Co., 343 U.S. 395, 402 (1952); *see* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 541 (1984) (Brennan, J., dissenting); First Nat'l Maintenance Corp. v. NLRB, 452 U.S. 666, 674 (1981). *See generally* Bordewieck & Countryman, *The Rejection of Collective Bargaining Agreements by Chapter 11 Debtors*, 57 Am. Bankr. L.J. 293, 297-300 (1983) (discussing the policies of the National Labor Relations Act).

40. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 521-22 (1984); *see, e.g.*, Local Unions 20 v. Brada Miller Freight Sys., Inc. (*In re* Brada Miller Freight Sys., Inc.), 702 F.2d 890, 896-97 (11th Cir. 1983); *cf.* Shopmen's Local Union No. 455 v. Kevin Steel Prods., Inc., 519 F.2d 698, 703-04 (2d Cir. 1975) (decided under § 313(1) of the Bankruptcy Act).

41. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 523-24 (1984). *Compare* Lubrizol Enter., Inc. v. Richmond Metal Finishers, Inc. (*In re* Richmond Metal Finishers, Inc.), 756 F.2d 1043, 1047 (4th Cir. 1985) (holding that executory contracts may be rejected if, absent bad faith or gross abuse of discretion, debtor sees some business advantage in doing so), *cert. denied*, 475 U.S. 1057 (1986) *with* Brotherhood of Railway, Airline and Steamship Clerks v. REA Express, Inc., 523 F.2d 164, 172 (2d Cir.) (stating that "in view of the serious effects which rejection [of the CBA] has on the carrier's employees it should be authorized only where it clearly appears to be the lesser of two evils and that, unless the agreement is rejected, the carrier will collapse and the employees will no longer have their jobs"), *cert. denied*, 423 U.S. 1017 (1975) *and* Local Unions 20 v. Brada Miller Freight Sys., Inc. (*In re* Brada Miller Freight Sys., Inc.), 702 F.2d 890, 899 (11th Cir. 1983) (rejecting the holding in *REA Express* as excessively burdensome to the debtor and opting for a balancing-of-equities standard, stating that this approach better accommodates the conflicting policies) *and In re* Alan Wood Steel Co., 449 F. Supp. 165, 169 (E.D. Pa. 1978) (holding that a CBA could be rejected only if the equities balance in favor of rejection and failure to reject would make successful reorganization impossible), *appeal dismissed*, 595 F.2d 1211 (3d Cir. 1979).

42. *See* National Labor Relations Act, ch. 372, § 8(5), 49 Stat. 449, 452-53 (1935) (codified as amended 29 U.S.C. § 158(a)(5), (d) (1982)).

43. *See* Allied Chemical & Alkali Workers v. Pittsburgh Plate Glass Co., 404 U.S. 157, 185-86 (1971) (holding unilateral modifications of CBA's impermissible).

Bildisco,[44] the Supreme Court addressed these issues, holding that CBA's could be rejected under section 365(a) if the balance of equities favored rejection,[45] and that such rejection was not an unfair labor practice.[46]

A. NLRB v. Bildisco & Bildisco

NLRB v. Bildisco & Bildisco[47] both illustrates the conflict between the rehabilitative policy of Chapter 11 and the national labor policy favoring collective bargaining of the National Labor Relations Act and attempts to resolve it. Bildisco, a party to a CBA, filed a voluntary petition for Chapter 11 reorganization.[48] The bankruptcy court then permitted Bildisco to reject its CBA.[49] Meanwhile, the union had brought an administrative proceeding before the National Labor Relations Board ("NLRB") against Bildisco alleging violation of the agreement.[50] The NLRB ordered Bildisco to comply with the terms of the CBA,[51] notwithstanding notification that the bankruptcy court had permitted Bildisco to reject it two months earlier.[52] The union appealed the bankruptcy court's ruling to the district court[53] and then to the Third Circuit,[54] while the NLRB applied to the Third Circuit for enforcement of its order.[55] The Court of Appeals consolidated the two cases, vacating the bankruptcy court's judgment allowing rejection of the CBA and remanding the case for a determination whether the balance of equities favored rejection.[56] The NLRB and the union appealed to the Supreme Court, which granted certiorari[57] to resolve the conflict among the courts of appeals as to the proper standard for rejecting CBA's.[58]

The Supreme Court first addressed the argument that the unique status of CBA's so distinguished them from ordinary contracts[59] that they were not covered by section 365, but only by the National Labor Rela-

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44. 465 U.S. 513 (1984).
45. *See id.* at 525-26.
46. *See id.* at 534.
47. 465 U.S. 513 (1984).
48. *See* NLRB v. Bildisco & Bildisco (*In re* Bildisco), 682 F.2d 72, 75 (3d Cir. 1982), *aff'd*, 465 U.S. 513 (1984).
49. *See id.*
50. *See* Bildisco & Bildisco, 255 N.L.R.B. 1203, 1203 (1981). The National Labor Relations Board is "empowered . . . to prevent any person from engaging in any unfair labor practice . . . affecting commerce." 29 U.S.C. § 160(a) (1982).
51. *See Bildisco*, 255 N.L.R.B. at 1205.
52. *See* NLRB v. Bildisco & Bildisco (*In re* Bildisco), 682 F.2d 72, 76 (3d Cir. 1982), *aff'd*, 465 U.S. 513 (1984).
53. *See id.* at 75.
54. *See* NLRB v. Bildisco & Bildisco (*In re* Bildisco), 682 F.2d 72, 76 (3d Cir. 1982), *aff'd*, 465 U.S. 513 (1984).
55. *See* NLRB v. Bildisco & Bildisco (*In re* Bildisco), 682 F.2d 72, 76 (3d Cir. 1982), *aff'd*, 465 U.S. 513 (1984).
56. *See id.* at 84-85.
57. *See* NLRB v. Bildisco & Bildisco, 459 U.S. 1145 (1983).
58. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 521 (1984); *supra note* 41 and accompanying text.
59. *See* United Steelworkers v. Warrior & Gulf Navigation Co., 363 U.S. 574, 578-80

tions Act.[60] The Court determined that because Congress expressly exempted CBA's subject to the Railway Labor Act from section 365(a)[61] treatment, but did not provide the same protection to CBA's covered by the National Labor Relations Act, Congress intended that such CBA's be covered by section 365(a).[62] Accordingly, it held that these types of contracts could be rejected.[63]

Next, the Court addressed the argument that even if CBA's were executory contracts within the meaning of section 365, a stricter standard than the business judgment test for rejection of CBA's was necessary to protect the national labor policy.[64] The NLRB and the union had argued that CBA's could be rejected only if it was essential to prevent liquidation of the debtor.[65] Although the majority concluded that the business judgment test did not sufficiently protect the national labor policy,[66] it rejected the strict standard,[67] opting instead for a balancing of interests approach.[68] Accordingly, it stated that rejection requires a finding that such action would serve the bankruptcy policy of encouraging successful reorganization.[69] To determine this, the bankruptcy court must balance the interests of the affected parties: the debtor, its creditors, and the employees.[70]

Last, the Court held that once a debtor files a petition for reorganization, enforcement of any CBA shifts from the NLRB to the bankruptcy courts.[71] Accordingly, the NLRB's attempt to enforce the agreement had "run directly counter to the express provisions of the Bankruptcy Code."[72] Thus, the Court held that the unilateral rejection of the CBA

(1960) (stating that a CBA is more than a contract: it represents "an effort to erect a system of industrial self-government").

60. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 522-23 (1984); *see also* Shopmen's Local Union No. 455 v. Kevin Steel Prods., Inc., 519 F.2d 698, 706 (2d Cir. 1975) (holding that CBA's could be rejected under § 313(1) of the Bankruptcy Act, *see supra* note 3).

61. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 522-23 (1984) (interpreting 11 U.S.C. § 1167 (1982)).

62. *See id.* at 523.

63. *See id.*

64. *See id.*

65. *See id.* at 524. The NLRB relied on the Second Circuit's holding in *Brotherhood of Railway, Airline and Steamship Clerks v. REA Express, Inc.*, 523 F.2d 164, 172 (2d Cir.) (holding that CBA's can be rejected only when it appears that, absent rejection, the debtor will liquidate), *cert. denied*, 423 U.S. 1017 (1975). *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 524 (1984).

66. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 524 (1984).

67. *See id.* at 525.

68. *See id.* at 527; *see also* Local Unions 20 v. Brada Miller Freight Sys., Inc. (*In re* Brada Miller Freight Sys., Inc.), 702 F.2d 890, 899 (11th Cir. 1983) (rejecting strict standard as excessively burdensome to debtor and opting for a balancing-of-equities standard, stating that it better accommodates conflicting policies).

69. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527 (1984).

70. *See id.*

71. *See id.* at 530-31.

72. *Id.* at 532. The dissent, however, noted that the majority

> points to no provision of [the Bankruptcy] Code that purports to render [the

did not violate the National Labor Relations Act.[73]

Four justices dissented from the Court's decision in *Bildisco*.[74] They argued that the majority undermined the policy behind the National Labor Relations Act by holding that unilateral rejection was not an unfair labor practice, stating the majority was "spawn[ing] precisely the type of industrial strife that [NLRA] § 8(d) was designed to avoid."[75] Some members of Congress, who were already struggling with extensive revisions in the bankruptcy laws, shared this concern.[76]

B. *The Passage of Section 1113*

The specter of debtors unilaterally rejecting CBA's by application of the bankruptcy laws spurred several pro-labor members of Congress to propose section 1113 of the Bankruptcy Code[77] to protect CBA's from what they perceived as a "new collective-bargaining weapon."[78] They feared that the *Bildisco* holding would allow the unilateral rejection, rather than renegotiation, of CBA's by debtors.[79] This ability would discourage collective bargaining and thus would run counter to the policy expressed in the National Labor Relations Act.[80]

The original House of Representatives version of section 1113[81] would have enabled a debtor to reject a CBA only upon court approval.[82] This

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> employer's duty to bargain collectively under § 8(d) of the NLRA] inapplicable. . . . Accordingly, in order to achieve its desired result, the Court is forced to infer from the Bankruptcy Code's general treatment of the executory contracts and from the policies that underlie that treatment, that Congress must have intended the filing of a bankruptcy petition to render § 8(d) inapplicable.

Id. at 539 (Brennan, J., dissenting).

73. *See id.* at 534.

74. *See id.* at 535 (Brennan, J., dissenting).

75. *Id.* at 554.

76. *See Effect of Bankruptcy Actions on the Stability of Labor-Management Relations and the Preservation of Labor Standards: Joint Hearing Before the Subcomm. on Labor-Management Relations and Subcomm. on Labor Standards of the Comm. on Education and Labor*, 98th Cong., 1st Sess. 2 (1983) [hereinafter *Hearings*] (statement of Rep. William Clay, Chairman, Subcomm. on Labor-Management Relations). Congress was revising the bankruptcy court system because the Supreme Court in *Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) had held part of the Bankruptcy Reform Act of 1978 unconstitutional. *See id.* at 87-88.

77. *See* Century Brass Prods., Inc. v. UAW (*In re* Century Brass Prods., Inc.), 795 F.2d 265, 266-67 (2d Cir.), *cert. denied*, 479 U.S. 949 (1986); Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1082-83 (3d Cir. 1986).

78. *Hearings*, *supra* note 76, at 1 (statement of Rep. Clay).

79. *See* 130 Cong. Rec. S6184 (daily ed. May 22, 1984) (statement of Sen. Packwood).

80. *See supra* note 39 and accompanying text.

81. *See* H.R. 5174, 98th Cong., 2d Sess. sec. 277, 130 Cong. Rec. H1842 (daily ed. Mar. 21, 1984). This draft was passed by the House of Representatives as § 277 of H.R. 5174, a preliminary version of the Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 333 (codified in scattered sections of 11 U.S.C.).

82. *See* H.R. 5174, 98th Cong., 2d Sess. sec. 277, 130 Cong. Rec. H1842 (daily ed. Mar. 21, 1984); Rosenberg, *Bankruptcy and the Collective Bargaining Agreement—A Brief Lesson in the Use of the Constitutional System of Checks and Balances*, 58 Am. Bankr. L.J. 293, 314-15 (1984).

version would have required the debtor, prior to making a motion to reject, to propose to the union modifications of the CBA that were necessary for successful reorganization and the preservation of jobs.[83] The bankruptcy court would not have been able to approve the debtor's motion unless the movant first had conferred with the union in good faith[84] and had provided the union with relevant financial and other information.[85] The court also would have had to determine that, absent rejection, the jobs of the workers would be lost and any reorganization would fail.[86] Accordingly, this original House bill would have incorporated a procedural framework that prevented unilateral rejection of CBA's while allowing rejection only if necessary to prevent liquidation of the debtor and to preserve jobs.[87]

When the bill reached the Senate, Senator Strom Thurmond and other members of the Judiciary Committee found the labor provision "completely unacceptable."[88] Senator Thurmond instead supported a substitute drafted by the National Bankruptcy Conference, essentially preserving the Supreme Court's *Bildisco* standard of balancing the parties' interests.[89] The Thurmond substitute limited the *Bildisco* holding, however, by preventing the debtor from unilaterally rejecting the collective agreement until thirty days after making a motion to reject.[90] The substitute also gave the debtor additional flexibility by providing emergency relief from the CBA if it proved essential to the continuation of the debtor's business.[91]

In an effort to find a middle ground between the House provision and the Thurmond substitute, Senator Robert Packwood proposed an amendment to the House bill that substantially altered the standards of the House section.[92] The Packwood amendment provided that in order for the debtor to reject a CBA, he first would have to propose to the

83. *See* H.R. 5174, 98th Cong., 2d Sess. sec. 277, 130 Cong. Rec. H1842 (daily ed. Mar. 21, 1984); Rosenberg, *supra* note 82, at 315.

84. *See* H.R. 5174, 98th Cong., 2d Sess. sec. 277, 130 Cong. Rec. H1842 (daily ed. Mar. 21, 1984); Rosenberg, *supra* note 82, at 315.

85. *See* H.R. 5174, 98th Cong., 2d Sess. sec. 277, 130 Cong. Rec. H1842 (daily ed. Mar. 21, 1984); Rosenberg, *supra* note 82, at 315.

