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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 have enabled bankruptcy trustees to reject executory contracts. In the 1970's, debtors began using this fundamen


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

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4. See supra note 3.


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' representative¹⁴ 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

¹⁰. See id. at 532-33.
(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 relevant 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.
¹⁴. 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.\textsuperscript{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.\textsuperscript{19} For example, in \textit{Wheeling-Pittsburgh Steel Corp. v. United Steelworkers},\textsuperscript{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.\textsuperscript{21} In contrast, the Second Circuit, in \textit{Truck Drivers Local 807 v. Carey Transportation Inc.},\textsuperscript{22} held that a debtor’s modifications need only be necessary for its successful long-term reorganization.\textsuperscript{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 \textit{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.

\begin{footnotes}
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\footnote{18. See 11 U.S.C. § 1113(c)(3); \textit{supra} note 12.}
\footnote{19. See 11 U.S.C. § 1113(b)(1)(A); \textit{supra} note 12; \textit{supra} note 13 and accompanying text.}
\footnote{20. 791 F.2d 1074 (3d Cir. 1986).}
\footnote{21. \textit{Wheeling-Pittsburgh Steel Corp. v. United Steelworkers}, 791 F.2d 1074, 1088-89 (3d Cir. 1986).}
\footnote{22. 816 F.2d 82 (2d Cir. 1987).}
\footnote{23. \textit{See id.} at 90. Despite the fact that Webster's dictionary indicates that the words “necessary” and “essential” have the same meaning, \textit{compare} Webster’s New Universal Unabridged Dictionary 1200 (2d ed. 1983) (stating that necessary means that which “cannot be dispensed with; essential”) \textit{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. \textit{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.” \textit{See id.} at 490.}
\end{footnotes}
I. REJECTION OF COLLECTIVE BARGAINING AGREEMENTS UNDER 11 U.S.C. SECTION 1113

Chapter 11 of the Bankruptcy Code provides a debtor corporation with the opportunity to reorganize while keeping its creditors at bay. The rationale underlying reorganization is that a successful reorganization is preferable to liquidation. 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. Thus, Chapter

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), upon which 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. § 1103 (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).


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.

11 is intended to achieve not mere short-term relief, but successful, long-term restructuring of the debtor's affairs. 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."

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. 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." The scope of section 365 is broad. The trustee may reject an executory contract if he perceives any business advantage in doing so. 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." 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.


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).


In the 1970's, debtors began using section 313 of the Bankruptcy Act, and then its successor, section 365(a), to reject CBA's. This tactic brought the rehabilitative policy of the Bankruptcy Code into conflict with the national labor policy of encouraging collective bargaining to ensure industrial peace. In addressing this conflict, appellate courts agreed that CBA's were executory contracts within section 365(a), but disagreed whether rejection should proceed under the business judgment test or under some stricter test. 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 as an unfair labor practice. In \textit{NLRB v. Bildisco} &...
Bildisco, the Supreme Court addressed these issues, holding that CBA's could be rejected under section 365(a) if the balance of equities favored rejection, and that such rejection was not an unfair labor practice.

A. NLRB v. Bildisco & Bildisco

NLRB v. Bildisco & Bildisco 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. The bankruptcy court then permitted Bildisco to reject its CBA. Meanwhile, the union had brought an administrative proceeding before the National Labor Relations Board ("NLRB") against Bildisco alleging violation of the agreement. The NLRB ordered Bildisco to comply with the terms of the CBA, notwithstanding notification that the bankruptcy court had permitted Bildisco to reject it two months earlier. The union appealed the bankruptcy court's ruling to the district court and then to the Third Circuit, while the NLRB applied to the Third Circuit for enforcement of its order. 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. The NLRB and the union appealed to the Supreme Court, which granted certiorari to resolve the conflict among the courts of appeals as to the proper standard for rejecting CBA's.

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

45. See id. at 525-26.
46. See id. at 534.
49. See id.
51. See Bildisco, 255 N.L.R.B. at 1205.
53. See id. at 75.
56. See id. at 84-85.
tions Act. The Court determined that because Congress expressly exempted CBA’s subject to the Railway Labor Act from section 365(a) 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). Accordingly, it held that these types of contracts could be rejected.

