

Comment

FROM LEGISLATION TO CONSTERNATION: HAS SECTION 1113 REALLY CHANGED *BILDISCO*?

I. INTRODUCTION

In 1984 the Supreme Court decided *National Labor Relations Board v. Bildisco & Bildisco*,¹ upholding the ability of a Chapter 11 debtor to unilaterally reject a collective bargaining agreement² where the debtor could establish that the agreement was burdensome to the estate and that the balance of the equities favored rejection.³ The decision created a great deal of uneasiness for union officials⁴ who feared a possible onslaught of bogus bankruptcy activities for the purpose of terminating unwanted collective bargaining agreements.⁵

1. 465 U.S. 513 (1984)

2. *Id.* at 516-17.

A collective bargaining agreement is an employment contract which is the result of negotiations between the employer and employees or their representative. It is normally stipulated that the employees agree not to strike during the life of the agreement. See BLACK'S LAW DICTIONARY 239 (5th ed. 1979).

Understandably, in many large corporations, the collective bargaining agreement represents a vital lynch pin to operation. In *United Steelworkers of America v. Warrior & Gulf Navigation Co.*, 363 U.S. 564 (1960), Justice Douglas stated:

A collective bargaining agreement is an effort to erect a system of industrial self-government. When most parties enter into contractual relationship [sic], they do so voluntarily, in the sense that there is no real compulsion to deal with one another, as opposed to dealing with other parties. This is not true of the labor agreement. The choice is generally not between entering or refusing to enter into a relationship, for that in all probability preexists the negotiations. Rather, it is between having that relationship governed by an agreed-upon rule of law or leaving each and every matter subject to a temporary resolution dependent solely upon the relative strength, at any given moment, of the contending forces.

Id. at 580.

3. *Bildisco*, 465 U.S. at 526.

4. See *In re Wheeling-Pittsburgh Steel Corp.*, 52 Bankr. 997, 999 (Bankr. W.D. Pa. 1985).

5. The *Bildisco* decision exacted a quick and intense response from labor groups who initiated vast lobbying efforts challenging the holding in *Bildisco*. Such concerns over "industrial strife" were recognized by the *Bildisco* dissenters with respect to the unilateral rejection issue. The four dissenting justices voiced their belief that the majority holding effectively subordinated the National Labor Relations Act (NLRA) to the Bankruptcy Code. See *Bildisco*, 465 U.S. at 539 (Brennan, J., dissenting). See also *infra* text accompanying notes 53-57.

In response to these concerns, Congress proposed an amendment to the then-pending Bankruptcy Amendments and Federal Judgeship Act of 1984.⁶ It thus enacted section 1113 of the Bankruptcy Code,⁷ which forbids a Chapter 11 debtor to unilaterally reject a collective bargaining agreement and also prescribes both substantive and procedural prerequisites to obtaining court authorization to reject.⁸

6. Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98 Stat. 390.

7. 11 U.S.C. § 1113 (Supp. 1986). *See also* 130 CONG. REC. 58,890 (daily ed. June 29, 1984).

8. Section 1113 states in its entirety:

(a) The debtor in possession, or the trustee if one has been appointed under the provisions of this chapter, other than a trustee in a case covered by subchapter IV of this chapter and by title I of the Railway Labor Act, may assume or reject a collective bargaining agreement only in accordance with the provisions of this section.

(b)(1) Subsequent to filing a petition and prior to filing an application seeking rejection of a collective bargaining agreement, the debtor in possession or trustee (hereinafter in this section "trustee" shall include a debtor in possession), shall-

(A) make a proposal to the authorized representative of the employees covered by such agreement, based on the most complete and reliable information available at the time of such proposal, which provides for those necessary modifications in the employees benefits and protections that are necessary to permit the reorganization of the debtor and assures that all creditors, the debtor and all of the affected parties are treated fairly and equitably; and

(B) provide, subject to subsection (d)(3), the representative of the employees with such relevant information as is necessary to evaluate the proposal.

(2) During the period beginning on the date of the making of a proposal provided for in paragraph (1) and ending on the date of the hearing provided for in subsection (d)(1), the trustee shall meet, at reasonable times, with the authorized representative to confer in good faith in attempting to reach mutually satisfactory modifications of such agreement.

(c) The court shall approve an application for rejection of a collective bargaining agreement only if the court finds that—

(1) the trustee has, prior to the hearing, made a proposal that fulfills the requirements of subsection (b)(1);

(2) the authorized representative of the employees has refused to accept such proposal without good cause; and

(3) the balance of the equities clearly favors rejection of such agreement.

(d)(1) Upon the filing of an application for rejection the court shall schedule a hearing to be held not later than fourteen days after the date of the filing of such application. All interested parties may appear and be heard at such hearing. Adequate notice shall be provided to such parties at least ten days before the date of such hearing. The court may extend the time for the commencement of such hearing for a period not exceeding

Enactment of this new legislation was accompanied by much comment and speculation as to its practical application and construction by the courts.⁹ Although to date there have been relatively few cases requiring implementation of section 1113, a great deal of light was shed upon its practical application and judicial construction in *In re American Provision Co.*¹⁰ and *In re Wheeling-Pittsburgh Steel Corp.*¹¹

The court in *American Provision*, the first case to be decided under section 1113, set forth interpretive guidelines which have been fol-

seven days where the circumstances of the case, and the interests of justice require such extension, or for additional periods of time to which the trustee and representative agree.

(2) The court shall rule on such application for rejection within thirty days after the date of the commencement of the hearing. In the interests of justice, the court may extend such time for ruling for such additional period as the trustee and the employees' representative may agree to. If the court does not rule on such application within thirty days after the date of the commencement of the hearing, or within such additional time as the trustee and the employees' representative may agree to, the trustee may terminate or alter any provisions of the collective bargaining agreement pending the ruling of the court on such application.

(3) The court may enter such protective orders, consistent with the need of the authorized representative of the employee to evaluate the trustee's proposal and the application for rejection, as may be necessary to prevent disclosure of information provided to such representative where such disclosure could compromise the position of the debtor with respect to its competitors in the industry in which it is engaged.

(e) 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, after notice and a hearing, may authorize the trustee to implement interim changes in the terms, conditions, wages, benefits, or work rules provided by a collective bargaining agreement. Any hearing under this paragraph shall be scheduled in accordance with the needs of the trustee. The implementation of such interim changes shall not render the application for rejection moot.

(f) No provision of this title shall be construed to permit a trustee to unilaterally terminate or alter any provisions of a collective bargaining agreement prior to compliance with the provisions of this section.