86. *See* H.R. 5174, 98th Cong., 2d Sess. sec. 277, 130 Cong. Rec. H1842 (daily ed. Mar. 21, 1984); Rosenberg, *supra* note 82, at 315.

87. *See* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1083 (3d Cir. 1986); 130 Cong. Rec. S6184 (daily ed. May 22, 1984) (statement of Sen. Packwood); H.R. 5174, 98th Cong., 2d Sess. sec. 277, 130 Cong. Rec. H1842 (daily ed. Mar. 21, 1984); Rosenberg, *supra* note 82, at 314-15.

88. 130 Cong. Rec. S6082 (daily ed. May 21, 1984) (statement of Sen. Thurmond); *see id.* at S6091 (statement of Sen. Hatch); Rosenberg, *supra* note 82, at 317.

89. *See* 130 Cong. Rec. S6126 (daily ed. May 21, 1984); *id.* at S6082-84 (statement of Sen. Thurmond); *supra* notes 68-72 and accompanying text (discussing the balancing-of-the-equities test of *Bildisco*).

90. *See* 130 Cong. Rec. S6126 (daily ed. May 21, 1984); *id.* at S6084 (statement of Sen. Thurmond); Rosenberg, *supra* note 82, at 317.

91. *See* 130 Cong. Rec. S6126 (daily ed. May 21, 1984); *id.* at S6084 (statement of Sen. Thurmond).

92. *See* 130 Cong. Rec. S6181-82, 6184 (daily ed. May 22, 1984).

employees' representative "minimum modifications in . . . employees [sic] benefits and protections that would permit the reorganization."[93] After making the proposal, the debtor would have to meet with the representative at reasonable times and, in good faith, attempt to reach mutually satisfactory modifications of the CBA.[94] Under the Packwood amendment, the bankruptcy court could approve rejection only if the debtor satisfied the above requirements and the employees' representative unjustifiedly refused to accept the proposal.[95] In addition to these somewhat procedural requirements, the Packwood amendment required bankruptcy courts to make a substantive determination that the balance of the equities clearly favored rejection.[96]

The purpose of the Packwood amendment was to place primary responsibility for the modification of a CBA on the parties to the agreement and thus discourage judicial interference.[97] The Packwood amendment, like the provision in the House bill, did not allow unilateral rejection of the contract by the debtor under any circumstances.[98]

The effect of the Packwood amendment's changes to the House bill was to eliminate the requirement that the proposed alterations to the CBA be necessary for the preservation of jobs. Instead, the proposal for modification merely must consider the employees' sacrifices as a factor.[99] Similarly, if the debtor met the amendment's procedural requirements, the bankruptcy court, prior to certifying the rejection, would not need to determine that absent rejection the jobs of the workers would be lost and reorganization would fail.[100]

After debate, Senators Thurmond and Packwood agreed to have a conference committee reach a compromise between their conflicting proposals.[101] Congress passed the compromise section 1113 on June 29,

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93. *Id.* at S6181.

94. *See id.* at S6182.

95. *See id.*

96. *See id.*

97. *See id.* at S6184 (statement of Sen. Packwood).

98. *See id.* at S6182; H.R. 5174, 98th Cong., 2d Sess. sec. 277(h), 130 Cong. Rec. H1842 (daily ed. Mar. 21, 1984).

99. *Compare* 130 Cong. Rec. S6181-82 (daily ed. May 22, 1984) (stating that the trustee shall make a proposal "taking into account the best estimate of the sacrifices expected to be made by all classes of creditors and other affected parties to the reorganization") *with* H.R. 5174, 98th Cong., 2d Sess. sec. 277, 130 Cong. Rec. H1842 (daily ed. Mar. 21, 1984) (trustee may file a motion to reject if trustee has proposed modifications necessary for successful reorganization and "preservation of jobs").

100. *Compare* 130 Cong. Rec. S6182 (daily ed. May 22, 1984) (stating that court, in order to reject a CBA, must determine that procedural requirements have been met, that union unjustifiably has refused to accept debtor's proposal and that balance of equities clearly favors rejection) *with* H.R. 5174, 98th Cong., 2d Sess. sec. 277, 130 Cong. Rec. H1842 (daily ed. Mar. 21, 1984) (stating that court may not approve rejection unless procedural requirements have been met and, absent rejection, jobs covered by agreement would be lost and reorganization would fail).

101. *See* 130 Cong. Rec. S7622-23 (daily ed. June 19, 1984) (statement of Sen. Packwood); Rosenberg, *supra* note 82, at 318.

1984[102] and the President signed it into law on July 10.[103]

Section 1113, as finally passed has two aspects: the first involves a series of procedural requirements designed to promote collective bargaining,[104] while the second sets out the substantive standards for rejection to be considered by the bankruptcy court once the procedural hurdles have been cleared.[105] The procedural aspect of section 1113(b) closely resemble those in the Packwood amendment.[106] The language governing the focus of the debtor's proposal, however, was changed from "minimum modifications in . . . employees [sic] benefits and protections that would permit the reorganization, taking into account the best estimate of the sacrifices expected to be made by all classes of creditors and other affected parties"[107] to "necessary modifications in the employees [sic] benefits and protections that are necessary to permit the reorganization of the debtor and assure[] that all creditors, the debtor and all of the affected parties are treated fairly and equitably."[108] The substantive standard of balancing the equities, contained in section 1113(c), is the same as that of the Packwood amendment,[109] which slightly modified the balancing of interests standard enunciated in *Bildisco*.[110] Section 1113, however, incorporates the Thurmond substitute provision allowing debtors to seek emergency relief from their CBA's if such relief is essential to the continuation of the debtor's business.[111]

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102. 130 Cong. Rec. S8900 (daily ed. June 29, 1984).

103. *See* 11 U.S.C. § 1113 (Supp. IV 1986). The section was incorporated in the Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 390 (codified as amended in scattered sections of 11 U.S.C.).

104. *See* Century Brass Prods., Inc. v. UAW (*In re* Century Brass Prods., Inc.), 795 F.2d 265, 273 (2d Cir.), *cert. denied*, 479 U.S. 949 (1986); 130 Cong. Rec. S8898 (daily ed. June 29, 1984) (statement of Sen. Packwood).

105. *See Century Brass Prods., Inc.*, 795 F.2d at 273; Gibson, *supra* note 31, at 335.

106. *See* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1087 (3d Cir. 1986); 130 Cong. Rec. S8888 (daily ed. June 29, 1984) (statement of Sen. Thurmond); *id.* at S8898 (statement of Sen. Packwood).

107. 130 Cong. Rec. S6181 (daily ed. May 22, 1984).

108. 11 U.S.C. § 1113(b)(1)(A) (Supp. IV 1986).

109. *Compare id.* at § 1113 (c)(2) & (3) (court can approve debtor's motion to reject only if union has refused to accept proposal without good cause and balance of equities clearly favors rejection) *with* 130 Cong. Rec. S6182 (daily ed. May 22, 1984) (court can approve debtor's motion to reject only if union unjustifiably refused to accept proposal and balance of equities clearly favors rejection).

