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Nobody Likes Rejection Unless You're a Debtor in Chapter 11: Rejection of Collective Bargaining Agreements Under 11 U.S.C. § 1113

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NOTES

NOBODY LIKES REJECTION UNLESS YOU'RE A DEBTOR IN CHAPTER 11: REJECTION OF COLLECTIVE BARGAINING AGREEMENTS UNDER 11 U.S.C. § 1113

I. INTRODUCTION

On June 16, 1988, President Reagan signed into law H.R. 2969,[1] the Retiree Benefits Bankruptcy Protection Act of 1988,[2] which amended Chapter 11 of the Bankruptcy Code [hereinafter the "Code"].[3] The amendment [hereinafter "section 1114"] is an attempt to address the discernable problems occurring in the wake of the filing of a Chapter 11 petition by LTV Corporation.[4] Clearly, the intent of Congress was to provide a protective measure to prevent the termination of retiree benefits established pursuant to collective bargaining agreements.[5]

The passage of section 1114 is significant because the legislative history accompanying the amendment outlines the standard for determining whether termination of retiree benefits should be permitted under Chapter 11.[6] The significance of the standard adopted under section 1114 is, however, problematic because of the potential influence it will have on courts applying the Code to requests by debtors-in-possession[7] to reject collective bargaining agreements.[8]

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1. H.R. 2969, 100th Cong., 2d Sess., 134 CONG. REC. S6823-24 (daily ed. May 26, 1988) (full text of legislation amending Chapter 11 to address rejection of retiree benefits, as adopted by both chambers of Congress).

2. Retiree Benefits Bankruptcy Protection Act of 1988, Pub. L. No. 100-334, 1988 U.S. CODE CONG. & ADMIN. NEWS (102 Stat.) 610 (to be codified at 11 U.S.C. § 1114).

3. 11 U.S.C. §§ 1101-1174 (1982 & Supp. V 1987).

4. 134 CONG. REC. S6825 (daily ed. May 26, 1988) (statement of Sen. Metzenbaum). LTV Corporation filed a Chapter 11 bankruptcy petition in 1986 and immediately thereafter terminated the health and life insurance benefits of its retirees. *Id.*

5. *Id.*; *see also* 134 CONG. REC. H3488-91 (daily ed. May 23, 1988) (statements made by House members in support of the legislation).

6. 134 CONG. REC. S6825 (daily ed. May 26, 1988) (statement of Sen. Metzenbaum). For a discussion of the standard adopted under section 1114, see *infra* text accompanying note 214.

7. For the purposes of this Note, debtor-in-possession, debtor, and employer are interchangeable.

8. Section 1114 will be discussed in the latter parts of this Note as a means to analyze possible modifications to section 1113.

Congress recognized that under certain circumstances, a Chapter 11 debtor should be able to reject collective bargaining agreements in order to reorganize. Under the present Code, as well as its predecessor,[9] Congress empowers a debtor with the ability to reject these agreements after meeting certain statutory requirements.

The Code permits a debtor who meets the requirements of section 1113[10] to seek rejection of the particular collective-bargaining agreement. While Congress intended section 1113 to establish a clear standard for rejection,[11] the application of section 1113 has, in reality, created not only confusion among the bankruptcy courts but also disharmony between the Second and Third Circuits.[12] This disharmony is troublesome due to the potential confusion that a section 1113 petition creates for the debtor, the union, the creditors, and the courts in their attempt to determine the proper standard for rejection.

This Note will examine the ability of a debtor-in-possession to terminate or reject terms and benefits granted employees in prior collective-bargaining agreements rather than focusing on Congress' recent attempts to protect retirement benefits.[13]

Moreover, this Note will analyze the following questions: (1) what were the standards for rejection employed by the Third Circuit in *Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of America*[14] and by the Second Circuit in *Truck Drivers Local 807 v. Carey Transportation, Inc.*,[15] and how did these two courts come to adopt different standards for rejection?; (2) why does the *Carey Transportation* standard represent a better understanding of the goal of Chapter 11?; and (3) what standard should be adopted, and what modifications are necessary to section 1113 and other sections of the Code in order to gener-

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9. 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. and 28 U.S.C.). This amendment to the Bankruptcy Code of 1978 was a result of the Supreme Court's decision in Northern Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50 (1982), which held that the "adjunct" bankruptcy court system created by Congress was an impermissible encroachment on the judicial power defined by article III of the Constitution. For a further discussion of *Marathon*, see *infra* note 118.

10. 11 U.S.C. § 1113 (Supp. V 1987).

11. Congress passed section 1113 in an attempt to clarify the standard for rejection of collective bargaining agreements. For a discussion of previous attempts to address this problem, see *infra* notes 23-31 and accompanying text.

12. The split between the Second Circuit's opinion in Truck Drivers Local 807 v. Carey Transp., Inc., 816 F.2d 82 (2d Cir. 1987), and the Third Circuit's opinion in Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of Am., 791 F.2d 1074 (3d Cir. 1986), will be a major part of the discussion of rejection of collective bargaining agreements.

13. Section 1114 will be discussed in the latter parts of this Note as a means to analyze possible modifications to section 1113.

14. 791 F.2d 1074 (3d Cir. 1986).

15. 816 F.2d 82 (2d Cir. 1987).

ate a workable and equitable standard for rejection of collective-bargaining agreements? These questions will aid in the discussion of the present status of section 1113 and will attempt to reach a resolution of the problems created by the present language of section 1113. Given the ramifications of rejection of a collective bargaining agreement,[16] the underlying theme of this Note will be to suggest an approach to section 1113 that would reconcile the respective goals of the National Labor Relations Act (NLRA)[17] and Chapter 11 of the Code.[18] Furthermore, to the degree that a standard for rejection can be established under section 1113, this standard may deter courts from blindly applying the well-defined standard adopted under section 1114 when confronted with a petition to reject a collective bargaining agreement under section 1113.

II. THE STANDARDS FOR REJECTIONS APPLIED BY THE SECOND AND THIRD CIRCUITS: TRYING TO DECIDE THE MEANING OF "NECESSARY"[19]

Section 1113 imposes a number of requirements that a debtor must fulfill prior to a court-approved rejection of a collective bargaining agreement.[20] The disharmony among the courts is centered on the interpretation of section 1113(b)(1)(A).[21] Specifically, the courts disagree as to the meaning of the phrase "necessary to permit the reorganization"[22] as it is used in the context of the debtor's request for modification of the terms of an existing agreement. In order to understand the different standards articulated in *Wheeling-Pittsburgh* and *Carey Transportation*, one must first understand the history surrounding the enactment of section 1113.

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16. For a discussion of the damages and claims that result from the rejection of a collective bargaining agreement, see *infra* notes 162-69 and accompanying text.

17. 29 U.S.C. §§ 151-169 (1982). For a discussion of the goals of the NLRA, see *infra* notes 139-41 and accompanying text.

18. 11 U.S.C. §§ 1101-1174 (1982 & Supp. V 1987). For a discussion of the goals of Chapter 11, see *infra* text accompanying note 137.

19. A major concern of this Note is to discuss the meaning of "necessary to permit reorganization of the debtor." 11 U.S.C. § 1113(b)(1)(A) (Supp. V 1987).

20. For a discussion of these requirements, see *infra* note 32.

21. 11 U.S.C. § 1113(b)(1)(A) (Supp. V 1987). A debtor seeking rejection of a collective bargaining agreement must make a proposal to the union which "provides for those necessary modifications in the employees benefits and protections that are necessary to permit the reorganization of the debtor and assures that all creditors, the debtor and all affected parties are treated fairly and equitably." *Id.*

22. *Id.*

III. SECTION 1113

Prior to July 10, 1984,[23] rejection of all executory contracts, including collective bargaining agreements, was governed by section 365(a).[24] Although governed by section 365, the courts were unable to agree upon a unified standard for the rejection of collective bargaining agreements.[25] On February 22, 1984 the Supreme Court decided *NLRB v. Bildisco & Bildisco*,[26] in which the Court attempted to resolve the previous differences between the circuits by creating a uniform standard for rejection. The ruling discussed many aspects of the nature of rejection of collective bargaining agreements under section 365(a),[27] but only two of these areas are of particular importance to the basic issues examined by this Note. First, the Court stated that rejection would be allowed if "the debtor can show that the collective bargaining agreement burdens the estate, and that after careful scrutiny, the equities balance in favor of rejecting the labor contract."[28] Second, the Court allowed the debtor to unilaterally reject the agreement before court approval.[29] *Bildisco* created a loose standard for rejection which was highly criticized by labor supporters.[30] In response to the *Bildisco* decision, Congress enacted section 1113[31] as a separate Code section to be applied when considering the rejection of collective bargaining agreements.

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23. Effective date of section 1113. 11 U.S.C. § 1113 (Supp. V 1987).

24. 11 U.S.C. § 365 (1982 & Supp. V 1987) (standard for rejection of executory contracts under Chapter 11).

25. *Compare* Brotherhood of Railway Airline & S.S. Clerks v. REA Express, Inc., 523 F.2d 164 (2d Cir.) (requiring showing that "rejection of the collective bargaining agreement is necessary to prevent the debtor from going into liquidation"), *cert. denied*, 423 U.S. 1017 (1975) *with In re* Brada Miller Freight Sys., Inc., 702 F.2d 890 (11th Cir. 1983) (arguing that rejection based on a showing of "necessary to prevent liquidation" was too strict and that the court should also consider other factors).

26. 465 U.S. 513 (1984).

27. *Id.* at 526.

28. *Id.*

29. *Id.* at 528. The Supreme Court split 5-4 on this issue and held that a debtor could reject a collective bargaining agreement prior to court approval without committing an unfair labor practice.

30. *See, e.g.*, Rosenberg, *Bankruptcy and Collective Bargaining Agreement—A Brief Lesson in the Use of the Constitutional System of Checks and Balances*, 58 AM. BANKR. L.J. 293 (1984) (providing an overview of the history leading up to enactment of section 1113 as well as commentary on the application of the section). The same day that *Bildisco* was decided, Congressmen Rodino introduced H.R. 4908, which would have created a stricter standard for rejection of collective bargaining agreements by incorporating the "necessary to prevent liquidation" standard adopted in *REA Express*. 130 CONG. REC. H809 (daily ed. February 22, 1984) (statement of Rep. Rodino).