11 U.S.C. § 1113 (includes Federal Judgeship Act of 1984, Pub. L. No. 980-353, tit. III, § 541(a), 98 Stat. 390).

9. See generally Note, *Rejection of Collective Bargaining Agreements in Bankruptcy: NLRB v. Bildisco & Bildisco and the Legislative Response*, 33 CATH. U.L. REV. 943, 995-99 (1984) (considering the practical consequences of § 1113); Note, *Rejection of Collective Bargaining Agreements in the Aftermath of 11 U.S.C. § 1113: What Does Congress Intend?*, 9 DEL. J. CORP. L. 701, 720-22 (1984) [hereinafter Note, *What Does Congress Intend?*] (discussing the operative effect and potential problems of § 1113).

10. 44 Bankr. 907 (Bankr. D. Minn. 1984).

11. 50 Bankr. 969 (Bankr. W.D. Pa. 1985), *aff'd*, 52 Bankr. 997 (W.D. Pa.), *vacated*, 791 F.2d 1074 (3d Cir. 1986).

lowed in subsequent cases.¹² *Wheeling-Pittsburgh*, involving the largest corporate debtor ever to seek rejection of a collective bargaining agreement, was one such case which relied upon the guidelines set forth in *American Provision*.

The importance of the *Wheeling-Pittsburgh* case in the recent struggle to implement section 1113 cannot be understated, for it is the first case to have taken the section 1113 issue to a court of appeals. The odyssey of the case through the courts, with the surprising reversal by the Third Circuit Court of Appeals, certainly illustrates the initial problems which courts have had in working out the interpretive "bugs" of the legislation embodied in section 1113.

In view of the size of the company involved, as well as the stricter standards of interpretation enunciated by the Third Circuit in *Wheeling-Pittsburgh*, this decision will doubtless have a definite impact upon similar cases to follow.¹³ Although until recently many disgruntled labor leaders were asking, Has section 1113 really changed *Bildisco*? the recent Third Circuit decision in *Wheeling-Pittsburgh* may well be interpreted as a significant step towards answering that question. This note will briefly examine the background leading to the present law of rejection of collective bargaining agreements in Chapter 11 reorganizations; the major attempts to date to interpret the new legislation in *American Provision* and the *Wheeling-Pittsburgh* cases; the possible flaws in these interpretations as enunciated by the Third Circuit in *Wheeling-Pittsburgh*, and the possible effect that the decision in this case will have on future attempts to reject collective bargaining agreements.

12. See *infra* text accompanying note 72.

13. Although the decision of the court of appeals will have no material effect upon the November 1, 1985 collective bargaining agreement between the parties pursuant to an agreement between the Wheeling-Pittsburgh Steel Company and the United Steelworkers of America, each agreed to continue the appeal due to the strong precedential considerations. This new agreement was entered into subsequent to the settlement of a labor strike which followed the bankruptcy court's decision authorizing the company to reject its prior collective bargaining agreement. See *In re Wheeling-Pittsburgh Steel Corp.*, 50 Bankr. 969 (Bankr. W.D. Pa. 1985), *aff'd*, 52 Bankr. 997 (W.D. Pa.), *vacated*, 791 F.2d 1074 (3d Cir. 1986).

As stated in the memorandum presented on appeal by the company's principal bank creditors, "[T]he USWA's real concern is with the possible adverse effects of the Bankruptcy and District Court opinions as precedents in possible future steel company bankruptcies" Memorandum of The Principal Bank Creditors at 4, *Wheeling-Pittsburgh Steel Corp. v. United Steelworkers of Am.*, 791 F.2d 1074 (3d Cir. 1986).

II. BACKGROUND

A. *Statutory Development in Bankruptcy*

Congress enacted the first Bankruptcy Act in 1898.¹⁴ It was recently replaced by the Bankruptcy Reform Act of 1978.¹⁵ Under the 1978 Act, a corporate debtor in severe financial difficulty has two options: he may seek relief under either Chapter 7¹⁶ or Chapter 11¹⁷ of the Bankruptcy Code. In a Chapter 7 proceeding, the debtor's assets are liquidated for distribution to creditors. In contrast, Chapter 11 was formulated to permit the debtor to reorganize while continuing to operate.¹⁸

14. Bankruptcy Act of 1898, ch. 541, 30 Stat. 544 (codified as amended at 11 U.S.C. §§ 1-1200 (1976)) (repealed 1978). Numerous amendments were made to the Act prior to its repeal: the Chandler Act of 1938, ch. 575, 52 Stat. 905; Act of July 1, 1945, ch. 532, 60 Stat. 409; Act of Sept. 25, 1962, Pub. L. No. 87-681, 76 Stat. 570; Acts of Nov. 28, 1967, Pub. L. No. 90-156, 90-157, 90-158, 81 Stat. 510, 511, 516; Act of Oct. 19, 1970, Pub. L. No. 91-467, 84 Stat. 990.

15. 11 U.S.C. §§ 101-151326 (1982 & Supp. 1986).

16. 11 U.S.C. §§ 701-766 (codification of Chapter 7).

17. 11 U.S.C. §§ 1101-1174 (codification of Chapter 11).

18. 11 U.S.C. §§ 101-151326. Normally, a Chapter 11 proceeding is commenced by the debtor filing a petition for reorganization. *Id.* § 301. When the case is commenced, an estate is credited, *id.* § 541(a), and a trustee, *id.* § 1104(a), or debtor-in-possession, *id.* § 1107 (which is usually the debtor itself, *id.* § 1101(1)), is appointed by the bankruptcy court. Unless ordered otherwise by the court, the trustee continues to run the business, *id.* § 1108, and subsequently files a reorganization plan designating claims against the estate, *id.* § 1121, as well as a plan for repayment of such claims. *See id.* §§ 1123, 1121-1129.

Such a plan was devised to permit the troubled business to get "back on its feet" in hopes that in the long run the return to creditors, shareholders, and employees would be preferable to an immediate liquidation. It was the congressional intent that such a business might reorganize "so that it may continue to operate, provide its employees with jobs, pay its creditors, and produce a return for its shareholders." H.R. REP. NO. 595, 95th Cong., 1st Sess. 220 (1977), *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 6179. It is not surprising, then, that in the balancing of benefits, a Chapter 11 reorganization, if feasible, is preferable as "the debtor, its creditors and employees, and the public at large benefit from the business' survival." *In re Bildisco*, 682 F.2d 72, 77 (3d Cir. 1982).

One study shows, for example, that in a Chapter 7 liquidation, priority creditors recover less than 33%, and unsecured creditors recover a median of 8%, of their valid claims. However, with a successful Chapter 11 reorganization, priority creditors usually recover fully on their claims, while unsecured creditors recover a median of 19% under one-payment plans, and 10% under deferred payment plans. D. STANLEY & M. GIRTH, *BANKRUPTCY: PROBLEM, PROCESS, REFORM* 129-30, 142-43 (1971).