110. Courts have agreed that the balancing-of-the-equities requirement is an extension of the Supreme Court's holding in *NLRB v. Bildisco & Bildisco*, 465 U.S. 513 (1984). *See* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 92 (2d Cir. 1987); *In re* Amherst Sparkle Mkt., Inc., 75 Bankr. 847, 853 (Bankr. N.D. Ohio 1987); *In re* Kentucky Truck Sales, Inc., 52 Bankr. 797, 805 (Bankr. W.D. Ky. 1985); *In re* Cook United, Inc., 50 Bankr. 561, 564 (Bankr. N.D. Ohio 1985); *In re* Salt Creek Freightways, 47 Bankr. 835, 841 (Bankr. D. Wyo. 1985). Bankruptcy courts have found that by requiring the balance of the equities clearly to favor rejection, "Congress intended to clarify that rejection was only appropriate where the equities balance decidedly in favor of rejection." *Id.*; *see In re* Walway Co., 69 Bankr. 967, 974 n.18 (Bankr. E.D. Mich. 1987); *In re* Cook United, Inc., 50 Bankr. 561, 564 (Bankr. N.D. Ohio 1985) (quoting *Salt Creek*).

111. *See* 11 U.S.C. § 1113(e) (Supp. IV 1986).

The first reported decision interpreting section 1113 developed a nine-step test to determine if the statute's requirements have been met.[112] Seven of the nine steps are devoted to whether the debtor has complied with the procedural aspects of section 1113(b) by negotiating in good faith,[113] while the last two ask whether the union has rejected the debtor's proposal without good cause[114] and whether the balance of the equities clearly favors rejection.[115] The majority of courts that have interpreted section 1113 have adopted this test.[116] The test's most contro-

112. *See In re* American Provision Co., 44 Bankr. 907, 909 (Bankr. D. Minn. 1984). The *American Provision* court set out the nine steps as follows:

1. The debtor in possession must make a proposal to the Union to modify the [CBA].
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 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 [CBA], 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 [CBA].
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 [CBA].

Id. (footnote omitted).

113. *See supra* note 112 (steps one through seven). *See generally* Vian, *The Rejection of Collective Bargaining Agreements Since the 1984 Amendments: The Case Law Under New Bankruptcy Code Section 1113*, 91 Comm. L.J. 252, 254-63 (1986).

114. *See supra* note 112 (step eight).

115. *See supra* note 112 (step nine).

116. *See In re* Sol-Sieff Produce Co., 82 Bankr. 787, 791-92 (Bankr. W.D. Pa. 1988); *In re* Amherst Sparkle Mkt., Inc., 75 Bankr. 847, 849 (Bankr. N.D. Ohio 1987); *In re* Walway Co., 69 Bankr. 967, 972 (Bankr. E.D. Mich. 1987); *In re* William P. Brogna and Co., 64 Bankr. 390, 393 (Bankr. E.D. Pa. 1986); *In re* Kentucky Truck Sales, Inc., 52 Bankr. 797, 800-01 (Bankr. W.D. Ky. 1985); *In re* Wheeling-Pittsburgh Steel Corp., 50 Bankr. 969, 974-75 (Bankr. W.D. Pa.), *aff'd*, 52 Bankr. 997 (W.D. Pa. 1985), *vacated and remanded on other grounds sub nom.* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074 (3d Cir. 1986); *In re* Cook United, Inc., 50 Bankr. 561, 563 (Bankr. N.D. Ohio 1985); *In re* K&B Mounting, Inc., 50 Bankr. 460, 463-64 (Bankr. N.D. Ind. 1985); *In re* Carey Transp., Inc., 50 Bankr. 203, 207 (Bankr. S.D.N.Y. 1985), *aff'd on other grounds sub nom.* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82 (2d Cir. 1987); *In re* Salt Creek Freightways, 47 Bankr. 835, 837-38 (Bankr. D. Wyo. 1985). *But see In re* Royal Composing Room, Inc., 62 Bankr. 403, 406 (Bankr. S.D.N.Y. 1986) ("[t]his court eschews the talismanic nine-step analysis of Bankruptcy Code § 1113 first used in *In re American Provision Co.*"), *aff'd on other grounds*, 78 Bankr. 671 (S.D.N.Y. 1987).

Courts that have not followed the nine-step test have followed the express language of the statute. *See In re* Valley Kitchens, Inc., 52 Bankr. 493, 495-96 (Bankr. S.D. Ohio 1985) (finding statutory requirements not met where certain proposed modifications re-

versial element is the determination, at the procedural level, whether the proposed modifications are "necessary to permit the reorganization of the debtor."[117]

The problem with the necessity requirement stems from section 1113's ambiguous language[118] and the lack of House, Senate, or committee reports to clarify how necessary the modifications must be and to what end

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sulted in no savings to debtor); *In re* Fiber Glass Indus., Inc., 49 Bankr. 202, 203-04 (Bankr. N.D.N.Y. 1985) (holding that proposal must be made postpetition, provide for necessary modifications, and be based upon correct and reliable information; that debtor must provide union with relevant information, and meet with union representative; and that court shall approve only if union's refusal of proposal was without good cause, and equities favor rejection); *In re* Allied Delivery Sys. Co., 49 Bankr. 700, 701 (Bankr. N.D. Ohio 1985) (holding that rejection is conditioned on proposal being based on complete and reliable information and providing for necessary modifications treating all parties fairly and equitably; debtor providing union with relevant data and meeting with union in good faith; union refusing the proposal without good cause; and the equities favoring rejection).

117. *In re* American Provision Co., 44 Bankr. 907, 909 (Bankr. D. Minn. 1984). *Compare* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 88-89 (2d Cir. 1987) (debtor must show its proposed modifications necessary to allow successful reorganization, but modifications need not be absolutely minimal) *with* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1088-89 (3d Cir. 1986) (debtor must show its proposed modifications essential to prevent debtor's liquidation). Of the other eight steps, steps one, that the debtor has made a proposal to the union, two, that the proposal is based on complete and reliable information, five, that the debtor provided the union with relevant information to evaluate the proposal, and six, that the debtor and the union have met at reasonable times, are merely factual questions. *See, e.g.*, *In re* Amherst Sparkle Mkt., Inc., 75 Bankr. 847, 850-53 (Bankr. N.D. Ohio 1987); *In re* Kentucky Truck Sales, Inc., 52 Bankr. 797, 801-02, 804 (Bankr. W.D. Ky. 1985); *In re* K & B Mounting, Inc., 50 Bankr. 460, 467-68 (Bankr. N.D. Ind. 1985); *In re* Salt Creek Freightways, 47 Bankr. 835, 841 (Bankr. D. Wyo. 1985).

Two other steps, step seven, the good faith requirements, and, step eight, good cause requirements, have been construed as directly dependent on the debtor satisfying the necessity requirement. *See In re* K & B Mounting, Inc., 50 Bankr. 460, 465 (Bankr. N.D. Ind. 1985); *In re* Salt Creek Freightways, 47 Bankr. 835, 841 (Bankr. D. Wyo. 1985).