31. For further discussion of congressional reaction to *Bildisco*, see Rosenberg, *supra* note 30; *see also* 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 (1984).

In the period since the enactment of section 1113 in 1984, the courts have uniformly followed the nine requirements for approval of rejection articulated in *In re American Provision Co.*[32] For the purposes of this discussion, however, the focus will center on the three requirements codified under section 1113(c)[33] because they are the most problematic and have been at the center of the controversy.[34] First, the trustee must, prior to the rejection hearing, make a proposal "that [is] necessary to permit the reorganization of the debtor";[35] second, the union must refuse to accept the proposal without good cause; and third, the balance of the equities must clearly favor rejection of the collective bargaining agreement.[36] Although the second and the third elements will be discussed more thoroughly in later sections of this Note,[37] it is important to recognize that these two requirements are easier to fulfill than the first requirement.[38] The need to satisfy these three requirements is not disputed; instead, the problem has

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32. 44 Bankr. 907, 909 (D. Minn. 1984). Essentially, the nine requirements followed by the court were:

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

Id.

33. 11 U.S.C. § 1113(c) (Supp. V 1987).

34. *See, e.g.*, Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of Am., 791 F.2d 1074, 1085 (3d Cir. 1986); Truck Drivers Local 807 v. Carey Transp., Inc., 816 F.2d 82, 88 (2d Cir. 1987).

35. 11 U.S.C. § 1113(b)(1)(A) (Supp. V 1987). This is requirement number three as articulated in *In re* American Provision Co., 44 Bankr. at 909. For a discussion of the nine requirements, see *supra* note 32.

36. 11 U.S.C. § 1113(c) (Supp. V 1987).

37. *See infra* notes 152-71 and accompanying text.

38. *See* Rosenberg, *supra* note 30, at 335.

been in the interpretation of the type of proposal required to fulfill section 1113(b)(1). The language of particular importance has been highlighted by the two questions posed by the Third Circuit in *Wheeling-Pittsburgh*: (1) what is the standard to be applied—for instance, how "necessary" must the proposal be—and (2) what is the object of the necessary inquiry—for instance, to what is the proposal "necessary."[39] A discussion of the other elements of section 1113 will also arise in the context of attempting to answer the questions posed by the *Wheeling-Pittsburgh* court.

Courts have struggled to resolve the meaning of the phrase "necessary to permit reorganization."[40] This phrase encompasses the paramount issue in a discussion of an analysis of section 1113 because it will, for the most part, determine whether a debtor's petition for rejection will be granted.[41] Evidence of the confusion surrounding the meaning of this phrase has surfaced in the different standards put forth by the Second and the Third Circuits in their interpretations of the statutory language. A careful review and analysis of the conflicting opinions are critical in trying to determine what standard, if any, Congress intended to create under section 1113(b)(1)(A).

A. *Wheeling-Pittsburgh Steel Corporation v. United Steelworkers of America*

In 1984, the seventh largest steel maker in the United States, Wheeling-Pittsburgh Steel Corporation, was facing a long-term debt of $527,000,000. The corporation also found that its financial losses between 1982-1984, as well as its need to pay the principal and interest on the debt, weakened its financial position.[42] In an effort to combat continuing losses, the company sought concessions from the union to reduce the average gross labor costs of $25 an hour.[43] In 1982, a new collective bargaining agreement was entered into which reduced labor costs to $18.60 an hour with a gradual restoration of benefits to the previous hourly level.[44] After incremental increases to $21.40 an hour, the union granted Wheeling-Pittsburgh further concessions, amounting to the cancellation of all scheduled wage scale restorations.[45] Deciding

39. Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of Am., 791 F.2d 1074, 1088 (3d Cir. 1986). This court was concerned with the degree of burden a debtor must show to prove that the proposal presented is "necessary to permit reorganization of the debtor." *Id.*

40. *See supra* notes 12, 21.

41. *See infra* notes 146-86 and accompanying text.

42. Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of Am., 791 F.2d 1074, 1076 (3d Cir. 1986).

43. *Id.* at 1076-77.

44. *Id.* at 1077.

45. *Id.*

that additional reductions in labor costs were still needed, the company again asked the union, in January 1985, to grant further concessions in the hopes of preventing financial ruin.[46] The union, however, refused to yield until Wheeling-Pittsburgh gained some concessions from its lenders.[47]

In response to this demand, Wheeling-Pittsburgh presented a restructuring proposal on March 8, 1985 to the union, the company's lenders, and its shareholders.[48] The union, however, adamantly refused to acquiesce if the company agreed to a creditor demand that Wheeling-Pittsburgh pledge its current assets as security for old loans.[49] In turn, the creditors refused to grant the requested moratoriums on debt payments[50] unless Wheeling-Pittsburgh pledged its current assets as security.[51] Faced with this dilemma, the company found that it was unable to accept either the union's or the lenders' counter proposal. Accordingly, Wheeling-Pittsburgh filed a Chapter 11 petition on April 16, 1985.[52]

On May 9, 1985, Wheeling-Pittsburgh presented a new proposal for modification of the existing collective bargaining agreement to the union.[53] The proposal, based on five-year forecasts that were more pessimistic than forecasts accompanying the previous proposal,[54] provided for a five-year term during which the average labor costs were not to exceed $15.20 an hour.[55] When the union refused this proposal, Wheeling-Pittsburgh filed for rejection of the collective bargaining agreement under section 1113.[56] The rejection was granted by the bankruptcy court on July 17, 1985.[57] Thereafter, the company imposed a $17.50 an hour[58] labor cost which, in turn, triggered a strike on July 21, 1985.[59]

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46. *Id.*

47. *Id.*

48. *Id.*

49. *Id.*

50. *Id.* (company wanted 100% moratorium on principal payments for 1985-1986 from all lenders and an additional moratorium of 50% from some of its lenders for 1987-1989).

51. *Id.* Pledging its assets would give the lenders collateral to secure the outstanding debt but would effectively dissolve the claims of the unsecured creditors—for instance, the union—if liquidation were to occur.

52. *Id.* at 1077.

53. *Id.*

54. *Id.* at 1078.

55. *Id.* at 1077.

56. *Id.* at 1078.

57. *In re* Wheeling-Pittsburgh Steel Corp., 50 Bankr. 969 (W.D. Pa. 1985), *rev'd sub nom.* Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of Am., 791 F.2d 1074 (3d Cir. 1986).

58. 791 F.2d at 1078.

59. *Id.*

The strike was settled by a new agreement on October 15, 1985.[60] As part of the agreement, if the union was successful in reversing the bankruptcy court's decision to allow rejection of the previous collective bargaining agreement, it could assert claims for those who worked during the strike.[61]

On appeal, the Third Circuit was confronted with the question of whether Wheeling-Pittsburgh had satisfied the requirements for rejection under section 1113. Specifically, the union argued that the proposal failed to provide for those modifications "necessary to permit reorganization."[62] Although the court rejected the union's initial argument that Wheeling-Pittsburgh "could have adhered to the agreement for its remaining [thirteen] months and still have had sufficient cash to operate for both the short and long term,"[63] the court's analysis of this issue was significant because of its interpretation of the standard for rejection created by section 1113. Recognizing the absence of committee reports concerning section 1113, the Third Circuit chose to rely instead on "the sequence of events leading to adoption" of that section and selected "statements on the House and Senate floor of the legislators most involved in its drafting."[64] Believing section 1113(b)(1)(A) was a "victory for labor,"[65] the Third Circuit chose to rely on the statements of Senator Thurmond who "explained that the Senate conferees had been required to accept a bankruptcy bill, if there was to be one at all, that contained 'a labor provision acceptable to organized labor', and that the provision was one whose 'procedures *and standard* are essentially the same as those of the Packwood amendment.' "[66] The Third Circuit, however, failed to recognize that Senator Thurmond would have opposed the amendment if he had been given the choice.[67]

Presuming that Congress' intent was to wholly adopt the Packwood amendment[68] in the construction of section 1113(b)(1)(A),

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60. *Id.*

61. *Id.*

62. *Id.* at 1086.

63. *Id.* at 1085.

64. *Id.* at 1086.

65. *Id.* (quoting 130 CONG. REC. S8888 (daily ed. June 29, 1984) (statement of Sen. Thurmond)).

66. *Id.* at 1087 (quoting 130 CONG. REC. S8888 (daily ed. June 29, 1984) (statement of Sen. Thurmond) (emphasis in original)).

67. Senator Thurmond was opposed to the labor provision but felt obligated to support the conferees' report in order to solve the problems created by the Supreme Court's decision in Northern Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50 (1982). *See* 130 CONG. REC. S8888 (daily ed. June 29, 1984) (statement by Sen. Thurmond) ("[W]ere it not for the critical need to pass this bankruptcy bill I could not have agreed to these [labor] provisions . . . ."). For discussions of *Marathon*, see *infra* note 118.

68. Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of Am., 791 F.2d 1074, 1087 (3d Cir. 1986). The Packwood amendment created a standard that allowed rejection

the court argued that the term "necessary" must be construed strictly.[69] In distinguishing between the short-term concern of the union and the long-term concern of the corporation, the court stated:

> [w]hile we do not suggest that the general long-term viability of the Company is not a goal of the debtor's reorganization, it appears from the legislators' remarks that they placed the emphasis in determining whether and what modifications should be made to a negotiated collective bargaining agreement on the somewhat shorter term goal of preventing the debtor's liquidation, the mirror image of what is "necessary to permit the reorganization of the debtor."[70]

The union then advanced three other arguments which the Third Circuit found persuasive, the most important of which was the absence of a "snap-back" provision in the Wheeling-Pittsburgh proposal of May 5, 1985.[71] The absence of such a provision was extremely troublesome and proved to be the major reason why the Third Circuit found that the proposal was not "necessary to permit the reorganization."[72]

Clearly, then, the opinion of the *Wheeling-Pittsburgh* court was that a section 1113(b)(1)(A) proposal must pass a very strict standard of review. The court viewed section 1113 as a complete dismissal of the *Bildisco* standard[73] and a clear victory for labor.[74] With this in mind, the Third Circuit chose to equate "necessary" with the meaning of "essential" as laid out in section 1113(e).[75] In rejecting the debtor's petition, the court relied on the belief that section 1113 was an adoption of the Packwood standard for rejection.[76] Therefore, the benchmark embraced by the court was that " 'necessity' be construed strictly to sig-

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if the debtor's proposal contained "minimum modifications in such employees' benefits and protections that would permit the reorganization." 130 CONG. REC. S6181-82 (daily ed. May 22, 1984) (statement of Sen. Packwood) (Sen. Packwood's amendment was to H.R. 5174, 98th Cong., 2d Sess., 130 CONG. REC. 1807-43 (1984)).