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. The NLRB and the union had argued that CBA’s could be rejected only if it was essential to prevent liquidation of the debtor. Although the majority concluded that the business judgment test did not sufficiently protect the national labor policy, it rejected the strict standard, opting instead for a balancing of interests approach. Accordingly, it stated that rejection requires a finding that such action would serve the bankruptcy policy of encouraging successful reorganization. To determine this, the bankruptcy court must balance the interests of the affected parties: the debtor, its creditors, and the employees.

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. Accordingly, the NLRB’s attempt to enforce the agreement had “run directly counter to the express provisions of the Bankruptcy Code.” 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(l) of the Bankruptcy Act, see supra note 3).


62. See id. at 523.

63. See id.

64. See id.


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).


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.\textsuperscript{73} Four justices dissented from the Court's decision in \textit{Bildisco}.\textsuperscript{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."\textsuperscript{75} Some members of Congress, who were already struggling with extensive revisions in the bankruptcy laws, shared this concern.\textsuperscript{76}

\textbf{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\textsuperscript{77} to protect CBA's from what they perceived as a "new collective-bargaining weapon."\textsuperscript{78} They feared that the \textit{Bildisco} holding would allow the unilateral rejection, rather than renegotiation, of CBA's by debtors.\textsuperscript{79} This ability would discourage collective bargaining and thus would run counter to the policy expressed in the National Labor Relations Act.\textsuperscript{80}

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

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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. 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 and had provided the union with relevant financial and other information. The court also would have had to determine that, absent rejection, the jobs of the workers would be lost and any reorganization would fail. 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.

When the bill reached the Senate, Senator Strom Thurmond and other members of the Judiciary Committee found the labor provision "completely unacceptable." 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. 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. 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.

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. The Packwood amendment provided that in order for the debtor to reject a CBA, he first would have to propose to the

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).
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,
1984 and the President signed it into law on July 10.\textsuperscript{103}

Section 1113, as finally passed has two aspects: the first involves a series of procedural requirements designed to promote collective bargaining,\textsuperscript{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.\textsuperscript{105} The procedural aspect of section 1113(b) closely resemble those in the Packwood amendment.\textsuperscript{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"\textsuperscript{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."\textsuperscript{108} The substantive standard of balancing the equities, contained in section 1113(c), is the same as that of the Packwood amendment,\textsuperscript{109} which slightly modified the balancing of interests standard enunciated in \textit{Bildisco}.\textsuperscript{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.\textsuperscript{111}

\textsuperscript{105} See Century Brass Prods., Inc., 795 F.2d at 273; Gibson, \textit{supra} note 31, at 335.
\textsuperscript{109} \textit{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) \textit{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).
\textsuperscript{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. The 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, while the last two ask whether the union has rejected the debtor's proposal without good cause and whether the balance of the equities clearly favors rejection. The majority of courts that have interpreted section 1113 have adopted this test. 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).


114. See supra note 112 (step eight).

115. See supra note 112 (step nine).


116 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

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 proportional 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 uniformly 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.

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

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*, 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. In *Truck Drivers Local 807 v. Carey Transportation Inc.*, 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.

In *Wheeling-Pittsburgh*, 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. Accordingly, it determined that the word “necessary” must be construed strictly because the

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


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." As a result, the court construed the phrase "a proposal . . . which provides for those necessary modifications in the employees' [sic] benefits and protections" to mean the debtor's proposal can contain only those modifications essential to the debtor's livelihood. 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. Similarly, the court interpreted the phrase "modifications . . . to permit the reorganization of the debtor" as meaning that any proposal made by the debtor must contain only those modifications that would prevent immediate liquidation, rather than those modifications that would permit successful, long-term reorganization.

In Carey, the Second Circuit disagreed sharply with the Wheeling-Pittsburgh holding. The Carey court examined the legislative history of section 1113 and found it dispersive that the Committee had changed the word "minimum" in the Packwood amendment to "necessary." It thereby concluded that "necessary" should not be equated with essential or bare minimum. 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. 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."

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-
ifications 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, it becomes clear that the primary purpose of both is to place the responsibility for modifying any CBA on the parties, thereby minimizing the need for judicial intervention. To effectuate this purpose, both the statute and its predecessor amendment set procedural hurdles to force the debtor to propose modifications in the CBA. The presumption is that if the debtor proposes modifications in good faith and fully discloses the information to enable the union to confirm the debtor's need for such modifications, 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. 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

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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.
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. 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, 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.