Moreover, the courts have construed the fair and equitable requirement (step four) relatively uniformly. *Compare* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1091 (3d Cir. 1986) (congressional intent of the fair and equitable requirement is that employees do not bear a disproportionate share of the reorganization burden) *with* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 90 (2d Cir. 1987) ("The purpose of this provision . . . 'is to spread the burden of saving the company to every constituency while ensuring that all sacrifice to a similar degree.' " (quoting Century Brass Prods. v. UAW (*In re* Century Brass Prods., Inc.), 795 F.2d 265, 273 (2d Cir.), *cert. denied*, 479 U.S. 949 (1986))). Accordingly, "[f]air and equitable treatment does not of necessity mean identical or equal treatment," *In re* Allied Delivery Sys. Co., 49 Bankr. 700, 703 (Bankr. N.D. Ohio 1985), but that all the affected parties shoulder a proportionate share of the burden. *See In re* Carey Transp., Inc., 50 Bankr. 203, 210 (Bankr. S.D.N.Y. 1985), *aff'd sub nom.* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82 (2d Cir. 1987); *In re* Salt Creek Freightways, 47 Bankr. 835, 838-39 (Bankr. D. Wyo. 1985). Consideration includes burdens carried pre- as well as postpetition. *See* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 91 (2d Cir. 1987).

Last, Courts uniformally have construed the balancing-of-equities standard (step nine) to be essentially the same as that enunciated by the Supreme Court in *Bildisco*. *See supra* note 110.

118. *See* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1086 (3d Cir. 1986); *see also* 130 Cong. Rec. S8888 (daily ed. June 29, 1984) (statement of Sen.

they must be necessary.[119] Accordingly, most courts have attempted to construe the necessity requirement of section 1113 by referring to the comments of its sponsors in Congress[120] and by comparing the proposed forms of the section with the version ultimately adopted by Congress.[121] The courts that have done so have reached conflicting results.[122]

II. THE NECESSITY REQUIREMENT

Facing substantially similar factual situations, the Second and Third Circuits have reached substantially different conclusions as to the meaning of the necessity requirement. In *Wheeling-Pittsburgh Steel Corp. v. United Steelworkers*,[123] the Third Circuit held that a debtor may not use section 1113(c) to reject a CBA unless the proposed modifications are essential to prevent liquidation.[124] In *Truck Drivers Local 807 v. Carey Transportation Inc.*,[125] the Second Circuit held that the necessity requirement of section 1113(b) is satisfied if the debtor has proposed, in good faith, modifications necessary to its successful, long-term reorganization.[126]

In *Wheeling-Pittsburgh*,[127] the Third Circuit found that the comments of the legislators indicated that the procedures and standards of section 1113 were those of the Packwood amendment.[128] Accordingly, it determined that the word "necessary" must be construed strictly because the

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Thurmond) ("Legitimate concerns have been raised regarding the broadness and vagueness of [the language in section 1113(b)].").

119. *See* Century Brass Prods. v. UAW (*In re* Century Brass Prods., Inc.), 795 F.2d 265, 274 (2d Cir.), *cert. denied*, 479 U.S. 949 (1986); Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1086 (3d Cir. 1986).

120. *See* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 88-89 (2d Cir. 1987); Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1086-88 (3d Cir. 1986); *In re* K & B Mounting, Inc., 50 Bankr. 460, 464 (Bankr. N.D. Ind. 1985); *In re* Salt Creek Freightways, 47 Bankr. 835, 838 (Bankr. D. Wyo. 1985). *But see In re* Carey Transp., Inc., 50 Bankr. 203, 207 (Bankr. S.D.N.Y. 1985) ("[T]his Court declines to give substantial weight to the aforementioned legislative statements and instead will be guided by the plain meaning of the statutory language . . . and by what little caselaw exists."), *aff'd sub nom.* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82 (2d Cir. 1987).

121. *See* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 89 (2d Cir. 1987); Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1086-88 (3d Cir. 1986); *In re* Allied Delivery Sys. Co., 49 Bankr. 700, 702 (Bankr. N.D. Ohio 1985).

122. *Compare* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 89 (2d Cir. 1987) ("[T]he legislative history strongly suggests that 'necessary' should not be equated with 'essential' or bare minimum.") *with* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1086-88 (3d Cir. 1986) (determining from the congressional statements that "necessary" should be construed strictly, and rejecting as "hypertechnical" the argument that "necessary" and "essential" have different meanings).

123. 791 F.2d 1074 (3d Cir. 1986).

124. *See id.* at 1088-89.

125. 816 F.2d 82 (2d Cir. 1987).

126. *See id.* at 90.

127. 791 F.2d 1074 (3d Cir. 1986).

128. *See* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074,

Packwood amendment allowed only "minimum modifications [in the employees' benefits and protections] that would permit the reorganization."[129] As a result, the court construed the phrase "a proposal . . . which provides for those necessary modifications in the employees [sic] benefits and protections"[130] to mean the debtor's proposal can contain only those modifications *essential* to the debtor's livelihood.[131] Thus, it was found that the debtor could not submit a proposal to modify the existing CBA over a five-year period without providing for restorations in worker pay if the debtor performed better than projected.[132] Similarly, the court interpreted the phrase "modifications . . . to permit the reorganization of the debtor"[133] as meaning that any proposal made by the debtor must contain only those modifications that would prevent immediate liquidation,[134] rather than those modifications that would permit successful, long-term reorganization.[135]

In *Carey*,[136] the Second Circuit disagreed sharply with the *Wheeling-Pittsburgh* holding.[137] The *Carey* court examined the legislative history of section 1113 and found it dispositive that the Committee had changed the word "minimum" in the Packwood amendment to "necessary."[138] It thereby concluded that "necessary" should not be equated with essential or bare minimum.[139] In addition, the court held that the section focuses not on the prevention of the debtor's liquidation, but rather on the debtor's likelihood of successful reorganization.[140] Thus, it affirmed the bankruptcy court's finding "that the proposed modifications [were] necessary to rehabilitate the debtor into a competitive business enterprise in its particular market and to provide for a successful reorganization."[141]

A. *The Procedural Hurdles of Section 1113(b)*

From the legislative statements, earlier drafts and final form of section 1113, it is apparent Congress intended to allow debtors to propose modi-

1087-88 (3d Cir. 1986); *supra* notes 88-100 and accompanying text (discussing Packwood amendment).

129. *See* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1088 (3d Cir. 1986) (quoting 130 Cong. Rec. S6181 (daily ed. May 22, 1984)).

130. 11 U.S.C. § 1113(b)(1)(A) (Supp. IV 1986).

131. *See* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1088 (3d Cir. 1986).

132. *See id.* at 1089-90.

133. 11 U.S.C. § 1113(b)(1)(A) (Supp. IV 1986).

134. *See* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1089 (3d Cir. 1986).

135. *See id.*

136. 816 F.2d 82 (2d Cir. 1987).

137. 791 F.2d 1074 (3d Cir. 1986).

138. *See* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 89 (2d Cir. 1987).

139. *See id.* at 90.

140. *See id.* at 89-90.

141. *In re* Carey Transp., Inc., 50 Bankr. 203, 209 (Bankr. S.D.N.Y. 1985), *aff'd sub nom.* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82 (2d Cir. 1987).

fications in CBA's necessary to a successful reorganization, not merely those essential to the debtor's short-term survival.