69. *Wheeling-Pittsburgh*, 791 F.2d at 1088.

70. *Id.* at 1089.

71. *Id.* The argument made by the union was that the proposal did not contain only "necessary" modifications because the proposal: (1) called for a five-year agreement with severely reduced labor costs; (2) was based on the " 'worst-case' scenario"; and (3) "failed to contain a 'snap-back' provision." *Id.* A "snap-back" provision gives the employee the right to increased wages and benefits and is triggered by the occurrence of a particular condition, usually profitability.

72. *Id.* The Third Circuit criticized the bankruptcy court's failure to address the absence of the "snap-back" provision in the debtor's proposal. *Id.*

73. For a discussion of *Bildisco*, see *supra* notes 26-31 and accompanying text.

74. *Wheeling-Pittsburgh*, 791 F.2d at 1087.

75. *See id.* at 1088 (rejecting as "hypertechnical" the argument that "essential" and "necessary" are different). For further discussion of this issue, see *infra* notes 183-86 and accompanying text.

76. *See supra* note 68.

nify only modifications that the trustee is constrained to accept because they are directly related to the Company's financial condition and its reorganization."[77]

The period following the Third Circuit's decision in *Wheeling-Pittsburgh* has been witness to a mixed reaction to the court's interpretation of section 1113(b)(1)(A). There have been essentially three types of responses by the bankruptcy courts. The first has been an adherence to the *Wheeling-Pittsburgh* standard and a belief that the Third Circuit effectively disposed of the conflict among the bankruptcy courts.[78] The second type of response illustrates that the confusion existing before the *Wheeling-Pittsburgh* decision still remains.[79] The last type of response has been a complete rejection of the Third Circuit standard, as exemplified by the Second Circuit's opinion in *Truck Drivers Local 807 v. Carey Transportation, Inc.*[80]

B. Truck Drivers Local 807 v. Carey Transportation, Inc.

Carey Transportation, Inc. operated a bus company between New York City and the two New York international airports.[81] Local 807 was the labor representative of Carey's bus drivers and station employees.[82] On August 20, 1982,[83] the parties entered into collective bargaining agreements covering both sets of employees that were to run until February 28, 1986.[84] In 1981, Carey began experiencing financial losses

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77. *Wheeling-Pittsburgh*, 791 F.2d at 1088. The court viewed the "necessity" requirement as an adoption of the standard for rejection announced in Brotherhood of Airline & S.S. Clerks v. REA Express, Inc., 523 F.2d 164 (2d Cir.), *cert. denied*, 423 U.S. 1017 (1975). REPORT OF SUBCOMMITTEE OF COMMITTEE ON BANKRUPTCY AND CORPORATE REORGANIZATION, ASSOCIATION OF THE BAR OF THE CITY OF NEW YORK, TREATMENT OF COLLECTIVE BARGAINING AGREEMENTS UNDER SECTION 1113 OF THE BANKRUPTCY CODE (Dec. 18, 1986) [hereinafter REPORT ON BANKRUPTCY AND REORGANIZATION]. For discussion of the *REA Express* standard, see *supra* note 25.

78. *See, e.g., In re* William P. Brogna and Co., 64 Bankr. 390, 393 (E.D. Pa. 1986) (finding the absence of a "snap-back" provision to be detrimental, despite the fact debtor proposed to pay all creditors 100% within three years of confirmation).

79. *See In re* Walway Co., 69 Bankr. 967, 973 (E.D. Mich. 1987) (citing *In re* Valley Kitchens, Inc., 52 Bankr. 493 (S.D. Ohio 1986)). This court believed it was following the Third Circuit standard when it stated that " 'necessary' means a modification that will result in a greater probability of successful reorganization than if the contract were allowed to continue in force." *Id.* Despite the court's opinion, this is much different than the Third Circuit's standard in *Wheeling-Pittsburgh*. *See Wheeling-Pittsburgh*, 791 F.2d at 1088 (rejecting a standard based on the likelihood of successful reorganization).

80. 816 F.2d 82, 89 (2d Cir. 1987) ("In making the decision whether to permit the debtor to reject its bargaining agreement . . . the court must consider whether rejection would increase the likelihood of successful reorganization.").

81. *Id.* at 85.

82. *Id.*

83. *Id.* The agreements settled a 64-day strike by the union.

84. *Id.*

which continually increased throughout the period of this agreement.[85] A total of forty-eight employees were dismissed in 1983 and 1984, resulting in an estimated cost savings to Carey of $1,144,000.[86] Faced with the continuing need to cut costs, in June 1984 Local 807 agreed to minor modifications in the bargaining agreements applicable to drivers hired after September 1984.[87] These concessions yielded savings of $100,000.[88] Unable to prevent continuing losses, on January 31, 1985, Carey sought further concessions that were projected to save the company $750,000 annually.[89] Management then added further modifications on March 27, 1985, consisting of an extension of the expiration date of the contract for an additional two years through February 1988 and a wage and benefit freeze until April 1, 1987.[90] Furthermore, Carey would agree only to reopen bargaining concerning wages and benefits after April 1, 1987 for the final year of the extended contract.[91] In response, the union asked that the parties submit to binding arbitration if they failed to agree upon terms for the final year of the contract; Carey refused this proposal.[92] Subsequently, the entire Carey package was rejected by Local 807 on March 29, 1985.[93]

Carey filed a Chapter 11 petition on April 4, 1985 and on the next day, presented the union with a proposal to modify the collective bargaining agreement pursuant to section 1113.[94] The company asked the union to make seven concessions which, if agreed to, would have yielded an annual savings of $1,800,000 for each of the next three years.[95] Although Carey projected losses for 1986 at only $746,000,[96] the company argued that it needed larger cost reductions than required to cover the estimated losses in order to improve its long-term financial health.[97] The company told the union that without the proposed savings it would be unable to propose a feasible plan for reor-

85. *Id.*

86. *Id.* Although Carey terminated 50 employees in September 1983, 10 were subsequently rehired at the direction of an arbitrator. Union concessions resulted in the layoff of an additional eight employees in 1984 and 1985.

87. *Id.*

88. *Id.*

89. *Id.*

90. *Id.*

91. *Id.*

92. *Id.*

93. *Id.* at 85-86. Union members were "particularly adamant" about rejecting the two year contract extension and the wage and benefits freeze. *Id.*

94. *Id.*

95. *Id.*

96. *Id.*

97. *Id.* Carey believed that further savings would allow it to expand its bus fleets, operations, and maintenance facilities and thereby attempt to expand its market share. *Id.*

ganization.[98] Three days into the section 1113 hearing, Local 807 proposed its own terms.[99] The union's proposal would have produced savings of $776,000 and extended the expiration date of the contract by fifteen months.[100] It would have also frozen wages and benefits subject to a "reopener" with binding arbitration.[101] Finding Local 807's proposal "unacceptable,"[102] Carey left the fate of the agreement to the bankruptcy court.[103]

On appeal to the Second Circuit,[104] Local 807 presented three arguments: (1) the Carey proposal sought more than break-even cost reductions; (2) the proposed three year extension of the union contract was too long in relation to the eight months remaining under the existing contract; and (3) the company's proposal lacked a "snap-back" provision.[105] In reviewing the bankruptcy court's decision to allow rejection of the collective bargaining agreement, the Second Circuit refused to follow the Third Circuit's interpretation of the word "necessary" in section 1113(b)(1)(A). Setting the tone of the ruling early in the opinion, the court stated that the "legislative history strongly suggests that 'necessary' should not be equated with 'essential' or bare minimum."[106] The court also found that section 1113(b)(1)(A) was not a codification of Senator Packwood's proposal, but rather that Congress settled on a "substitute for this clause."[107] Lastly, the court stated that equating "necessary" with bare minimum would "make it virtually impossible for the debtor to meet its other statutory obligations."[108]

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98. *Id.*

99. *Id.*

100. *Id.*

101. *Id.*

102. *Id.*

103. *Id.* at 86-87. The bankruptcy court granted the motion for rejection on July 17, 1985. The court adopted, with certain modifications, the nine-step analysis of section 1113 used in *In re* American Provision Co., 44 Bankr. 907 (D. Minn. 1984), and found that Carey had met its burden of proving compliance with the procedural and substantive standards of section 1113. *Carey Transp.*, 816 F.2d at 86-87.

104. *Id.* The United States District Court for the Southern District of New York affirmed the bankruptcy court's decision. Local 807 appealed to the Second Circuit on September 12, 1986. *Id.*

105. *Id.* at 89. The union based its arguments on those which had been successful in *Wheeling-Pittsburgh. See supra* note 71 and accompanying text; Wheeling-Pittsburgh Steel Corp. v. United States Workers of Am., 791 F.2d 1074, 1088-90 (3d Cir. 1986).

106. *Carey Transp.*, 816 F.2d at 89.

107. *Id.* (quoting *Wheeling-Pittsburgh*, 791 F.2d at 1087).

108. *Id.* "Because the statute requires the debtor to negotiate in good faith over the proposed modifications, an employer who initially proposed minimal changes would have no room for good faith negotiating, while one who agreed to any substantive changes would be unable to prove that its initial proposals were minimal." *Id.* (quoting *In re* Allied Delivery Systems Co., 49 Bankr. 700, 702 (N.D. Ohio 1985)).