In an effort to assist the debtor in his attempts to reorganize, section 365(a) of the Bankruptcy Code provides for the rejection by the debtor of any executory contracts¹⁹ which are financially burdensome to the reorganization enterprise.²⁰ Although it has been argued that there was no intent by Congress to subject collective bargaining agreements to this provision,²¹ courts have generally recognized collective bargaining agreements as executory contracts subject to the provision of section 365(a).²² This inference is supported by the fact that section 365(a) provides a specific exemption for agreements subject to the Railway Labor Act (RLA) without creating a similar exemption for those agreements governed by the National Labor Relations Act (NLRA).²³ The fact that no such exception was included, it is reasoned, points to the conclusion that Congress intended to subject all other labor contracts, including NLRA collective bargaining agreements, to the executory contract provision of section 365(a).²⁴

It is at this juncture that a conflict arises. The rejection provisions of section 365(a) stand in sharp contrast to the provisions of the NLRA, of which section 8(d) prohibits unilateral modification or termination of collective bargaining agreements and provides specific guidelines for negotiating any changes in such agreements.²⁵ This conflict has led to the result that many debtors seeking to reject collective bargaining agreements under section 365(a) have been charged with unfair labor practices under the NLRA.²⁶ This appar-

19. An executory contract has been defined, for bankruptcy purposes, as a contract "on which performance remains due to some extent on both sides." H.R. REP. No. 595, 95th Cong., 1st Sess. 347 (1977), *reprinted in* 1978 U.S. CONG. CODE & AD. NEWS 5963, 6303.

20. See 11 U.S.C. § 365(a) which states that "[e]xcept as provided in Section 765 and 766 of this title and in subsections (b), (c), and (d) of this section, the trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor."

21. See Note, *What Does Congress Intend?*, *supra* note 9, at 704.

22. See *American Provision*, 44 Bankr. at 908.

23. 11 U.S.C. § 1167 provides in pertinent part:

23. 11 U.S.C. § 1167 provides in pertinent part: "Notwithstanding section 365 of this title, neither the court nor the trustee may change the wages or working conditions of employees of the debtor established by a collective bargaining agreement that is subject to the Railway Labor Act"

24. See *supra* note 20.

25. See 29 U.S.C. § 158(d) (1982).

26. See, e.g., *Shopmen's Local Union No. 455 v. Kevin Steel Products, Inc.*, 519 F.2d 698 (2d Cir. 1975).

ently irreconcilable discrepancy led to a plethora of litigation which set the stage for the enactment of section 1113.

B. *Attempts to Reject Agreements: Early Cases*

The Second Circuit, in *Shopmen's Local Union No. 455 v. Kevin Steel Products*,²⁷ was the first appellate court to address the conflict between section 313(1) of the Bankruptcy Act (the forerunner of section 365(a)) and section 8(d) of the NLRA.²⁸ The court permitted rejection of the agreement and appeared to reconcile the conflict by enunciating the "new entity theory."²⁹ Under this theory, the debtor-in-possession became a "new entity" separate and distinct from the pre-bankruptcy corporation. As such, the "new entity" debtor was not a party subject to the termination restrictions imposed upon the prior agreement by section 8(d) of the NLRA.³⁰ While under this analysis the conflict would cease to exist, the court also addressed the factual issue of whether the bankruptcy court properly permitted rejection.³¹ Although the court affirmed the bankruptcy court's decision, it found the standard for rejection used by that court too narrow³² because it failed to consider labor practices. The Second Circuit, therefore, adopted the standard employed in *In re Overseas*

27. *Id.*

28. See 29 U.S.C. § 158(d). The union had filed unfair labor practices charges against Kevin Steel alleging violations of § 8(a)(1) of the NLRA through offers to bribe a union employee to abandon the union, by firing employees on the basis of union affiliation, and by refusing to sign a new collective bargaining agreement. Shortly thereafter, the company filed its petition for reorganization under Chapter 11 of the Bankruptcy Act (now incorporated in Chapter 22 of the Bankruptcy Code). The NLRA found the company guilty of unfair labor practices and ordered the company to sign the collective bargaining agreement. Kevin Steel successfully moved to reject the agreement in the bankruptcy court, but the district court reversed, holding § 313(1) (the forerunner of § 365(a)) inapplicable to such agreements. *Kevin Steel*, 519 F.2d at 700-01.

29. *Kevin Steel*, 519 F.2d at 704. This theory met with a great deal of criticism, for although its adoption would render as moot the § 365(a) versus § 8(d) conflict, it was believed that if Congress intended such an exception to § 365(a), this would have been provided for in the statutory framework. The Supreme Court reflected this belief by rejecting the "new entity" theory in *Bildisco*, 465 U.S. at 525. See *infra* text accompanying notes 48-50.

30. *Kevin Steel*, 519 F.2d at 704.

31. *Id.* at 706. The "new entity" theory precluded the conflict question; however, the court found that it was important to reach the rejection standard question.

32. *Id.* at 707. The bankruptcy court had considered only whether rejection would improve the financial status of the company.

National Airways.³³ This standard was stricter and required a more stringent balancing of the equities.³⁴

The Second Circuit court's opinion in *Kevin Steel* met with some disapproval, especially in regard to the "new entity" theory.³⁵ However, the same court modified its approach a few weeks later in *Brotherhood of Railway, Airline and Steamship Clerks v. REA Express, Inc.*,³⁶ adopting a rejection standard even stricter than that of *Kevin Steel*. Whereas the *Kevin Steel* standard required a somewhat stringent balancing of the equities before permitting rejection,³⁷ the standard enunciated in *REA Express* permitted rejection only where, after a careful weighing of all equities involved, a court could conclude that an onerous and burdensome executory collective bargaining agreement would "thwart efforts to save a failing carrier in bankruptcy from collapse . . ."³⁸ Although *REA Express* was easily distinguishable from *Kevin Steel* in that it involved an agreement under the RLA,³⁹ the court chose not to limit its rejection standard on this basis, but rather to adopt this stricter standard for all cases involving collective bargaining agreements under either the RLA or the NLRA.⁴⁰

33. 238 F. Supp. 359 (E.D.N.Y. 1965).

34. The *Overseas* standard adopted in *Kevin Steel* would permit rejection of an agreement only:

[a]fter thorough scrutiny, and a careful balancing of the equities on both sides, for, in relieving a debtor from its obligations under a collective bargaining agreement, it may be depriving the employees affected of their seniority, welfare and pension rights, as well as other valuable benefits which are incapable of forming the basis of a provable claim for money damages. That would leave the employees without compensation for their losses, at the same time enabling the debtor, at the expense of the employees, to consummate what may be a more favorable plan of arrangement with its other creditors.

Id. at 361-62.

35. *See supra* note 29.

36. 523 F.2d 164 (2d Cir. 1975) (issue of whether a collective bargaining agreement subject to the Railway Labor Act (RLA) was controlled by the same principles governing agreements subject to the NLRA). *See also supra* note 23.