First, in analyzing section 1113, or, as the Third Circuit did in *Wheeling-Pittsburgh*, the Packwood amendment,[142] it becomes clear that the primary purpose of both is to place the responsibility for modifying any CBA on the parties,[143] thereby minimizing the need for judicial intervention.[144] To effectuate this purpose, both the statute and its predecessor amendment set procedural hurdles to force the debtor to propose modifications in the CBA.[145] The presumption is that if the debtor proposes modifications in good faith[146] and fully discloses the information to enable the union to confirm the debtor's need for such modifications,[147] the union will have an incentive to negotiate a settlement, and thereby preserve the jobs of its members, rather than gamble on its ability to convince the court that its refusal to do so is justified.[148] Conversely, requiring the debtor to comply with the standards of section 1113 protects the union from a debtor seeking rejection when it is unnecessary for its reorganization.

The effect of interpreting "necessary to permit reorganization" as meaning "essential to prevent liquidation" would be to discourage good faith negotiation and prevent modifications of CBA's in all but the most dire cases. If courts set the specific procedural hurdles too high, as the Third Circuit has done, then they remove the incentive to negotiate a

142. *See* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1086-87 (3d Cir. 1986).

143. *See supra* note 97 and accompanying text.

144. *See* Century Brass Prods., Inc. v. UAW (*In re* Century Brass Prods., Inc.), 795 F.2d 265, 273 (2d Cir.), *cert. denied*, 479 U.S. 949 (1986); 130 Cong. Rec. S8898 (daily ed. June 29, 1984) (statement of Sen. Packwood); 130 Cong. Rec. S6184 (daily ed. May 22, 1984) (statement of Sen. Packwood).

145. *See* 11 U.S.C. § 1113(b) (Supp. IV 1986); Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 88 (2d Cir. 1987); Wheeling-Pittsburgh Steel Corp. v. United Steelworkers, 791 F.2d 1074, 1088 (3d Cir. 1986); 130 Cong. Rec. S6184 (daily ed. May 22, 1984) (statement of Sen. Packwood).

146. *See* 11 U.S.C. § 1113 (b)(2) (Supp. IV 1986); *supra* note 12.

147. *See In re* K & B Mounting, Inc., 50 Bankr. 460, 467-68 (Bankr. N.D. Ind. 1985); In re Carey Transp., Inc., 50 Bankr. 203, 208 (Bankr. S.D.N.Y. 1985), *aff'd sub nom.* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82 (2d Cir. 1987); 130 Cong. Rec. S6184 (daily ed. May 22, 1984) (statement of Sen. Packwood).

148. *See* 130 Cong. Rec. S6184 (daily ed. May 22, 1984) (statement of Sen. Packwood); Note, *Bankruptcy and the Union's Bargain: Equitable Treatment of Collective Bargaining Agreements*, 39 Stan. L. Rev. 1015, 1051 (1987) (stating reasons why a union may resist requested modifications in a CBA made by a debtor). A union might actually resist modification in order to cause liquidation of the debtor. *See* Bordewieck & Countryman, *supra* note 39, at 319. For example, the union may wish to sacrifice employees covered by the debtor's CBA in order to preserve the rights of other union members under CBA's with solvent employers. *See* Landmark Hotel & Casino, Inc. v. Local Joint Executive Board of Las Vegas, Culinary Workers Union, Local No. 226 (*In re* Landmark Hotel & Casino, Inc.), 78 Bankr. 575, 578, 580 (Bankr. 9th Cir. 1987) (union rejected debtor's modification of its CBA because a clause in other CBA's with different employers required that if one employer received concessions from union, union would have to extend those concessions to all other employers).

settlement, because a union always can reject some or all of a debtor's proposal, whether in good faith or not, as not essential to prevent liquidation.[149] On appeal to the bankruptcy court, this high standard makes it almost impossible for the debtor to prove the union's refusal was unjustified. Accordingly, rather than encouraging negotiated modifications in CBA's, this interpretation discourages them by placing the debtor in an unfair bargaining position,[150] because it enables the union to use the threat of an almost certainly unfavorable bankruptcy court ruling as leverage against the debtor. This would make the debtor's remedy of rejection difficult to realize, denying it an important remedial device and defeating the Bankruptcy Code's goal of flexibility.[151]

In contrast, allowing the debtor to make modifications that are necessary to successful, long-term reorganization gives it the room to bargain in good faith. Moreover, because the necessity requirement is viewed as a mechanism to give both parties the incentive to negotiate in good faith,[152] courts have held that where a debtor-in-possession has shown no more than the desirability or convenience of obtaining certain modifications, it has failed to show that they are necessary.[153] Thus, interpreting the necessity requirement as allowing the debtor to propose those modifications it believes are appropriate to permit reorganization puts the debtor and the union in equal bargaining positions, thus encouraging negotiation and decreasing the need for judicial intervention.

Further examination also makes it clear that the original House bill, the Packwood amendment, and, therefore, section 1113, mandate that the debtor's proposal must be made with a view to aiding long-term reorganization.[154] Although the original House bill would have allowed modifications to serve successful long-term reorganization,[155] it would have required the debtor to compromise this goal for the immediate preservation of jobs.[156] It also required the bankruptcy court to determine that, absent rejection of the CBA, the debtor would liquidate.[157] The Packwood amendment liberalized these strict standards by requiring that the relative sacrifice of the workers merely be one of several factors the

149. *See In re* Royal Composing Room, Inc., 62 Bankr. 403, 407 (Bankr. S.D.N.Y. 1986), *aff'd*, 78 Bankr. 671 (S.D.N.Y. 1987); Gibson, *supra* note 31 at 341.

150. *See In re Royal Composing Room, Inc.*, 62 Bankr. at 407.

151. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 525 (1984).

152. *See supra* notes 145-47 and accompanying text.

153. *See, e.g., In re* Valley Kitchens, Inc., 52 Bankr. 493, 495-97 (Bankr. S.D. Ohio 1985); In re K & B Mounting, Inc., 50 Bankr. 460, 468 (Bankr. N.D. Ind. 1985).

154. *See* 130 Cong. Rec. S8898 (daily ed. June 29, 1984) (statement of Sen. Packwood); 130 Cong. Rec. S6181 (daily ed. May 22, 1984); 130 Cong. Rec. H1842 (daily ed. March 21, 1984); Wines, *An Overview of the 1984 Bankruptcy Amendments: Some Modest Protection for Labor Agreements*, 36 Lab. L.J. 911, 917 (1985).

155. *See* H.R. 5174, 98th Cong., 2d Sess. sec. 277, 130 Cong. Rec. H1842 (daily ed. Mar. 21, 1984).

156. *See id.*

157. *See id.*

debtor must consider in making its proposal,[158] and by substituting the balancing-of-the-equities standard for the essential-to-prevent-liquidation standard of the House bill.[159] The Packwood amendment, however, preserved the House bill's focus on successful reorganization.[160] Accordingly, because Congress did not alter the language of this portion of the Packwood amendment, Congress adopted the amendment's focus.