In deciding the meaning of "necessary to permit reorganization," *Carey Transportation* re-examined the question posed by the Third Circuit in *Wheeling-Pittsburgh*: "[T]o what must those alterations be necessary?"[109] The Second Circuit responded by stating that, "in making the decision whether to permit the debtor to reject its bargaining agreement . . . the court must consider whether rejection would increase the likelihood of successful reorganization."[110] The court found that, "it becomes impossible to weigh necessity as to reorganization without looking into the debtor's ultimate future and estimating what the debtor needs to attain financial health."[111] The court interpreted the "necessity" requirement as placing the burden on the debtor to present a proposal for modifications that while not absolutely essential, "will [instead] enable the debtor to complete the reorganization process successfully."[112] In doing so, the Second Circuit adopted a looser reading of the word "necessary," as opposed to the strict construction adopted by the Third Circuit.

Both the *Wheeling-Pittsburgh* and *Carey Transportation* courts purport to base their decisions on the legislative history surrounding section 1113(b)(1)(A).[113] In reality, neither decision reflects a complete and thorough reading of the history surrounding the enactment of section 1113. The absence of a committee report accompanying the bill has caused the courts to rely on statements made from the floor,[114] while failing to recognize other events that led to the adoption of the present language of section 1113. The absence of a committee report has allowed the courts to choose the standard they wish to apply first and then look to the Congressional Record for statements that support the chosen interpretation.

C. *An Alternative Interpretation of the Legislative History of Section 1113*

Although the Second and Third Circuits have gleaned two different standards from the meaning of "necessary," there may be a third

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109. *Id.* at 88 (citing *Wheeling-Pittsburgh*, 791 F.2d at 1088).

110. *Carey Transp.*, 816 F.2d at 89. (quoting *In re* Royal Composing Room, Inc., 62 Bankr. 403, 417 (S.D.N.Y. 1986), *aff'd*, 848 F.2d 345 (2d Cir. 1988)).

111. *Id.*

112. *Id.* at 90.

113. In fact, the Third Circuit argued that section 1113(b)(1)(A) is a clear adoption of the Packwood amendment. *See supra* note 68 and accompanying text.

114. Garcia v. United States, 469 U.S. 70, 76-78 (1984) (Committee Reports "more authoritative" than comments from the floor) (quoting United States v. O'Brien, 391 U.S. 367, 385 (1968)). It is clear from this opinion that courts should avoid relying upon statements from the floor because of their questionable accuracy. *Id.* at n.3 (citing Schwegmann Bros. v. Calvert Distillers Corp., 341 U.S. 384, 395-96 (1951) (Jackson, J., concurring)).

interpretation. The next part of this Note will attempt to present a third interpretation which more accurately reflects the history of section 1113, as well as encompasses the function and purpose of reorganization.[115]

Clearly, the enactment of section 1113 was a direct response to the Supreme Court's decision in *Bildisco*.[116] Of equal concern was the fact that, as a result of *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*,[117] Congress was faced with the knowledge that the bankruptcy courts were operating under an interim rule which was to expire on March 31, 1984.[118] These pressures were the key reasons for the swift enactment of section 1113.[119]

When the Conferees emerged with the House Conference Report,[120] many viewed the collective bargaining provision as a victory for labor. At the very least, the fact that Congress eventually enacted a separate Code section[121] to deal with the rejection of collective bargaining agreements reveals a recognition of this triumph. Although there is no question that section 1113 represented a victory for labor, the more pertinent inquiry concerns the size of this victory. A major reason for the present form of section 1113 is the fact that the labor lobby was able to muster enough control to limit the debate in the House and to permit only one amendment to H.R. 5174, the bill proposed by Congressman Rodino.[122] This "ensured that the labor language could only

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115. Bendixsen, *Enforcing the Duty to Arbitrate Claims Under a Collective Bargaining Agreement Rejected in Bankruptcy: Preserving the Parties' Bargain and the National Labor Relations Policy*, 8 INDUS. REL. L.J. 401, 437 (1986); M. BIENENSTOCK, BANKRUPTCY REORGANIZATION 5 (1987) (providing a general discussion of the primary goals of Chapter 11).

116. Rosenberg, *supra* note 30.

117. 458 U.S. 50 (1982).

118. Rosenberg, *supra* note 30, at 310. In 1982, the Supreme Court held that the jurisdictional grant of the bankruptcy courts was unconstitutional, because the bankruptcy judges were exercising article III powers but were not article III judges. *Marathon*, 458 U.S. at 88. In the aftermath of *Marathon*, the bankruptcy courts were operating under an interim rule which was to expire on March 31, 1984 and was creating great pressures on Congress to enact revisions to rectify the jurisdictional deficiency. *See* Rosenberg, *supra* note 30, at 310.

119. *See* Rosenberg, *supra* note 30, at 315-21 (describing the events leading to the passage of section 1113 and the pressures facing Congress in light of the fact that the bankruptcy courts were operating under an emergency jurisdictional rule).

120. H.R. CONF. REP. No. 882, 98th Cong., 2d Sess. (1984), 130 CONG. REC. H7471 (daily ed. June 29, 1984) (report did not contain a joint explanatory statement).

121. Prior to enactment of section 1113, rejection of collective bargaining agreements was covered under 11 U.S.C. § 365 (1982 & Supp. V 1987) (rejection of executory contracts).

122. Rosenberg, *supra* note 30, at 315 (supporters of labor on the House Rules Committee were able to ensure that there could be only one amendment to the Rodino bill). On March 19, 1984, Congressman Rodino introduced H.R. 5174 which limited rejection to proposals that were deemed necessary for successful financial reorganization and pres-

be voted upon as part of the entire package."[123] This "package" included the pressing issue of the jurisdictional problems remaining in the bankruptcy court system. Therefore, the pressures created by the jurisdictional issue coupled with the limited debate was a major reason for the version of the bill that was passed by the House. The Senate, however, did not adopt H.R. 5174 in the form in which it had passed through the House. Subsequently, Congress agreed to three more extensions of the expiration date of the interim rule until June 20, 1984.[124]

Most of the debate that occurred between March and June of that year was between the Packwood pro-labor and the Thurmond pro-debtor amendments.[125] On June 19, the Senate passed the Packwood amendment without any mention of the collective bargaining issue and left the decision to the House-Senate Conference Committee. After passing two emergency extensions, the Committee finally emerged with a compromise which both Houses eventually approved.[126]

Although there are many statements in the record which can be construed as support for either the Third or the Second Circuit opinions, the fact is that Congress was looking for a "compromise so that they would not be viewed as casting a vote for or against anyone . . . ."[127] One commentator noted that:

> [n]either the labor proponents nor any of the dozen other interest groups had sufficient power to enact its proposal as a separate piece of legislation, yet many were strong enough individually or collectively to block passage of bankruptcy legislation, which was essential because all enabling authority of judges was due to terminate June 27, 1984.[128]

Clearly, the pressures felt by Congress as a result of the *Bildisco* and *Marathon* decisions demonstrated themselves in the language of section 1113.

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ervation of the jobs covered under the agreement. 130 CONG. REC. H1727 (daily ed. March 19, 1984) (statement of Rep. Rodino).

123. Rosenberg, *supra* note 30, at 315.

124. *Id.* at 315-18.

125. For a discussion of the Packwood amendment, see *supra* note 68. The Thurmond amendment would have "preserve[d] the balancing of the equities standard for rejection of [collective bargaining agreements]." 130 CONG. REC. S6082 (daily ed. May 21, 1984) (statement of Sen. Thurmond).

126. Rosenberg, *supra* note 30, at 318. The House passed the Conferees' compromise on June 29, 1984. 130 CONG. REC. H7499 (daily ed. June 29, 1984). The Senate passed the Conferees' compromise on June 29, 1984. 130 CONG. REC. S8887 (daily ed. June 29, 1984).

127. Rosenberg, *supra* note 30, at 318.

128. Merrick, *The Bankruptcy Dynamics of Collective Bargaining Agreements*, 91 COMM. L.J. 169, 179 n.38 (Summer 1986). Senator Thurmond stated that he would not have voted in favor of the bill if an emergency had not existed. *See supra* note 67.

What, then, is the standard created by section 1113? Although the standard has elements of both the Second and Third Circuit opinions, both courts have interpreted the legislative intent incorrectly. Neither branch of Congress was able to adopt language exclusively favoring either the Packwood or the Thurmond view of "necessary." As a result, section 1113 was left to the Conferees. The Conferees, in turn, were unwilling to shoulder the decision[129] and, therefore, crafted language somewhere in between the two major interests. While a compromise between the competing interests apparently resulted, the present ambiguities in the language of section 1113 has left the courts, debtors, and creditors without a clear standard for rejection.[130] The outcome is that section 1113 is a codification of Congress' intent to avoid voting against either labor or management. Faced with the need to pass the Bankruptcy Judgeship Act, but squeezed by those who refused to pass such an act without a labor provision amending the Code, members of both houses of Congress reluctantly accepted the language in section 1113(b)(1)(A).[131]

The pendulum did not swing back in favor of labor;[132] instead, "the Senate and House Conferees made the point clear that the road to resolution of the conflict between labor and bankruptcy law lies in honest compromise."[133] In light of this statement, it is more accurate to view section 1113 as a codification of the congressional intent that the parties seek resolution through compromise and collective bargaining.[134] Neither labor nor the debtor clearly prevailed through the enactment of section 1113. The "necessary" language in section 1113(b)(1) is an adoption of a standard somewhere between the long and short term. This compromise has given rise to the difficulty the courts have experienced in applying section 1113. If, however, this section is viewed as a means for promoting private collective bargaining, it does provide a basis for a restructuring of section 1113 to meet the equitable standard for rejection of collective bargaining agreements. In the following parts of this Note, the goal will be to propose an approach to section 1113 that will reconcile the conflict between labor policies and reorganization policies, while reaffirming Congress' desire to promote collective bargaining between the debtor and its employees.

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129. *See* Rosenberg, *supra* note 30, at 318 (Conferees did not want to be viewed as casting a vote against either side).

130. *See supra* note 12.