37. *See supra* note 34.

38. *REA Express*, 523 F.2d at 169.

39. As was noted earlier, Congress carved out an exception for agreements under the RLA in § 365(a). *See supra* note 23. A similar exception existed in the old Bankruptcy Act § 77(n) (under which *REA Express* was decided), prohibiting bankruptcy courts or trustees from changing working conditions or wages of railroad employees except as provided in § 151 of the RLA. 11 U.S.C. § 205(n) (1976) (repealed).

40. The court noted:

The purpose of these provisions of the RLA, like that of § 8(d) of

Up to this point, it was evident that the standards for the rejection of collective bargaining agreements were far from fully evolved. It was against this backdrop that judicial decisions were to unfold which would fuel the need for legislative response.

C. *Bildisco and Section 1113*

In *In re Bildisco*,⁴¹ the Third Circuit was the first appellate court to address the conflict between the NLRA and section 365(a) of the new Bankruptcy Code. The court adopted the *Kevin Steel* "new entity" theory,⁴² holding that as the debtor-in-possession was not a party to the agreement, rejection did not constitute an unfair labor practice under section 8(d) of the NLRA.⁴³ Rejecting the "certain failure" test of *REA Express*⁴⁴ as too strict, the court sought to adopt a different standard for rejection of a collective bargaining agreement. Although the court noted that the business judgment standard was the usual standard of review for rejection of executory contracts, it also stressed that Congress intended a stricter standard for rejection of collective bargaining agreements.⁴⁵ Affirming the district court's holding permitting rejection, the court adopted the two-part test first enunciated in *Kevin Steel* which required a showing that an agreement was burdensome to the estate and that a balancing of the equities favored rejection.⁴⁶

the National Labor Relations Act, 29 U.S.C. § 158(d), which was before us in *Kevin Steel*, is to avoid disruptions of commerce by forcing the parties to exhaust collective bargaining procedures and, where the RLA applies, to encourage use of arbitration and mediation before engaging in self-help, strikes or other forms of unilateral action.

REA Express, 523 F.2d at 168.

41. 682 F.2d 72 (3d Cir. 1982).

Bildisco & Bildisco was a general partnership in New Jersey. It filed a petition for reorganization under Chapter 11 on April 11, 1980, and moved to reject its collective bargaining agreement, claiming that rejection would save the company \$100,000 in 1981. The bankruptcy court permitted rejection. Meanwhile, the union filed charges of unfair labor practices with the NLRA. The case before the Third Circuit was a consolidation of the union's appeal from the bankruptcy court's order and the NLRA's petition for enforcement of its order against *Bildisco* for refusing to comply with the collective bargaining agreement. *Id.* at 75-76.

42. *See supra* note 29 and accompanying text.

43. *Bildisco*, 682 F.2d at 78-79.

44. *See supra* text accompanying note 38.

45. *Bildisco*, 682 F.2d at 79. *But see In re Ateco Equip., Inc.*, 18 Bankr. 915 (Bankr. W.D. Pa. 1982) (collective bargaining agreements subject to the same standard of review for rejection as other executory contracts).

46. *Bildisco*, 682 F.2d at 79.

The Supreme Court granted certiorari in *Bildisco* to examine the conflict between this case and the Second Circuit's decision in *REA Express*. It affirmed the Third Circuit's decision,⁴⁷ although expressly rejecting the "new entity" theory. The first issue the court addressed was the correct standard to be used in deciding whether to permit rejection. On this issue, the court unanimously affirmed the *Kevin Steel* balancing standard adopted by the Third Circuit.⁴⁸ On the second issue of whether post-petition unilateral modification of a collective bargaining agreement constituted an unfair labor practice, the court held in a 5-4 decision⁴⁹ that the NLRB could not impose unfair labor practice charges on a debtor for unilateral modification or rejection.⁵⁰ To do so, the majority concluded, would undermine the reorganization goals of section 365(a).⁵¹ The dissent, led by Justice Brennan, criticized the majority for failing to consider national labor policies of encouraging collective bargaining.⁵² It was this view which became the cornerstone of the soon to be adopted section 1113.

On the day following the *Bildisco* decision, amendment to bankruptcy reform legislation then pending was proposed which aimed to overturn the holding in *Bildisco*.⁵³ Although the reform bill eventually passed by the Senate did not contain these proposals, a conference committee was later appointed which drafted a bill incorporating the proposals now embodied in section 1113.⁵⁴ This bill was promptly enacted by both houses and signed into law by the President on July 10, 1984, as section 1113 of the Bankruptcy Code.⁵⁵ It forbade the unilateral rejection of collective bargaining agreements by a Chapter 11 debtor,⁵⁶ and established substantive

47. *Bildisco*, 465 U.S. at 517, 528.

48. *Id.* at 526. See *supra* note 34 and accompanying text.

49. Justice Rehnquist delivered the opinion of the Court, joined by Justices Burger, Powell, Stevens, and O'Connor. Justice Brennan dissented, joined by Justices White, Marshall, and Blackmun.

50. *Bildisco*, 465 U.S. at 532.

51. *Id.*

52. *Id.* at 553.

53. The proposal was drafted as an amendment to a bill then pending to revise the bankruptcy court system pursuant to the Supreme Court's earlier decision in *Northern Pipeline Constr. Co. v. Marathon Pipeline Co.*, 458 U.S. 50 (1982), which held that the bankruptcy court system had been given powers through the 1978 Reform Act which went beyond the scope of the Constitution.

54. 11 U.S.C. § 1113.

55. See *supra* text accompanying note 8.

56. 11 U.S.C. § 1113(a).

and procedural requirements which must be met before authority to reject would be granted.⁵⁷

Such prerequisites include providing the union with relevant information necessary to evaluate the proposed modifications,⁵⁸ and conferring with the union in good faith in an effort to reach "mutually satisfactory modifications" of the existing collective bargaining agreement.⁵⁹ If such negotiations fail to produce an agreement, authorization to reject may be granted only if the bankruptcy court finds that the debtor's proposal "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 of the affected parties are treated fairly and equitably."⁶⁰ Furthermore, authorization will be granted only where the union has refused to accept these proposals "without good cause"⁶¹ and where the balance of the equities clearly favors rejection.⁶² As it was realized that often these processes may be too lengthy for a debtor in dire circumstances, a provision was included permitting the court to authorize "interim changes" in order to avoid irreparable damage.⁶³

With the enactment of section 1113 came hopes of a balancing of the perceived inequalities wrought upon labor forces under section 365(a) of the Bankruptcy Code, and which were exacerbated by the *Bildisco* decision.⁶⁴ However, much was to rest upon subsequent judicial interpretation of this amendment and how its provisions would actually be construed on a case-to-case basis. In *American Provision*,⁶⁵ the bankruptcy court for the District of Minnesota made the first attempt to develop guidelines for interpreting and implementing section 1113.⁶⁶ The opinions in the recent *Wheeling-Pittsburgh*⁶⁷

57. See *infra* notes 58-63 and accompanying text.

58. 11 U.S.C. § 1113(b)(1)(B).