Moreover, the final form of section 1113, when read in conjunction with the rest of the Bankruptcy Code, indicates that debtors should be able to focus their proposals toward long-term reorganization. Although reorganization does not mean the debtor must develop a comprehensive plan of reorganization at this initial stage in the bankruptcy proceeding,[161] it does mean that successful reorganization forms the ultimate purpose behind the debtor's action.[162] Section 1129(a)(11) of the Bankruptcy Code[163] states that in order to confirm a plan of reorganization, the bankruptcy court must examine the feasibility of the debtor achieving fiscal health.[164] Section 1113 and the legislative statements must be read in conjunction with this feasibility requirement.[165] Accordingly, any proposal made by the debtor must be made with a view toward successful, long-term reorganization, rather than toward merely preventing liquidation.[166]

Once it is accepted that the debtor's proposals should relate to the success of a confirmed, long-term plan of reorganization, which potentially lies years away, a requirement that these proposals be essential to that future reorganization is absurd, because it is impossible for the debtor or the bankruptcy court to know what modifications in a CBA are essential to an event so far away.[167] Another aspect of section 1113's legislative history also indicates that the necessity requirement should not be construed as allowing debtors to propose only essential modifica-

158. *See* 130 Cong. Rec. S6181 (daily ed. Mar. 21, 1984); *supra* note 99 and accompanying text.

159. *See id.* at S6182; *supra* note 100 and accompanying text.

160. *See* 130 Cong. Rec. S8898 (daily ed. June 29, 1984) (Statement of Sen. Packwood) ("As to the first requirement [of § 1113], similar to the proposal which I had made, only modifications which are necessary to successful reorganization may be proposed."); *supra* note 93 and accompanying text.

161. *See* 130 Cong. Rec. S8892 (daily ed. June 29, 1984) (statement of Sen. Hatch); *supra* note 25.

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

163. *See* 11 U.S.C. § 1129(a)(11) (1982).

164. *See supra* note 5 and accompanying text; *see also* Teamsters Nat'l Freight Indus. Negotiating Comm. v. U.S. Truck Co. (*In re* U.S. Truck Co.), 800 F.2d 581, 589 (6th Cir. 1986) (discussing factors relevent to determining feasibility of a debtor's plan of reorganization).

165. *See* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 89 (2d Cir. 1987); *In re* Royal Composing Room, Inc., 62 Bankr. 403, 417 (Bankr. S.D.N.Y. 1986), *aff'd*, 78 Bankr. 671 (S.D.N.Y. 1987).

166. *See Carey Transp. Inc.*, 816 F.2d at 89; *In re Royal Composing Room, Inc.*, 62 Bankr. at 417.

167. *See* NLRB v. Bildisco & Bildisco (*In re* Bildisco), 682 F.2d 72, 80 (3d Cir. 1982), *aff'd*, 465 U.S. 513 (1984).

tions in CBA's: Congress rejected language mandating only minimal modifications.[168]

Moreover, because Congress in section 1113(e)[169] expressly provides debtors with emergency, interim relief from CBA's if such relief is found to be essential to prevent liquidation,[170] it could not have intended that the same standard be applied to the necessity requirement of section 1113(b).[171] Otherwise, a debtor truly facing liquidation would use the emergency procedures found in 1113(e) to obtain relief rather than the elaborate procedures of sections 1113(b) and (c). Although section 1113(e) provides only interim relief,[172] that relief can be structured to extend past the confirmation of a plan of reorganization, or even allow rejection of a CBA.[173] Clearly, Congress did not intend section 1113(e) to be used as a by-pass of sections 1113(b) and (c).[174] Therefore, section 1113(b) must not be focused on the short-term, but oriented to the successful reorganization of the debtor.

In addition to running counter to the legislative history of section 1113 and section 1129(a)(11) of the Bankruptcy Code, the courts that interpret the necessity requirement of section 1113(b) as meaning that debtors only may make proposals essential to avoid liquidation render irrelevent the substantive balancing-of-the-equities standard contained in section 1113(c).[175] The legislators retained the balancing-of-equities requirement so that, in situations where negotiations have failed, the bankruptcy court would determine whether the CBA should be rejected.[176] Under the Third Circuit's interpretation, the balancing-of-the-equities requirement does not fulfill its intended function; if modifications are essential to avoid liquidation, and the union refuses them, the equities always will balance in favor of rejection of the CBA.[177] In the alternative, if the

168. *See* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 89 (2d Cir. 1987).

169. *See* 11 U.S.C. § 1113(e) (Supp. IV 1986).

170. *See id.*; *see, e.g.*, Landmark Hotel & Casino, Inc. v. Local Joint Executive Board of Las Vegas, Culinary Workers Union, Local No. 226 (*In re* Landmark Hotel & Casino, Inc.), 78 Bankr. 575, 585 (Bankr. 9th Cir. 1987).

171. *See In re* Royal Composing Room, Inc., 62 Bankr. 403, 417-18 (Bankr. S.D.N.Y. 1986), *aff'd*, 78 Bankr. 671 (S.D.N.Y. 1987); *In re* Allied Delivery Sys. Co., 49 Bankr. 700, 702 (Bankr. N.D. Ohio 1985).

172. *See* 11 U.S.C. § 1113(e) (Supp. IV 1986).

173. *See* Landmark Hotel & Casino, Inc. v. Local Joint Executive Board of Las Vegas, Culinary Workers Union, Local No. 226 (*In re* Landmark Hotel & Casino, Inc.), 78 Bankr. 575, 582 (Bankr. 9th Cir. 1987). In *Landmark*, the interim relief was fashioned in such a way that the CBA was rejected. *See id.*

174. *See In re Landmark Hotel & Casino, Inc.*, 78 Bankr. at 582; *In re* Beckley Coal Mining Co., 81 Bankr. 6, 7 (Bankr. D. Del. 1987).

175. *See* 11 U.S.C. § 1113 (c)(3) (Supp. IV 1986).

176. *See* Landmark Hotel & Casino, Inc. v. Local Joint Executive Board of Las Vegas, Culinary Workers Union, Local No. 226 (*In re* Landmark Hotel & Casino, Inc.), 78 Bankr. 575, 583 (Bankr. 9th Cir. 1987); *In re* K & B Mounting, Inc., 50 Bankr. 460, 466 (Bankr. N.D. Ind. 1985); 130 Cong. Rec. S8888 (daily ed. June 29, 1984) (statement of Sen. Thurmond).

177. *See In re* Sol-Sieff Produce Co., 82 Bankr. 787, 795 (Bankr. W.D. Pa. 1988); *In re*

proposals made by the debtor are not found to be absolutely essential to prevent liquidation, then the court will find that the debtor has not met the requirements of section 1113(b) and will not perform a substantive balancing of equities.[178]

B. *Balancing the Equities*

Although the Second Circuit's interpretation of the necessity requirement in *Truck Drivers Local 807 v. Carey Transportation Inc.*[179] is the proper one, its reading of section 1113's balancing-of-the-equities requirement shows how the balancing can be skewed in favor of the debtor.[180] The balancing-of-the-equities standard found in section 1113 codifies the *Bildisco* balance-of-interests approach.[181] Accordingly, the Second Circuit determined that the bankruptcy court is bound to "focus on the ultimate goal of Chapter 11 when considering these equities."[182] It noted that "[t]he Bankruptcy Code does not authorize freewheeling consideration of every conceivable equity, but rather only how the equities relate to the success of the reorganization."[183] As a result, the Second Circuit gleaned six "permissible equitable considerations" to be evaluated.[184] Of the six, however, four clearly are structured to favor the

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Walway Co., 69 Bankr. 967, 973-74 (Bankr. E.D. Mich. 1987); *In re* Kentucky Truck Sales, Inc., 52 Bankr. 797, 806 (Bankr. W.D. Ky. 1985).