131. Merrick, *supra* note 128, at 178 n.40.

132. Century Brass Prods. Inc. v. International Union, 795 F.2d 265, 276 (2d Cir.) (explicitly rejecting the statement in *Wheeling-Pittsburgh* that Congress swung the pendulum back in favor of labor as a reaction to the *Bildisco* decision), *cert. denied,* 479 U.S. 949 (1986).

133. *Id.* at 276.

134. *See infra* note 144 and accompanying text.

IV. What Standard Should Section 1113 Create for Rejection of Collective Bargaining Agreements?

In attempting to establish the standard to be employed by the courts in considering a motion for rejection of a labor contract, it is important to recognize the competing interests involved in the process. The concerns underlying the enactment of section 1113 derive from the competing goals of reorganization—Chapter 11[135]—and the National Labor Relations Act.[136]

Chapter 11 has two objectives: (1) to rehabilitate the debtor, and (2) to confirm a plan that will provide for the greatest return on creditors' claims.[137] The debtor seeking rejection of a collective bargaining agreement is, in effect, saying that the present labor costs are preclusive of the goals of reorganization under Chapter 11. Labor tends to be the cost factor over which the debtor has the most control.[138] Therefore, the potential ability to reduce labor costs is frequently a dispositive factor of whether the debtor will be able to reorganize successfully.

The goal of section 8(d) of the National Labor Relations Act (NLRA) is to establish the duty of employers and employees to bargain collectively and to prevent termination or modification of agreements entered into as a result of collective bargaining.[139] In effect, section 8(d) seeks to protect an employee under a collective bargaining agreement from the "unfair labor practices" of the employer.[140] The courts consistently have recognized that Congress has granted collective bargaining agreements a special status that executory contracts do not normally possess.[141]

In light of these two competing interests, section 1113 is an attempt to reconcile the concerns of labor and the debtor. It is clear that the ability to reject a labor contract should not become a "medicine [of management] to rid [itself] of corporate indigestion."[142] Yet, management's need to reduce labor costs is a primary concern of the reorganization process under Chapter 11.

> [Thus,] if the protections of the Labor Act are held to be su-

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135. 11 U.S.C. §§ 1101-1174 (1982 & Supp. V 1987).

136. 29 U.S.C. §§ 151-169 (1982 & Supp. V 1987).

137. Bendixsen, *supra* note 115, at 437.

138. Merrick, *supra* note 128, at 170.

139. 29 U.S.C. § 158(d) (1982).

140. *Id.* §§ 158, 160.

141. *See, e.g.*, International Bhd. of Teamsters v. IML Freight, Inc., 789 F.2d 1460, 1462 (10th Cir. 1986). The "special nature of labor contracts is rooted in the national policy which favors collective bargaining in employment and . . . Congress has strongly cautioned the bankruptcy courts to be considerate of that policy." *Id.*

142. Century Brass Prods., Inc. v. International Union, 795 F.2d 265, 272 (2d Cir.), *cert. denied*, 479 U.S. 949 (1986).

> preme even when a debtor is suffering extremely heavy financial losses due to a rigid and inefficient collective bargaining agreement, the result may be the unnecessary destruction of the firm, and the workers' jobs, contrary to the rehabilitative policy of the Bankruptcy Code.[143]

The Conferees may have been unable to agree on the extent of the burden that a debtor faces in making a modification proposal under section 1113(b)(1)(A), but they were able to agree that the major purpose of section 1113 is to encourage the parties to solve their dispute through private collective bargaining.[144]

Throughout section 1113, the underlying intent is to combine, in a "workable manner,"[145] the reorganization goals of Chapter 11 with the protection of labor under section 8(d). Recognition of this intent reaffirms the point that the most important feature of section 1113 should be the desire to promote negotiation and compromise. In determining the best standard for the rejection of collective bargaining agreements, the first task is to assure that the standard will promote compromise and represent a reconciliation of the policies of the NLRA and Chapter 11.

Application of section 1113 in a "workable manner" may be initiated in two ways. The first approach would be through amendments to the language of section 1113. The feasibility of such an approach is dubious, however, given the continuing existence of many of the political forces that affected the original drafting of the section. The conflicts between the labor interests and the interests of the debtor remain an obstacle to congressional consensus. Therefore, it is unlikely that such an approach would be successful. The second and more feasible approach is to have the courts initiate the establishment of a clear standard through judicial application of section 1113. This would require the courts to recognize that inherent in a workable standard is the establishment of a uniform rejection standard which reconciles the underlying goals of Chapter 11 and the NLRA.

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143. Gibson, *supra* note 31, at 326.

144. *See, e.g.*, 130 CONG. REC. S8888 (1984) (statement of Sen. Thurmond) ("I would hope that the courts interpret both provisions in the most practical and workable manner."); *id.* at S8898 (statement of Sen. Kennedy) ("The conference agreement . . . substitute[s] a rule of law that encourages the parties to solve their mutual problems through the collective bargaining process."). The contrast here is between private collective bargaining and court involvement through arbitration or rejection of the agreement.

145. *Id.* at S8888 (statement of Sen. Thurmond).

V. Looking for the Meaning of "Necessary": An Inquiry into the Other Requirement of Section 1113

The discussion, thus far, has concentrated on the meaning of the term "necessary" as it is used in section 1113(b)(1)(A). Although the courts generally accept the concept that section 1113 establishes nine requirements for rejection of collective bargaining agreements,[146] a debtor able to satisfy the court that it has presented a "necessary" proposal to "permit reorganization" will usually be granted a rejection.[147] Nevertheless, this does not render the other requirements useless. In fact, these additional requirements aid in the inquiry as to the necessity of the debtor's proposal to reorganization. The most important of these nine requirements are:[148] 1) the union "has refused to accept such proposal without good cause,"[149] 2) the "balance of the equities clearly favors rejection,"[150] and 3) "all of the affected parties are treated fairly and equitably."[151]

The "without good cause" requirement's only real purpose may be to prevent the union from stonewalling[152] and "to ensure that a continuing process of good faith negotiations will take place before court involvement."[153] While this may be a "long-winded way of saying that this provision means nothing at all,"[154] a more optimistic view is that it is another indication of Congress' desire to foster negotiation and compromise, and reduce the need for court involvement. If the union recognizes that it may not reject a proposal "without good cause," it will have an incentive to seek a compromise with the debtor to prevent complete rejection of the collective bargaining agreement by the court.[155] On the other hand, the union is still protected from bad faith

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146. *In re* American Provision Co., 44 Bankr. 907, 909 (D. Minn. 1984). For a discussion of the nine requirements followed by the court in the rejection hearing, see *supra* note 32.

147. *See In re* Walaway Co., 69 Bankr. 967, 973-74 (E.D. Mich. 1987) ("good cause" and "equity" are related to the "necessity" requirement).

148. *See id.* at 974 n.16.

149. 11 U.S.C. § 1113(c)(2) (Supp. V 1987). This is requirement eight of the nine steps required for rejection. *See supra* note 32.

150. 11 U.S.C. § 1113(c)(3) (Supp. V 1987). This is requirement number nine of the nine steps required for rejection. *See supra* note 32.

151. 11 U.S.C. § 1113(b)(1)(A) (Supp. V 1987). This is requirement number four of the nine steps required for rejection. *See supra* note 32.

152. *See* Truck Drivers Local 807 v. Carey Transp., Inc., 816 F.2d 82, 92 (2d Cir. 1987) (stonewalling "is unacceptable and inconsistent with Congressional intent") (citing *In re* Royal Composing Room, Inc., 62 Bankr. 403, 407 (S.D.N.Y. 1986), *aff'd*, 848 F.2d 345 (2d Cir. 1988)). *But see* Gibson, *supra* note 31, at 341 (suggesting stonewalling may be permissible).

153. 130 Cong. Rec. S8898 (daily ed. June 29, 1984) (statement of Rep. Morrison).

154. Gibson, *supra* note 31, at 340-41.

155. Clearly, the union wants to avoid rejection given the Code limitations on pre-

proposals by the employer since the employer maintains the burden of proving the necessity of the proposal.[156] As one court suggested, a court "must review the union's rejection utilizing an objective standard which narrowly construes the phrase 'without good cause' in light of the main purpose of Chapter 11, namely reorganization of financially distressed businesses."[157]

The "balancing of the equities" requirement is viewed as a codification of the holding in the first part of *Bildisco*.[158] The use of "clearly" indicates that Congress favored rejection only when "the equities balanced decidedly in favor of rejection."[159] The analysis of this requirement in *In re Carey Transportation*[160] outlined two elements of concern. The first element concentrated on "whether the policy [and success] of reorganization will be furthered by the rejection of the collective bargaining agreement."[161] The second one examined "how damage claims resulting from rejection would be treated under section 502(c)."[162]

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and post-petition claims in relation to employment contracts. For a discussion of the claims arising from rejection, see *infra* notes 162-71 and accompanying text.

156. *See* 130 CONG. REC. S8898 (daily ed. June 29, 1984) (statement of Sen. Packwood) ("The 'without good cause' language provides an incentive or pressure on the debtor to negotiate in good faith."). Senator Packwood felt that there would be an incentive for the debtor to present a good faith proposal which, by the terms of the statute, the union would be unable to reject. The burden is on the debtor to satisfy the nine requirements by a preponderance of the evidence. However, once the debtor has established prima facie compliance, the burden shifts to the union to produce evidence contradicting one or more of the nine requirements. *In re* Salt Creek Freightways, 47 Bankr. 835, 838 (D. Wyo. 1985). For a listing of the nine requirements for rejection, see *supra* note 32.

157. *Salt Creek*, 47 Bankr. at 840.

158. Truck Drivers Local 807 v. Carey Transp., Inc., 816 F.2d 82, 92 (2d Cir. 1987) (citing Century Brass Prods., Inc., v. International Union, 795 F.2d 265, 273 (2d Cir.), *cert. denied*, 479 U.S. 949 (1986)). The court "must focus on the ultimate goal of Chapter 11" and thus balance the equities as they "relate to the success of reorganization." NLRB v. Bildisco & Bildisco, 465 U.S. 513, 527 (1984).

159. *Salt Creek*, 47 Bankr. at 841 (citing 130 CONG. REC. S8898 (daily ed. June 29, 1984) (statement of Sen. Packwood)).