59. *Id.* § 1113(b)(2).

60. *Id.* § 1113(b)(1)(A).

61. *Id.* § 1113(c)(2).

62. *Id.* § 1113(c)(3).

63. *Id.* § 1113(e).

64. See *supra* text accompanying note 52.

65. 44 Bankr. 907 (Bankr. D. Minn. 1984).

66. See *infra* text accompanying note 72.

67. 50 Bankr. 969 (Bankr. W.D. Pa.), *aff'd*, 52 Bankr. 997 (W.D. Pa. 1985), *vacated*, 791 F.2d 1074 (3d Cir. 1986). This was the first case involving a dispute over the application of § 1113 to be heard by a circuit court of appeals.

cases utilized these standards,⁶⁸ but also illustrate the conflicting interpretations of section 1113 by various courts which, until the Third Circuit decision, had unions asking: Has section 1113 *really* changed *Bildisco*?

III. ANALYSIS

A. *First Stabs: Interpreting Section 1113 in American Provision and Wheeling-Pittsburgh*

*American Provision*⁶⁹ was the first case to be decided after the enactment of section 1113. American Provision, the debtor-in-possession, sought to reject a collective bargaining agreement with members of the Miscellaneous Drivers, Helpers, and Warehouseman's Union, which was approximately eight months from expiration, and which affected a total of two employees.⁷⁰

Judge Kressel of the Bankruptcy Court for the District of Minnesota refused to permit rejection, holding that the debtor had failed to show that rejection was necessary for reorganization, and that its attempts to negotiate with the union were inadequate.⁷¹ In arriving at his decision, Judge Kressel attempted to set forth a guideline for interpretation of the new legislation:

While § 1113 is not a masterpiece of draftsmanship, I think nine requirements for court approval of the rejection of collective bargaining agreements can be gleaned from § 1113.

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

68. See *supra* note 66. The first case to follow the decision in *American Provision* was *In re Salt Creek Freightways*, 47 Bankr. 835 (Bankr. D. Wyo. 1985). In *Salt Creek*, the United States Bankruptcy Court for the District of Wyoming permitted rejection of a contract with the International Brotherhood of Teamsters, Chauffeurs, Warehousemen, and Helpers of America, holding that: (1) the modifications proposed were only those necessary to a successful reorganization, (2) the debtor provided the union with all information necessary to evaluate the debtor's proposal, (3) the debtor had bargained in good faith, (4) the union rejected the debtor's proposal without good cause, and (5) the equities favored rejection. *Id.* at 838-41. The decision in this case was based upon a careful analysis of the *American Provision* nine-point test.

69. *American Provision*, 44 Bankr. at 907.

70. *Id.* at 910 n.3.

71. *Id.* at 910-11.

2. The proposal must be based on the most complete and reliable information available at the time of the proposal.
3. The proposed modifications must be necessary to permit the reorganization of the debtor.
4. The proposed modifications must assure that all creditors, the debtor and all of the affected parties are treated fairly and equitably.
5. The debtor must provide to the Union such relevant information as is necessary to evaluate the proposal.
6. Between the time of the making of the proposal and the time of the hearing on approval of the rejection of the existing collective bargaining agreement, the debtor must meet at reasonable times with the Union.
7. At the meetings the debtor must confer in good faith in attempting to reach mutually satisfactory modifications of the collective bargaining agreement.
8. The Union must have refused to accept the proposal without good cause.
9. The balance of the equities must clearly favor rejection of the collective bargaining agreement.⁷²

Judge Kressel also attempted to set forth some standard for the allocation of burdens of persuasion and going forward, indicating that although section 1113 “does not discuss the burden of proof of showing that the requirements have been met . . . it seems to me that . . . the debtor bears the burden of persuasion by the preponderance of the evidence on all nine elements.”⁷³ The judge realized, however, that the burden of going forward with the evidence is not in all instances on the debtor, and that the assignment of the initial burden of production always should depend upon the circumstances.⁷⁴

Approximately seven months after the decision in *American Pro-*

72. *Id.* at 909.

73. *Id.*

74. *Id.*

vision, the bankruptcy court for the Western District of Pennsylvania was faced with applying section 1113 to a rejection request on a much larger scale in *In re Wheeling-Pittsburgh Steel Corp.*⁷⁵ Wheeling-Pittsburgh, the seventh largest steel manufacturer in the United States, filed its petition for relief under Chapter 11 of the Bankruptcy Code on April 16, 1985.⁷⁶ On May 31 of the same year, the company filed its motion to reject its collective bargaining agreements with the United Steelworkers of America. These agreements had thirteen months to run, and affected approximately 8,500 of the company's employees.⁷⁷

In ruling on the application for rejection, the bankruptcy court carefully considered the history of the company's collective bargaining agreements with the union, as one of the union's major contentions was that in light of several prior wage and benefit concessions obtained by the company, the company's present proposals were unreasonable and unnecessary to achieve reorganization.⁷⁸ In reaching his decision

75. 50 Bankr. 969 (Bankr. W.D. Pa.), *aff'd*, 52 Bankr. 997 (Bankr. W.D. Pa. 1985), *vacated*, 791 F.2d 1074 (3d Cir. 1986).

76. *Id.* at 973. The company, which had commenced a major capital investment program for modernization in the late 1970s, was hit hard by the deteriorating condition of the American steel industry. As the modernization effort had required the company to borrow heavily (spending \$540 million between 1980-1985 to meet customer service demands), these loans, "combined with 'significant 1982, 1983 and 1984 losses . . . substantially weakened the corporation's financial position.'" *Id.* The particular plight of the American steel industry was a major factor considered by the court in rendering its decision. *Id.* at 983-84. *See also infra* note 81 and accompanying text.

77. *Wheeling-Pittsburgh*, 50 Bankr. at 973-74.

78. *Id.* at 973-74. The company had obtained several prior concessions from the union hoping to weather its increasing financial difficulties. In 1980-1981, the company asked for and was granted certain concessions from its Allenport plant employees. In 1982, after consulting with its financial experts, the company asked for further concessions, obtaining one in April and the second in December. The second of these was made as part of a new 3 1/2 year bargaining agreement scheduled to expire on July 31, 1986. These concessions reduced average labor costs to \$18.60 per hour, which were to be restored during the life of the agreement to the level of \$25 per hour. By the end of 1984, there had been restorations to \$21.40 per hour. In November of 1984, due to worsening financial conditions, Wheeling-Pittsburgh asked the union to cancel anticipated restorations above \$21.40. The union agreed to defer restorations indefinitely, subject to reimposition on short notice, after financial experts confirmed the company's worsening condition. *Id.* at 973.