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, 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. 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. Although the original House bill would have allowed modifications to serve successful long-term reorganization, it would have required the debtor to compromise this goal for the immediate preservation of jobs. It also required the bankruptcy court to determine that, absent rejection of the CBA, the debtor would liquidate. The Packwood amendment liberalized these strict standards by requiring that the relative sacrifice of the workers merely be one of several factors the

152. See supra notes 145-47 and accompanying text.
156. See id.
157. See id.
debtor must consider in making its proposal, and by substituting the balancing-of-the-equities standard for the essential-to-prevent-liquidation standard of the House bill. The Packwood amendment, however, preserved the House bill's focus on successful reorganization. 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, it does mean that successful reorganization forms the ultimate purpose behind the debtor's action. Section 1129(a)(11) of the Bankruptcy Code states that in order to confirm a plan of reorganization, the bankruptcy court must examine the feasibility of the debtor achieving fiscal health. Section 1113 and the legislative statements must be read in conjunction with this feasibility requirement. Accordingly, any proposal made by the debtor must be made with a view toward successful, long-term reorganization, rather than toward merely preventing liquidation.

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. 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 modific-

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.
tions in CBA's: Congress rejected language mandating only minimal modifications.\textsuperscript{168}

Moreover, because Congress in section 1113(e)\textsuperscript{169} expressly provides debtors with emergency, interim relief from CBA's if such relief is found to be essential to prevent liquidation,\textsuperscript{170} it could not have intended that the same standard be applied to the necessity requirement of section 1113(b).\textsuperscript{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,\textsuperscript{172} that relief can be structured to extend past the confirmation of a plan of reorganization, or even allow rejection of a CBA.\textsuperscript{173} Clearly, Congress did not intend section 1113(e) to be used as a by-pass of sections 1113(b) and (c).\textsuperscript{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 irrelevant the substantive balancing-of-the-equities standard contained in section 1113(c).\textsuperscript{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.\textsuperscript{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.\textsuperscript{177} In the alternative, if the

\textsuperscript{168} See Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82, 89 (2d Cir. 1987).
\textsuperscript{170} See id.; see, e.g., Landmark Hotel & Casino, Inc. v. Local Joint Executive Board of Las Vegas, Culinary Workers Union, Local No. 226 (\textit{In re} Landmark Hotel & Casino, Inc.), 78 Bankr. 575, 585 (Bankr. 9th Cir. 1987).
\textsuperscript{172} See 11 U.S.C. § 1113(e) (Supp. IV 1986).
\textsuperscript{173} See Landmark Hotel & Casino, Inc. v. Local Joint Executive Board of Las Vegas, Culinary Workers Union, Local No. 226 (\textit{In re} Landmark Hotel & Casino, Inc.), 78 Bankr. 575, 582 (Bankr. 9th Cir. 1987). In \textit{Landmark}, the interim relief was fashioned in such a way that the CBA was rejected. See \textit{id}.
\textsuperscript{174} See \textit{In re Landmark Hotel & Casino, Inc.}, 78 Bankr. at 582; \textit{In re} Beckley Coal Mining Co., 81 Bankr. 6, 7 (Bankr. D. Del. 1987).
\textsuperscript{177} See \textit{In re} Sol-Sieff Produce Co., 82 Bankr. 787, 795 (Bankr. W.D. Pa. 1988); \textit{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.\textsuperscript{178}

### B. Balancing the Equities

Although the Second Circuit's interpretation of the necessity requirement in \textit{Truck Drivers Local 807 v. Carey Transportation Inc.}\textsuperscript{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.\textsuperscript{180} The balancing-of-the-equities standard found in section 1113 codifies the \textit{Bildisco} balance-of-interests approach.\textsuperscript{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."\textsuperscript{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."\textsuperscript{183} As a result, the Second Circuit gleaned six "permissible equitable considerations" to be evaluated.\textsuperscript{184} Of the six, however, four clearly are structured to favor the

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\textsuperscript{178} See \textit{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").

\textsuperscript{179} 816 F.2d 82 (2d Cir. 1987).

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


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

\textsuperscript{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.

\textit{Id.}; see also \textit{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 foreseeable future." (citation omitted), \textit{aff'd}, 78 Bankr. 671 (S.D.N.Y. 1987)); \textit{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.").
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." Moreover, section 1113(c) codifies this consideration. 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."

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." 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. The equity balance, therefore, should at least reflect the possibility that rejection of the CBA will not substantially promote successful reor-
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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