160. 50 Bankr. 203, 212-13 (S.D.N.Y. 1985), *aff'd sub nom.* Truck Drivers Local 807 v. Carey Transp., Inc., 816 F.2d 82 (2d Cir. 1987) (citing *In re* Salt Creek Freightways, 47 Bankr. 835 (D. Wyo. 1985)). A third element, whether the union asserted that the debtor filed solely to disencumber itself from the collective bargaining agreement, was rejected as more appropriate for discussion under 11 U.S.C. § 1112(b) (1982) ("Conversion or Dismissal"). 50 Bankr. at 212-13.

161. 50 Bankr. at 212 (quoting *Salt Creek*, 47 Bankr. at 841).

162. *Id.* Under 11 U.S.C. § 502(c):

> [t]here shall be estimated for the purpose of allowance under this section (1) any contingent [a claim contingent on the happening of an event] of unliquidated [undisputed] claim, the fixing or liquidation of which, as the case may be, would unduly delay the administration of the case; or (2) any right to payment arising from a right to an equitable remedy for breach of performance.

Damages resulting from rejection must be determined because, in "balancing the equities," the court must be aware of the effect that rejection will have on the employees. Under section 507(a)(3), a claim for services rendered prior to the filing for protection under the Code will constitute a third priority unsecured claim but only for those amounts earned ninety days prior to filing and limited to two thousand dollars.[163] Priority claims are entitled to deferred cash payments if the class of creditors has accepted the confirmation plan[164] or cash payments on the effective date of the plan if the class has not accepted the plan.[165] Any pre-petition claim beyond the two thousand dollar maximum is an unsecured claim and therefore is not likely to be recouped.[166] Claims arising for services rendered post-petition are unsecured first priority administrative claims,[167] which must be paid under the reorganization plan.[168] Finally, the entire claim for damages arising out of the termination of an employment contract is limited to the amount reserved under the contract for the year following the earlier of the date of filing or the date of termination plus any unpaid compensation due under such contracts.[169]

Therefore, the rejection of a labor agreement should only be granted if the "balance of the equities" favors such a decision. The equities would clearly weigh against rejection if a large amount of the claim was unsecured[170] or disallowed.[171]

In light of these two elements, "balancing the equities" seems to be connected to the "necessity" requirement. In concentrating on the goal of successful reorganization, the first element is concerned with the impact of rejection on the rehabilitation of the debtor. Rehabilitation, as opposed to the short-term goal of preventing liquidation, is the first and foremost policy objective of reorganization. The second element, the concern over the determination of damages, is a feature of

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163. 11 U.S.C. § 507(a)(3) (1982 & Supp. V 1987).

164. 11 U.S.C. § 1129(a)(9)(B)(i) (1982).

165. 11 U.S.C. § 1129(a)(9)(B)(ii) (1982).

166. An unsecured claim is to be distinguished from a claim which is secured by a lien on property—a secured claim. *See* 11 U.S.C. § 506(a) (1982). Furthermore, an unsecured claim must be distinguished from a priority (unsecured) claim. 11 U.S.C. § 507 (1982 & Supp. V 1987). A non-priority unsecured claim is unlikely to be recovered since both secured and priority claims must be paid first.

167. 11 U.S.C. § 507(a)(1) (1982) (administrative expenses are first priority claims). Under 11 U.S.C. § 503(b)(1)(A), administrative expenses include: "expenses of preserving the estate, including wages, salaries or commissions for services rendered after the commencement of the case . . . ."

168. 11 U.S.C. § 1129(a)(9)(A) (1982).

169. 11 U.S.C. § 502(b)(7) (1982 & Supp. V 1987).

170. For a discussion of unsecured claims, see *supra* note 166.

171. For a discussion of the disallowance of claims, see *supra* text accompanying note 169.

another goal of Chapter 11 which is to maximize returns on creditors' claims.[172] Determination of damages will enable the court to calculate the monetary amounts that the union would recover through reorganization and the increased availability of funds that would result from rejection of the labor contract. These amounts should be compared with the possible chance of the creditors receiving any part of their claims upon liquidation. The ultimate concern of this comparison is that the increased recovery of claims in reorganization is not solely attained by placing an unfair burden on the employees. Therefore, this examination will assure the union that the goal of a fair and equitable rejection will be accomplished. The court will then have the discretion to refuse rejection where the "balance of the equities" weighs against such a decision.

The requirement that "all of the affected parties are treated fairly and equitably" also reflects the "necessity" requirement.[173] The congressional intent is reasonably clear. This requirement was meant to spread the burden of reorganization to all affected parties.[174] The problem with implementing this requirement, however, is twofold: 1) it is fact specific and is therefore subject to ad hoc court decisions and 2) it demands reliance upon evaluations that may be exceedingly difficult to make either at the time the proposal was drafted or at the time of the rejection hearing.[175] The courts agree that although equity requires management to "tighten their belts," it "does not of necessity mean identical or equal treatment."[176]

In reviewing the necessity of a proposal, the court must be aware of the concerns of the other parties affected by the reorganization of the debtor. Inherent in this review is the uncertainty of the degree of impairment of the creditors' and equity holders' interests.[177] The Third Circuit opined that this uncertainty adds credence to a stricter view of necessity because it will protect the union from concessions beyond the absolute minimum reductions needed to prevent liquidation.[178] Al-

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172. *See* Bendixson, *supra* note 115, at 437.

173. Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of Am., 791 F.2d 1074, 1089 (3d Cir. 1986).

174. *See, e.g.*, 130 CONG REC. S8898 (daily ed. June 29, 1984) (statement of Sen. Packwood); *id.* at S8899 (statement of Rep. Morrison).

175. *See* REPORT ON BANKRUPTCY AND REORGANIZATION, *supra* note 77, at 8.

176. *In re* Carey Transp., Inc., 50 Bankr. 203, 210 (S.D.N.Y. 1985) (quoting in part *In re* Allied Delivery Sys. Co., 49 Bankr. 700, 703 (N.D. Ohio, 1985) ("Fair and equitable treatment does not of necessity mean identical or equal treatment.")), *aff'd sub nom.* Truck Drivers Local 807 v. Carey Transp. Inc., 816 F.2d 82 (2d Cir. 1987).

177. REPORT ON BANKRUPTCY AND REORGANIZATION, *supra* note 77, at 15.

178. *See* Wheeling-Pittsburgh Steel Corp., v. United Steelworkers of Am., 791 F.2d 1074, 1090-93 (3d Cir. 1986). Arguably, this opinion places great weight on the absence of a "snap-back" provision because the court believes it is the best manner in which to deal with the uncertainty of the economic projections. For a further discussion of the "snap-

though this view limits the sacrifices of the union, it also places a disproportionate share of reorganization on the other creditors involved. The most important goal of Chapter 11 is to emerge with a reorganization plan that addresses the long-term rehabilitation of the debtor.[179] If the union is only required to make concessions based on a myopic view of Chapter 11, one of four results could occur: 1) the plan will be approved but, because of its short-sightedness, the plan will be unable to accommodate the future needs of the debtor;[180] 2) the classes of creditors will not approve the plan;[181] 3) the creditors, despite the chance that they may bear a disproportionate share of the burden, will approve the plan in the hope that they may benefit from the continued existence of the debtor; or 4) the plan will be confirmed by the court notwithstanding nonacceptance by a class of creditors impaired under the plan.[182] The coexistence of the "equity" requirement and the "necessity" requirement is further proof that, while the parties must share proportionately in the burdens and sacrifices of reorganization, the goal of rehabilitation of the debtor would be undermined by a failure to recognize the debtor's long-term needs.

In looking at section 1113(e),[183] a final point must be made. The

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back" issue, see *infra* notes 208-13 and accompanying text.

179. Bendixson, *supra* note 115, at 437. *See generally* M. BIENENSTOCK, *supra* note 115 (general discussion of the primary goals of Chapter 11).

180. It is questionable whether such a plan should be confirmed by the court given the Code requirements for confirmation. 11 U.S.C. § 1129(a)(11) (1982) (court shall confirm the plan only if confirmation "is not likely to be followed by the liquidation, or the need for further financial reorganization . . . . "). For further discussion of confirmation of a reorganization plan, see *infra* notes 181-82, 197 and text accompanying notes 199-207.

181. Confirmation of the reorganization plan occurs after the court has deemed the debtor to meet specified requirements—including approval of the creditors. 11 U.S.C. § 1129(a) (1982 & Supp. V 1987). Each class of claims or interests must accept the plan or not be impaired under the plan. A class is "impaired" under 11 U.S.C. § 1124(1) (1982 & Supp. V 1987), unless "with respect to each claim or interest of such class, the plan leaves unaltered, equitable and contractual rights" of each claim or interest. If a class is "impaired," it will be deemed to accept the plan if it will receive, on the effective date of the plan, an amount not less than it would have received upon liquidation—this is in regard to unsecured claims, secured claims are treated separately under section 1129(a)(7)(B) (Supp. V 1987). Paragraph eight requires each class to accept the plan or not be impaired. 11 U.S.C. § 1129(a)(8) (1982). This requirement is subject to the "cramdown" exception in 11 U.S.C. § 1129(b) (1982 & Supp. V 1987). For a discussion of "cramdown," see *infra* note 182.

182. 11 U.S.C. § 1129(b) (1982 & Supp. V 1987). This is commonly referred to as "cramdown" because it allows the court, if dissenting classes are paid in full before junior classes, to confirm the plan despite failure to comply with section 1129(a)(8).

183. 11 U.S.C. § 1113(e) (Supp. V 1987) ("If during a period when the collective bargaining agreement continues in effect, and if essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate," the court may authorize interim changes.).

Wheeling-Pittsburgh court opined that the words "necessary" and "essential" were synonymous,[184] supporting its view that "necessary" is to be equated with bare minimum. This argument, however, fails to explain why Congress chose to use different words in the two provisions. Other courts have recognized that section 1113(e) was intended to serve the short-term, interim period when emergency modifications are "essential to the continuation of the debtor's business."[185] These modifications were not intended to remain in force beyond the court's decision on the debtor's motion to reject. Furthermore, section 1113(e) is a "provisional remedy . . . [and therefore,] it will be frequently necessary to consider interim relief before the debtor's proposal can be refined through the negotiation process."[186]

VI. What Occurs After Rejection and How Should This Assist the Courts in Their Application of the "Necessity" Requirement?