In January 1985, the company asked for further concessions. The union refused unless the company first secured concessions from its lenders. The company then issued a three-prong restructuring proposal (known as the "three-legged stool") on March 8, 1985, which sought concessions from the union, lenders, and shareholders.

to permit rejection, Judge Bentz adopted the nine point test of *American Provision*,⁷⁹ as well as Judge Kressel's view of the allocation of burdens.⁸⁰ He concluded that the union had failed to accept the proposed modifications without good cause, and that rejection of the agreements would have a significant positive effect on the company's prospects for reorganization.⁸¹ Notably, Judge Bentz, in discussing several points of the *American Provision* analysis,⁸² offered interpretations of certain terms of section 1113 which appeared to be less strict than the unions had hoped.⁸³ In arriving at the meaning of "good faith" within the context of section 1113,⁸⁴ Judge Bentz rejected the interpretation usually given "good faith" in labor law, adopting instead, the "good faith" standard set forth in *Bildisco*.⁸⁵ The judge also rejected the union's contention that "fair and

As a *quid pro quo* for making its concessions, the lenders insisted upon Wheeling-Pittsburgh's pledge of its current assets to secure its old debt. The union insisted, as a condition to concession, that the company not pledge its current assets as collateral for old debt. Due to these opposing demands, the restructuring program failed and, shortly thereafter, the company filed its Chapter 11 petition. *Id.* at 973-74.

79. See *supra* text accompanying note 72.

80. See *supra* text accompanying notes 73-74.

81. *Wheeling-Pittsburgh*, 50 Bankr. at 979, 983. The court stated:

Rejection of the Company's collective bargaining agreements will have a significant and positive effect on Wheeling-Pittsburgh's prospects for reorganization. Wheeling-Pittsburgh is in this bankruptcy proceeding because of substantial and continuing losses. These losses appear to be the result of weak demand, weakening prices, foreign competition, and an excess of industry-wide capacity as compared with demand. There is very little the Company can do to reduce non-labor costs. The result is that either the labor costs are reduced or the losses will continue. Present labor costs are simply above the Company's ability to pay. This situation of financial distress is not the fault of either party. But the inescapable fact is that the continuing losses must be stopped if the Company is to reorganize.

Id. at 983-84. See also *supra* note 76.

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

83. See Brief for Appellant at 31, *Wheeling-Pittsburgh Steel v. USWA*, 791 F.2d 1074 (3d Cir. May 28, 1986) [hereinafter Appellant's Brief].

84. 11 U.S.C. § 1113(b)(2).

85. The court interpreted the "good faith" standard of § 1113(b)(2) not in the strict sense that the union urged but in keeping with the "spirit" of *Bildisco*. Relying for its interpretation upon what the court referred to as § 1113's "scant" legislative history, it took into consideration the following comments on § 1113 made by Senator Hatch: "[G]ood faith negotiations between the parties . . . was a requirement articulated by the Supreme Court in the *Bildisco* case. The conference, once again, preserved the spirit of that Court holding by requiring good faith efforts to confer in an effort to reach an agreement between the business and its union

equitable"⁸⁶ treatment must insure equal treatment for all parties, pointing out that the legislative intent of "fair and equitable" was merely to guarantee that the cost-cutting focus not be directed exclusively at the union workers.⁸⁷ Thus, although one party may not be singled out to bear the financial brunt of the reorganization, "[f]air and equitable treatment does not of necessity mean identical or equal treatment."⁸⁸ Also considered was the interpretation to be given the word "necessary" as used in the phrase "necessary to permit reorganization."⁸⁹ Here Judge Bentz disagreed with the union's contention that the phrase required absolute necessity, concentrating more upon the long range necessity of ensuring a successful reorganization.⁹⁰

In rendering these interpretations, Judge Bentz made a substantial addition to the section 1113 interpretation begun by Judge Kressel in *American Provision*.⁹¹ Considering the relative leniency of

employees.' " *Wheeling-Pittsburgh*, 50 Bankr. at 976 (quoting 130 CONG. REC. S8892 (daily ed. June 29, 1984)).

The court then looked to the language of *Bildisco* to which Senator Hatch referred to arrive at its interpretation of the "good faith" requirement of § 1113(b)(2): "Before acting on a petition to modify or reject a collective bargaining agreement, . . . the Bankruptcy Court should be persuaded that *reasonable efforts to negotiate a voluntary modification have been made* and are not likely to produce a prompt and satisfactory solution . . . that court need not determine that the parties have bargained to impasse or make any other determination outside the field of its expertise."

Id. (quoting *Bildisco*, 465 U.S. at 526-27 (emphasis added)).

86. *Wheeling-Pittsburgh*, 50 Bankr. at 975-76.

87. *Id.* at 979. Looking again to § 1113's legislative history, the court carefully considered Senator Packwood's description of the intent of the "fair and equitable" language: "This language guarantees that the focus for cost-cutting must not be directed exclusively at unionized workers. Rather the burden of sacrifices in the reorganization process will be spread among all affected parties.'" *Id.* at 979-80 (quoting 130 CONG. REC. S8898 (daily ed. June 29, 1984)).

88. *Wheeling-Pittsburgh*, 50 Bankr. at 980 (citations omitted).

89. 11 U.S.C. § 1113(b)(1)(A).

90. *Wheeling-Pittsburgh*, 50 Bankr. at 978. See also *Wheeling-Pittsburgh*, 52 Bankr. at 997.

91. Prior to the recent Third Circuit decision in *Wheeling-Pittsburgh*, the question of the proper construction of § 1113 was faced by bankruptcy courts in other districts. In *In re Carey Transp.*, 50 Bankr. 203 (Bankr. S.D.N.Y. 1985), the bankruptcy court for the Southern District of New York authorized rejection of a collective bargaining agreement with drivers and station personnel of Carey's bus line which provided service between JFK and La Guardia Airports and New York City. Authorization to reject was based upon the fact that the proposed modifications were necessary, and treated all parties fairly. *Id.* at 209-11.

In *In re Cook United, Inc.*, 50 Bankr. 561 (Bankr. N.D. Ohio 1985), the

these interpretations, the first decision in *Wheeling-Pittsburgh* understandably raised doubts in the minds of union forces as to whether section 1113 could actually provide the anti-rejection safeguards they had expected.