178. *See In re* William P. Brogna and Co., 64 Bankr. 390, 393 (Bankr. E.D. Pa. 1986) (applying the essential-to-avoid-liquidation standard and finding that where the debtor fails to meet this requirement balancing of the equities need only be done for "completeness").

179. 816 F.2d 82 (2d Cir. 1987).

180. *See infra* notes 184-88 and accompanying text (discussing equities balanced in *Truck Drivers Local 807 v. Carey Transp. Inc.*).

181. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527 (1984); *supra* note 110.

182. Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 92 (2d Cir. 1987) (quoting NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527 (1984)).

183. *Id.* at 92-93 (quoting NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527 (1984)).

184. *Id.* at 93. The six equities are:

> (1) the likelihood and consequences of liquidation if rejection is not permitted; (2) the likely reduction in the value of creditors' 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.; *see also In re* Royal Composing Room, Inc., 62 Bankr. 403, 408 (Bankr. S.D.N.Y. 1986) ("The balance of the equities . . . clearly favors rejection when it is apparent that a debtor is in need of substantial relief under a union contract and the bargaining process has failed to produce any results and is unlikely to produce results in the forseeable future." (citation omitted), *aff'd*, 78 Bankr. 671 (S.D.N.Y. 1987)); *In re* Kentucky Truck Sales, Inc., 52 Bankr. 797, 806 (Bankr. W.D. Ky. 1985) ("[T]he primary question in a balancing test is the effect the rejection of the agreement will have on the debtor's prospects for reorganization.").

debtor.[185] The sixth equity appears to take the bad faith of the debtor into account,[186] but the facts of the *Carey* case belie the court's apparent concern that a debtor should not use Chapter 11 for the primary purpose of ridding itself of its CBA. Ample evidence exists that the *Carey* debtor did precisely that.[187] The fifth equity is the only one to take into account the effect rejection will have on the employees,[188] and even this concern is conditioned upon creditors being able to bear the costs of the CBA.[189]

The failure of the Second Circuit to take into account the hardship of the employees runs directly counter to the mandate of *Bildisco*. *Bildisco* expressly states that "the Bankruptcy Court must consider . . . the impact of rejection on the employees."[190] Moreover, section 1113(c) codifies this consideration.[191] Accordingly, in striking a balance between the interests of the debtor, its creditors, and its employees, the 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."[192]

In practical terms, the hardship of the employees should be taken into account because a debtor seeking to reject its CBA "can be expected to argue that rejection is essential to a successful reorganization, whether it believes that to be the case or not."[193] In contrast, a union would be foolish to argue against rejection if such was justified to prevent liquidation, because with liquidation the union members' jobs would be lost.[194] The equity balance, therefore, should at least reflect the possibility that rejection of the CBA will not substantially promote successful reorgani-

185. *See supra* note 184. For example, if rejection should cause a strike, the equities focus solely on the strike's effect on the debtor. *See* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 93 (2d Cir. 1987). Moreover, if the contract is rejected, the employees will have an unsecured prepetition claim against the estate, *see supra* note 31, thus, it is unlikely that the employees' claim against the estate would have substantial effect on the debtor. *See infra* note 195.

186. *See* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 93 (2d Cir. 1987).

187. Not only did Carey begin the rejection process the day after it filed its petition for reorganization, but it had stated to the union prior to entering Chapter 11 that if the union failed to accept certain modifications in the agreement, Carey would be forced into Chapter 11. *See id.* at 85. Moreover, the debtor's proposal pursuant to § 1113 sought much deeper concessions than the prepetition proposal and the debtor rejected a union counterproposal that was similar to one made by Carey prior to entering Chapter 11. *See In re* Carey Transp., Inc., 50 Bankr. 203, 205 (Bankr. S.D.N.Y. 1985), *aff'd on other grounds sub nom.* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82 (2d Cir. 1987). The bankruptcy court noted that Carey's financial difficulties were primarily a result of excessive labor costs, which Carey attributed to its CBA. *See id.* at 204.

188. *See* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 93 (2d Cir. 1987); *supra* note 184.

189. *See* Local Unions 20 v. Brada Miller Freight Sys., Inc. (*In re* Brada Miller Freight Sys., Inc.), 702 F.2d 890, 900 (11th Cir. 1983).

190. NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527 (1984).

191. *See* Gibson, *supra* note 31, at 347-48; *supra* note 110.

192. NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527 (1984).

193. Bordewieck & Countryman, *supra* note 39, at 319.

194. *See id.*

zation, and in such cases rejection should not be used to subordinate the claims of the debtor's employees. The bankruptcy court should take into account the adequacy of the bankruptcy law to compensate unionized employees for their monetary and nonmonetary losses.[195]

CONCLUSION

Section 1113(b) acts as a procedural hurdle that, in order to encourage debtors and unions to negotiate modifications of CBA's in good faith, and to allow the courts to balance the equities only when the parties fail, should be set neither too high nor too low. In considering the equities, bankruptcy courts should focus on the need for the debtor to reorganize successfully, but should temper this concern with adequate regard for the effect that rejection of the CBA will have on the debtor's employees and the adequacy of the bankruptcy laws to compensate the employees for the loss of monetary and nonmonetary benefits. This will ensure that CBA's will be rejected only in cases where good faith negotiations have taken place and failed and where the equities in favor of both retention and rejection have been considered.

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195. Section 502(c) of the Bankruptcy Code, 11 U.S.C. § 502(c) (1982 & Supp. IV 1986), requires that losses suffered by employees covered by a CBA as a result of its rejection be estimated and accounted for in a plan of reorganization. *See* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 530 n.12 (1984). This includes losses attributable to fringe benefits or security provisions such as seniority rights. *See id. But see* Local Unions 20 v. Brada Miller Freight Sys., Inc. (*In re* Brada Miller Freight Sys., Inc.), 702 F.2d 890, 900 (11th Cir. 1983) (stating that nonmonetary benefits cannot be compensated under reorganization plan). Moreover, bankruptcy courts have held that claims arising out of rejection of a CBA are limited by § 502(b)(7). *See* 11 U.S.C. § 502(b)(7) (Supp. IV 1986) (limiting claims arising from termination of employment contracts to one year of compensation, without acceleration, following the earlier of the filing of petition for reorganization or termination of the employment). *See In re* N & T Assoc., Inc., 78 Bankr. 285, 288 (Bankr. D. Nev. 1987); *In re* Continental Airlines Corp., 64 Bankr. 865, 873 (Bankr. S.D. Tex. 1986). *But see In re* Gee & Missler Serv., Inc., 62 Bankr. 841, 843 (Bankr. E.D. Mich. 1986) (holding CBA's not to be employment contracts within the meaning of § 502(b)(7)). Moreover, if the liquidation value of the estate is small, these claimants probably would not receive compensation. *See In re* Carey Transp., Inc., 50 Bankr. 203, 213 (Bankr. S.D.N.Y. 1985), *aff'd on other grounds sub nom.* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82 (2d Cir. 1987).