A major problem with the framing of section 1113 was Congress' failure to enact provisions dealing with the post-rejection period. Unlike section 365, the other sections of the Code do not refer to section 1113 or to the fate of a labor contract if it is rejected.[187] Outright rejection would result in termination of the contract and would give rise to claims for damages.[188] The focal point, however, concerns the status of the parties' relationship and how the debtor is to structure the reorganization plan after rejection has been approved. Most courts[189] have failed to recognize the importance of looking beyond the immediate impact of granting rejection of collective bargaining agreements in formulating a standard for rejection.

Rejection of a collective bargaining agreement does not change the underlying relationship between the parties. Although a debtor-em-

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

185. *See, e.g., In re* Royal Composing Room, Inc., 62 Bankr. 403, 417-18 (S.D.N.Y. 1986), *aff'd*, 848 F.2d 345 (2d Cir. 1988); Truck Drivers Local 807 v. Carey Transp., Inc., 816 F.2d 82, 89 (2d Cir. 1987).

186. *Royal Composing*, 62 Bankr. at 417-18.

187. If an executory contract is not rejected prior to the plan of confirmation, a debtor may choose to assume, assign, or reject the contract, 11 U.S.C. § 365(a) (1982 & Supp. V 1987), in the plan of confirmation itself. 11 U.S.C. § 1123(b)(2) (1982 & Supp. V 1987). In contrast, no reference is made to section 1113 in any other provision of the Code.

188. For a discussion of the claims arising from rejection of an executory contract, see *supra* notes 162-69 and accompanying text.

189. *Contra* Truck Drivers Local 807 v. Carey Transp., Inc., 816 F.2d 82 (2d Cir. 1987) (court looked beyond rejection of the collective bargaining agreement and focused on the future of the debtor under the reorganization plan).

ployer seeks rejection, it still requires the services of labor and must seek to contract for these services on new terms.[190] Consistent with the congressional intent underlying section 1113 is the debtor-employer's duty to bargain with the employee's representative even after rejection.[191] Throughout the rejection process, there is a tension between the goals of the NLRA and those of Chapter 11. Arguably, the concerns of reorganization of the debtor predominate as the court analyzes the necessity of rejection to the future viability of the debtor. Once rejection occurs, however, the balance shifts. The bargaining process is then controlled under the auspices of the NLRA, and the duty to bargain ends only after an "impasse" has been reached.[192]

What happens if the parties agree to a new contract? The Code does not specifically attend to this question, but a reference to section 1123[193] and its treatment of regular executory contracts is illuminating. Under section 1123 (b)(2),[194] a debtor may choose to assume, assign, or reject an executory contract as part of a plan for reorganization. The key language under this provision is the word "may." If a debtor desires, it may choose to continue to honor the executory contract and provide for assumption of the contract as part of the Chapter 11 plan.[195] In the case of a contract entered into postpetition, the debtor should be afforded the same opportunities under section 1123 as if rejection had not occurred. This would mean that the debtor could seek assumption of the new contract in the confirmation plan or rejection prior to confirmation.[196]

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190. George, *Collective Bargaining in Chapter 11 and Beyond*, 95 YALE L.J. 300, 310-11 (1985).

191. *In re* American Provision Co., 44 Bankr. 907, 909 n.8 (D. Minn. 1984) ("As a general principle, rejection of collective bargaining agreements does not affect the rights and responsibilities under the National Labor Relations Act.") (citing Briggs Transp. Co. v. International Bhd. of Teamsters, 40 Bankr. 972 (D. Minn. 1984), *aff'd*, 739 F.2d 341 (8th Cir.), *cert. denied*, 469 U.S. 917 (1984)).

192. George, *supra* note 190, at 312-13 n.69. "[A] debtor-in-possession, even after rejection, is compelled to bargain with an established bargaining unit in attempt to execute a new collective bargaining agreement." *In re* Brada Miller Freight, 702 F.2d 890, 899 (11th Cir. 1983). " 'Duty to bargain' is a 'term of art' in labor law and is understood to include the concept of 'impasse' unless explicitly qualified." *Id.* at 313 n.69 (citing NLRB v. Katz, 369 U.S. 736 (1962); NLRB v. American Nat'l Ins. Co., 343 U.S. 395 (1952)).

193. 11 U.S.C. § 1123 (1982 & Supp. V 1987).

194. 11 U.S.C. § 1123(b)(2) (1982 & Supp. V 1987).

195. The debtor need not assume existing executory contracts under the plan of confirmation. 11 U.S.C. § 1123(b)(2) (1982 & Supp. V 1987). If a debtor wishes to assume an executory contract, it must cure any breach of the contract, as well as obtain court approval for assumption within the plan. If this path is not chosen, then the contract is rejected. 11 U.S.C. § 365(a), (b) (1982 & Supp. V 1987). In this particular scenario, the debtor has negotiated a new contract; therefore, the concerns differ from assuming a previously breached executory contract.

196. Accomodating this proposal would probably require amendments to the lan-

The negotiation of a new collective bargaining agreement should be viewed as an assumed contract that, upon court approval, will become a part of the plan. The need to seek court approval for assumption of a new agreement should allay any fears that the debtor has not sought a viable collective bargaining agreement. Arguably, this puts a great deal of pressure on the debtor to be sure that a negotiated agreement will improve the likelihood of a successful reorganization. When the debtor seeks approval by creditors under section 1129,[197] their decisions will balance the projected costs of the new labor agreement and their desire to maximize their own claims through the revitalization of the debtor. If, prior to confirmation, the new agreement is incompatible with the goal of rehabilitation, the debtor should be able to seek rejection of this agreement. This situation would further forestall confirmation of a reorganization plan but should be allowed if the court determines that the congeries of interests favor rejection as necessary to permit the likelihood of the successful reorganization of the debtor.

The more difficult question is what happens if the parties bargain to an "impasse" without entering into a new agreement. If the parties have reached that juncture, the predominant intent of Congress to promote private collective bargaining has failed. Arguably, the debtor-employer should be able to unilaterally impose terms resembling those under which the court allowed rejection. This would afford the union employees the maximum protection because these terms would have arisen from the negotiations that are required to continue throughout a section 1113 hearing. Furthermore, if the union finds these changes unacceptable, it may exercise its right to strike.[198] One may argue that the imposition of these terms would eliminate the debtor's incentive to bargain after rejection is granted. This is not likely to occur for two reasons: (1) the debtor will be monitored under the provisions of the NLRA in order to assure that it has met its duty to bargain to an "impasse," and (2) the debtor will recognize that the union's right to strike would seriously jeopardize the confirmation of any reorganization plan. Uncertainty as to labor costs would mean that the creditors, non-union employees, and equity holders would be unable to determine their respective positions in reorganization. This would obstruct the possibility of approval by the creditors or the submission of a via-

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guage of 11 U.S.C. § 365(a), (b) and 11 U.S.C. § 1123(b)(2).

197. 11 U.S.C. § 1129(a)(10) (Supp. IV 1986) (confirmation does not require unanimous consent but it does require at least one class that is "impaired" under the plan to accept the plan). For a discussion of confirmation of a Chapter 11 plan, see *supra* notes 180-81. A plan may be approved without consent of the creditors if the conditions of section 1129(b) are fulfilled—"cramdown". For a discussion of "cramdown," see *supra* note 182 and accompanying text.

198. *In re* Royal Composing Room, Inc., 62 Bankr. 403, 405 (S.D.N.Y. 1986), *aff'd*, 848 F.2d 345 (2d Cir. 1988).

ble plan that would allow confirmation by the court. The debtor, faced with the possibility of a strike and a delay in confirmation of the reorganization plan, would seek to compromise with the union.

The purpose of rejection is to increase the ability of the debtor to reorganize,[199] but the likelihood of confirmation, outside of "cramdown,"[200] will depend on the availability of sufficient funds to assure acceptance of the plan by the unsecured creditors.[201] Hence, if a court adopts the Third Circuit's interpretation of "necessary," there will be a greater burden on the creditors—other than the affected unions—and a reduction of the funds available for reorganization. Since labor costs are usually the largest cost factor of concern in a reorganization,[202] a court's refusal to allow rejection will undermine cost reductions and decrease the amount of funds available for successful reorganization. On the other hand, if rejection was permitted based on the Third Circuit's standard, the union would shoulder a disproportionately smaller burden than the other creditors. This disproportionate burden would arise because rejection would be based upon a minimum amount of reductions in labor costs. Since it would be unlikely that any final agreement would deviate from the rejection proposal, the plan for reorganization would include a labor contract that puts a significant burden on the other creditors involved in the reorganization plan.

Emphasis by the court on short-term goals, rather than the debtor's ultimate future, fails to recognize the debtor's obligation under section 1129(a)(11).[203] Section 1129(a)(11) requires the debtor to present a confirmable plan that will avoid either liquidation or further reorganization.[204] As the *Carey Transportation* court stated, "it becomes impossible to weigh necessity as to reorganization without looking into the debtor's ultimate future and estimating what the debtor needs to attain financial health."[205] This provision recognizes that in-

199. *See, e.g.*, Merrick, *supra* note 128, at 170 (labor is largest cost factor over which the debtor has control as most other costs are determined by external forces).

200. For a discussion of "cramdown," see *supra* note 182 and accompanying text.

201. Given the limitations under 11 U.S.C. § 507(a)(3) (1982 and Supp. V 1987), a portion of the damages will be considered unsecured claims as opposed to priority claims. For a discussion of section 507(a)(3), see *supra* text accompanying note 163. Unsecured claims do not have priority status; therefore, the chances of them receiving their claims are much less. For a discussion of unsecured versus priority claims, see *supra* note 166. Thus, a confirmation plan leaving little chance for the unsecured claims to receive the amounts that they would in liquidation is not likely to be approved by the creditors. For a discussion of the requirements for approval of a plan of confirmation, see *supra* notes 180-82 and accompanying text.