B. Wheeling-Pittsburgh: *The District Court Opinion*

On appeal to the district court, the union argued that the collective bargaining agreement modifications proposed by the company were not necessary to permit the reorganization of the debtor and that, even if some modification was necessary, that sought by the company was "unduly drastic and unworkable."⁹² The district court concluded that although it may not have made the same findings of fact as the bankruptcy court, it found no clearly erroneous application or interpretation of section 1113 which would merit reversal.⁹³ In affirming the bankruptcy court's decision, the district court agreed with Judge Bentz's conclusion that the "necessary" standard of section 1113 does not mean "absolutely essential" as the union contended on appeal.⁹⁴ This apparent discrepancy in the interpretation of the term "necessary" as found in section 1113(b)(1)(A) remained the point of dissension between the union and the debtor corporation on appeal in *Wheeling-Pittsburgh*.⁹⁵ The Third Circuit's decision will have great precedential value for similar cases in the future, and has, in large part, answered the question: Has section 1113 *really* changed *Bildisco*?

C. *The Third Circuit Opinion*

On appeal to the Third Circuit, the union argument centered upon the district court's interpretation of and decision regarding four of the nine factors of the rejection test set forth in *American Provision*.⁹⁶

bankruptcy court for the Northern District of Ohio came to the opposite conclusion on the same points, denying the debtor's petition to reject. The court held that Cook (a department store chain) had failed to demonstrate that the equities favored rejection, and that the modifications were necessary to permit reorganization. *Id.* at 563.

92. *Wheeling-Pittsburgh*, 52 Bankr. at 1001.

93. *Id.* at 1003.

94. *Id.*

95. *But see supra* note 13.

96. *See supra* note 72 and accompanying text. The union on appeal took to task the district court's interpretation of points 3, 4, 5, and 7 of the nine-point test enunciated in *American Provision*. Appellant's Brief, *supra* note 83, at 18-19.

The union alleged three points of error and urged that adoption of any of these points would require reversal of the decisions below.⁹⁷ The first point contended by the union was that the company did not prove that any relief from the collective bargaining agreement was necessary to permit reorganization,⁹⁸ because according to the company's own projections, based on worst-case assumptions,⁹⁹ it could complete the remaining thirteen months of the agreement and still have the cash necessary to operate.¹⁰⁰ Although the district court's permission to reject was based largely on the fact that such compliance with the agreement would be inherently unfair to creditors,¹⁰¹ the union contended that unfairness, as a matter of law, does not qualify as a necessity to reorganization under section 1113.¹⁰²

The union further contended that even if some modification to the agreement was deemed necessary, the company's proposals were too overreaching, as these were based upon worst-case assumptions¹⁰³ and provided no "snap-back" provision¹⁰⁴ should the worst-case

97. See Appellant's Brief, *supra* note 83, at 19-22.

98. See *id.* at 19.

99. See *id.* at 19-21. The union urged that the company's proposed modifications, based as they were upon worst possible case assumptions regarding the company's future, could never be justified as necessary. This was especially true, the union contended, as there was no "snap-back" provision included to restore portions of concessions granted should the worst case assumptions prove overly pessimistic. *Id.* at 19. Thus, the union concluded:

The effect of these interrelated provisions is that, unless the worst-case eventuates, a pool of money will be generated — out of the hides of the employees — that is not necessary to permit reorganization and that will inure to the benefit of the company (i.e. the shareholders), the unsecured creditors, or both.

Id. at 21.

100. Although the company did not preclude the possibility that it might have the cash to ride out the remaining 13 months of the then-current collective bargaining agreement, it argued that such an arrangement might so deplete the cash flow as to prompt creditors to opt for liquidation. This was a point with which the lower courts agreed. See *Wheeling-Pittsburgh*, 50 Bankr. at 984; *Wheeling-Pittsburgh*, 52 Bankr. at 1007.

101. See Appellant's Brief, *supra* note 83, at 34-35.

102. See *id.* In support of this proposition, the union offered the following quote from 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, 338 (1984): "[M]odifying a labor contract to build a larger pool for creditors 'without the justification of helping to keep the firm in business, unnecessarily and unjustly subordinates the interests of the workers to the other creditors and is an improper use of Section 1113.'" *Id.* at 34.

103. Appellant's Brief, *supra* note 83, at 21, 37. See also *supra* note 99 and accompanying text.

104. See Appellant's Brief, *supra* note 83, at 21, 37.

assumptions prove too pessimistic during the five-year life of the new agreement.¹⁰⁵ The last point put forth by the union centered upon its claim that even if the company's proposal met the substantive requirements of section 1113, the company failed to satisfy the negotiating prerequisites.¹⁰⁶ Here, the union asserted that the company failed to furnish information necessary to evaluate the proposal, as well as to confer in good faith to reach mutually satisfactory modifications of the existing agreement.¹⁰⁷

In vacating the district court's order, the court of appeals first dismissed the mootness argument put forth by the principal bank creditors.¹⁰⁸ The court then turned to a consideration of the issues raised by the union. It first dismissed the union's contention that the bankruptcy court erred in even evaluating Wheeling-Pittsburgh's proposal under section 1113.¹⁰⁹ The court then turned to the question of the "necessity" standard of section 1113. Relying heavily upon the legislative history of the section,¹¹⁰ the court concluded that the

105. *See id.*

106. *See id.* at 21.

107. *See id.* at 21-22.

108. *Wheeling-Pittsburgh*, 791 F.2d at 1074. The bank creditors argued that the appeal was moot because, under the new collective bargaining agreement between Wheeling-Pittsburgh and the USWA, the outcome of this appeal would have no substantial effect on the parties' positions. *See supra* note 13. However, the court noted that as this appeal involved \$146,000 in possible back pay for plant guards who had continued to work during the July 21-October 15, 1985 strike, a controversy did indeed exist to merit appeal. The court stated: "All parties acknowledge that if Wheeling-Pittsburgh does not prevail on appeal, it will be required to pay the \$146,000 as an administrative expense. That sum is not de minimis for any company, and particularly not for a bankrupt one." *Wheeling-Pittsburgh*, 791 F.2d at 1079. In dismissing the mootness claim, Judge Sloviter also pointed out that the union's counsel had apparently told the company's counsel that if an offer were made in the disputed amount, the union would accept, even if this appeal were rendered moot. *Id.* She continued to note that even though the union admitted an interest in the precedential value of this case, this point did not render the case moot where there were "in fact, stakes at issue." *Id.* at 1080.

109. *Wheeling-Pittsburgh*, 791 F.2d at 1084-85. The union alleged that under the facts of the case, Wheeling-Pittsburgh could have continued to operate for the remaining 13 months of the collective bargaining agreement. On these facts, the union contended that no modification was "necessary," and that this was a conclusion which should have been reached by the bankruptcy court. In dismissing this contention, the court of appeals pointed out that § 1113 does not require such a preliminary determination, other than those provided for under § 1113(e) which provides for court-authorized interim contract changes where "essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate." *Id.* at 1085. However, this was not the applicable provision in the instant case.