202. Merrick, *supra* note 128, at 170.

203. 11 U.S.C. § 1129(a)(11) (1982 & Supp. IV 1986).

204. *Id.*

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

herent in Chapter 11 reorganization is a degree of uncertainty created by the unpredictability of long-term economic conditions. "Projections are necessarily speculations about the future and are an art, rather than a science."[206] Basing the final modifications on bare survival indicates a refusal to recognize the inevitable uncertainties of the future. Therefore, the reorganization plan must consider the long-term picture instead of relying on minimal cost reductions that are unable to accommodate future economic needs and uncertainties.[207]

One troublesome issue raised in *Wheeling-Pittsburgh* was the court's clear decision to deny the debtor's rejection petition because of the lack of a "snap-back" provision.[208] A "snap-back" provision allows for incremental increases in wages and benefits upon the triggering of a certain event. In this case, the union wanted the increases to coincide with future profits of the company.[209] Many unions have sought to rely on such an argument in seeking to oppose rejection.[210] This argument, however, is further evidence that a strict view of "necessary" will undermine the original intent behind a debtor's section 1113 petition. If a "snap-back" is required, the courts would not reject a labor contract, and a debtor would only be able to seek modifications that would last until a return to financial profitability.[211] The problem with such an approach is that often labor costs are a significant element of the company's poor financial health. If a debtor is required to provide for wage increases as its financial strength increases, these modifications may undermine much of the reason for the success of the reorganization. Indeed, there will be cases where short-term profitability is increasing simply because of the prior reduction in labor costs. Furthermore, continued financial uncertainty will require stabilized operating costs until the strength of the company can be assured.

One approach to dealing with the issue of "snap-back" provisions may be found in the provisions of section 1114(g)(3),[212] which allows the parties to seek more than one modification of retirement benefits prior to confirmation. As posited earlier, under section 1113 the debtor

206. *In re* Royal Composing Room, Inc., 62 Bankr. 403, 407 (S.D.N.Y. 1986), *aff'd*, 848 F.2d 345 (2d Cir. 1988).

207. *Id.* at 418.

208. Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of Am., 791 F.2d 1074, 1090 (3d Cir. 1986).

209. *Id.*

210. *E.g., In re* William P. Brogna and Co., 64 Bankr. 391, 392 (E.D. Pa. 1986) (debtor proposed to pay creditors 100% of claims within three years after confirmation but rejection was not granted because the proposal did not contain a "snap-back" provision).

211. *In re* Walway Co., 69 Bankr. 967, 974 n.17 (E.D. Mich. 1987).

212. Retiree Benefits Bankruptcy Protection Act of 1988, Pub. L. No. 100-334, 1988 U.S. CODE CONG. & ADMIN. NEWS (102 Stat.) 610 (to be codified at 11 U.S.C. § 1114). For a further discussion of section 1114(g)(3), see *infra* text accompanying note 215.

should be able to seek rejection of a newly-entered into agreement that has arisen as a result of an earlier court-ordered rejection.[213] As a corollary to this argument, prior to confirmation, the union should be able to seek modifications amounting to an increase in wages. Allowing the possibility of modifications would help assure the continuing negotiations between the debtor and the union throughout the reorganization period.

VII. SECTION 1114

In adopting section 1114, Congress clearly rejected the *Carey Transportation* standard by stating that, "[i]t is intended that the words 'necessary for the reorganization of the debtor' . . . be interpreted as the Third Circuit interpreted them in *In re Wheeling-Pittsburgh Steel Corporation* . . . ."[214] While this statement clarified the standard to be employed in section 1114 hearings, it also provided ammunition to those arguing that the *Wheeling-Pittsburgh* standard is applicable to determine if a debtor should be able to reject a collective bargaining agreement. Notwithstanding the adoption of section 1114, courts must avoid the temptation to rely on the legislative history of section 1114 when interpreting section 1113. A clear reason to avoid such an interpretation exists in the fact that section 1114 deals solely with modification of retirement benefits, and its concerns differ from those in section 1113. Furthermore, as stated previously, the *Wheeling-Pittsburgh* standard undermines the ability of a debtor-in-possession to seek rejection of collective bargaining agreements and jeopardizes the ability of the debtor to reorganize.

Despite Congress' adoption of the *Wheeling-Pittsburgh* standard under section 1114, there are two key provisions adopted under the new law which should be considered when discussing section 1113. The first provision allows a debtor and the retiree to make more than one application for modification.[215] This provision demonstrates Congress' desire to allow the parties to seek adjustments that will best suit the parties as they enter into the confirmation stage. Such modifications should only be allowed if they do not adversely affect the equitable treatment of all parties involved in the reorganization. As suggested above,[216] application of this provision in the context of section 1113

213. *See supra* notes 193-98 and accompanying text.

214. H.R. 2969, 100th Cong., 2d Sess., 134 CONG. REC. S6825 (daily ed. May 26, 1988) (statement of Sen. Metzenbaum).

215. *Id.* at S6823-24. (section 1114(g)(3) allows a trustee to seek more than one reduction in the level of retiree benefits and allows the union to seek more than one increase, as long as the modifications are sought prior to confirmation of the reorganization plan).

216. *See supra* text accompanying notes 212-13.

would have important implications for newly negotiated contracts. If the union has knowledge that they can continue to seek adjustments until confirmation, they may be more willing to compromise in the earlier stages of rejection. Where the period before confirmation is expected to be quite lengthy, the opportunity to seek adjustments might serve to soften the blow of rejection of the original agreement and promote good faith bargaining.

The second provision proposed by Congress is by way of an amendment to section 1129(a). This amendment requires that the confirmation plan provide for the continuation of retiree benefits at the level established by the court pursuant to section 1114.[217] This level would be established either by agreement between the debtor and the union or by the court at a level no lower than that under which the court granted the motion to modify the existing agreement.[218] The clear intent was to protect retiree benefits and to assure their proper place in the confirmation plan.[219] Interestingly, section 1129(a) does not provide for a similar assurance in the case of collective bargaining agreements. Although a plan would not be confirmed without an understanding regarding the status of such an agreement, the lack of such a provision is further evidence of the problems in the language of section 1113.[220] A similar provision should exist as to section 1113 which, by its design, would mandate the existence of a collective bargaining agreement as part of the plan. Such a provision would: 1) protect creditors and equity holders from uncertain labor costs; 2) promote negotiations on the part of a debtor attempting to establish a reorganization plan; and 3) strengthen the position of the union by forcing the debtor to bargain for a new agreement in order to avoid delay and the financial danger associated with a strike by a union.

VIII. CONCLUSION

The problem with the *Carey Transportation* decision is not the holding nor its rejection of the Third Circuit standard. Rather, the problem is that the Second Circuit enunciated the correct standard but failed to do so convincingly. The sole reason for this failure may be that, given the factual background of the case, rejection would have been permitted under either standard. At the time of the hearing, Local 807 had done very little to refute the evidence that there was a strong relationship between Carey's past and projected losses and its

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217. H.R. 2969, 100th Cong., 2d Sess., 134 CONG. REC. S6824 (referring to an amendment to section 1129(a) to be called section 1129(a)(13)).

218. *Id.* at S6823-24 (referring to section 1114(g)(3)).

219. *Id.*

220. It is not clear why Congress omitted such a provision in section 1113 and has not acted to amend section 1113 accordingly.

excessive labor costs. Furthermore, the union also failed to offer evidence to disprove the necessity of the modifications to Carey's reorganization.[221] This inaction may lead to the suggestion that the Second Circuit would have granted Carey's petition for rejection even under the stricter "necessity" standard. For that reason, *Carey Transportation* should be limited to its particular set of facts. Thus, the standard that the court enunciated requires greater support than the Second Circuit provided.

In contrast, the *Wheeling-Pittsburgh* decision is an example of the failure of the courts to look beyond the hearing to the financial realities of reorganization. The decision is bothersome because of the influence it will have on future bankruptcy court decisions. As the situation stands, courts can choose to manipulate the standard depending on their view of section 1113.

Perhaps the most problematic development in this area has been the adoption by Congress of the *Wheeling-Pittsburgh* standard for rejection of retirement benefits in section 1114. The possibility that courts will see this as a mandate to apply this standard to section 1113 is extremely troublesome. Courts should avoid this inclination and realize that the application of this standard to the rejection of a collective bargaining agreement will undermine the goals of the Chapter 11 reorganization process.

The likelihood that Congress will recognize the problem and amend section 1113 is quite small. The interest groups and political forces that influenced Congress in 1984 would certainly prevent a further codification of a clear standard for rejection. Thus, the burden is on the courts to implement modifications, as part of their structuring of the rejection standard. The courts should choose to adopt a standard that is not myopic and which recognizes the goal of long-term financial health of the debtor. On the other hand, the courts should seek to encourage private compromise and to prevent a disproportionate sharing of the burden of reorganization.

The phrase "necessary to permit reorganization of the debtor" must be seen to have meaning outside of section 1113(b)(1)(A). Defining the proper standard means adopting one that can be administered in a "workable manner." In this case, it requires reconciliation of the goals of reorganization and the need to protect employees from unfair labor practices. This reconciliation means that the most important goal of section 1113 is to promote compromise in the search for an equitable proposal that will increase the likelihood of the long-term financial stability of the debtor.

Congress obviously thought section 1113 could stand alone, and

221. Brief for the Debtor-Appellee at 33-34, Truck Drivers Local 807 v. Carey Transp., Inc., 816 F.2d 82 (2d Cir. 1986) (No. 86-5057).

therefore, failed to recognize that this provision is interrelated to other concerns of Chapter 11. The courts must overcome the legislative isolation of section 1113 and realize that the process of reorganization does not end after a decision concerning rejection has been made. Adopting a standard that contemplates the long-term probability of successful reorganization encompasses a more realistic understanding of the goal of Chapter 11. The job of the courts in administering section 1113 will be to understand that proper application of this standard will not jeopardize the protections that labor is afforded under the NLRA. A section 1113 proposal that looks at the long-term financial health of the debtor will not lay a disproportionate burden of reorganization on the shoulders of labor.

Jeffrey W. Berkman