110. In considering the legislative history, the court noted the support of labor for the Packwood Amendment to the bill, which required that a trustee's (debtor's)

bankruptcy court had applied an incorrect, and far too lenient, standard of necessity which echoed *Bildisco* and ignored legislative intent.¹¹¹ It also stressed the district court's error in treating the bankruptcy court's findings of "necessity" as factual findings, subject only to "clearly erroneous" review.¹¹² This finding of "necessity," the court noted, should have been reviewed by the district court as a mixed question of law and fact.¹¹³ In its examination of the legislative and caselaw history of section 1113, the court stressed that the "necessity" standard should be stricter than that applied by the bankruptcy court, permitting only the " 'minimum modifications . . . that would permit the reorganization.' "¹¹⁴ The court noted that emphasis should be more strongly placed upon the short-term reorganizational goals, rather than on the "long-term economic health of the debtor."¹¹⁵ This stricter standard is reflected in the language of the court: "We reject the hypertechnical argument that 'necessary' and 'essential' have different meanings because they are in different subsections. The words are synonymous."¹¹⁶ The court also stated that the legislative history of section 1113 "illuminates two aspects of the court's inquiry into necessity: (1) the standard to be applied, i.e., 'how necessary' must the proposed modifications be, and (2) the object of the 'necessary' inquiry, i.e., 'necessary to what' "¹¹⁷ From the court's discussion of these questions, it appears that the answer to "how necessary" is essential,¹¹⁸ and that the answer to "necessary to what" is (a) short-term reorganization and (b) the fair and equitable treatment of all affected parties.¹¹⁹

The court then turned its attention to the question of how "fair and equitable" the proposed modifications were. In holding that the proposed modifications were not "necessary" and were not in ac-

proposal make the "minimum modifications in [the] employees' benefits and protections that would permit the reorganization." *Id.* at 1087. For this amendment, the conference committee substituted the clause "for those necessary modifications in the employees' benefits and protections that are necessary to permit the reorganization of the debtor." *Id.* This standard was seen as a victory for labor. *Id.*

111. *Id.* at 1090-91.

112. *Id.* at 1091.

113. *Id.*

114. *Id.* at 1088.

115. *Id.* at 1089.

116. *Id.* at 1088.

117. *Id.*

118. *Id.*

119. *Id.* at 1089.

cordance with the fair and equitable standard,¹²⁰ the court relied heavily upon the argument offered by the union which assailed the modification for its lack of "snap-back" provisions, and the fact that it was based on worst-case assumptions.¹²¹ Although the union found no fault with the bankruptcy court's articulation of the standard of fair and equitable as a proposal which would not impose a disproportionate burden on the employees,¹²² the union did allege a misapplication of the standard in this case.¹²³ The court agreed, holding that the proposed five-year modified contract, which provided for no wage increases for union employees should the company fare better than the worst-case assumptions on which the proposal was based, would benefit the creditors and burden the employees should the worst case projections prove overly pessimistic.¹²⁴ The company had contended that the proposal did not provide for any *downward* adjustment in the event of continued losses, heralding this factor as a "wage stability" feature which should clear the "fair and equitable" hurdle, as workers would not be subject to further pay decreases regardless of the health of the business. The court rejected this argument, stating "[T]he workers did not ask for or need 'wage stability' at a rate they considered substandard. Therefore, such 'stability' cannot be considered to be a benefit to them to compensate for the absence of any share of better-than-anticipated recovery."¹²⁵

Finally, the court considered the union's claim that the bankruptcy court erred in its ruling that *Wheeling-Pittsburgh* satisfied the procedural elements of section 1113.¹²⁶ This claim centered upon the union's contention that it was given neither adequate time nor

120. *Id.* at 1090. The court noted that the bankruptcy court erred in that its discussion of "necessity" did not contain a consideration of the "snap-back" issue. The court stated:

The court [bankruptcy] confined its consideration of the absence of a "snap back" provision to its discussion of the second prong of the standard, whether the proposal treated all affected parties "fairly and equitably." In failing to focus on the Union's contention about the "snap back" provision when deciding whether the modifications were "necessary," the bankruptcy court erroneously treated the two prongs of the standard as disjunctive rather than conjunctive.

Id.

121. *Id.* at 1091.

122. *Id.*

123. *Id.*

124. *Id.* at 1093.

125. *Id.* at 1092-93.

126. *Id.* at 1093.

information to consider the proposal.¹²⁷ Although the court made no determination that the bankruptcy court's finding was clearly erroneous, it noted that "the need for haste in itself" may not always support a finding that a company has met its negotiating requirement.¹²⁸ An emergency situation requiring undue haste, the court stated, is provided for in section 1113(e), under which Wheeling-Pittsburgh did not apply. In concluding, the court directed that this issue be reconsidered on remand to the bankruptcy court.¹²⁹

V. WHERE TO FROM THE THIRD CIRCUIT?: WILL ANY BE SO BOLD AS TO ELECT TO REJECT?

The fears engendered by the decision in *Bildisco* were thought to have been assuaged by the enactment of section 1113, for it was believed that the procedural and substantive guidelines which this section required prior to rejection would preclude many "unnecessary" and arbitrary rejections by Chapter 11 debtors. However, prior to the Third Circuit's reversal in *Wheeling-Pittsburgh*, labor believed section 1113's effect was illusory at best, dependent as it was in large part upon any one court's interpretation of such key terms as "necessary." As is evident from the Third Circuit's decision in *Wheeling-Pittsburgh*, the trend may be towards a stricter application of the "necessity" standard, as well as a focus on the short-term, as opposed to long-term, stability of the Chapter 11 debtor.

Prior to the court of appeals' decision, the courts' consideration of the necessity standard in *Wheeling-Pittsburgh* focused on a long-range necessity standard which emphasized the ultimate goal of Chapter 11 reorganization. In its opinion, the district court in *Wheeling-Pittsburgh* stressed the belief that its interpretation of the "necessary" standard of section 1113 reflected the congressional intent:

[W]e agree with Judge Bentz's conclusion that the necessary" standard of § 1113 does not mean "absolutely essential" as the USWA contend here. A more practical long range test of a less stringent nature is more compatible with congressional intent where the emphasis in § 1113(b)(1)(A)

127. *Id.* The union was given three weeks in which to consider the company's proposal. The bankruptcy court found this period "not inherently unreasonable." *Id.* (quoting *Wheeling-Pittsburgh*, 50 Bankr. at 976).

128. *Id.* at 1093-94.

129. *Id.* at 1094.

is upon the reorganization of the debtor and the fair and equitable treatment of all creditors, the debtor and all affected parties. The prevention of the debtor going into liquidation, ensuring the loss of jobs, is a goal and policy decision of the Bankruptcy Code which indicates an intent of Congress to impose a "necessary" standard to be satisfied by considerations of feasibility for reorganization.¹³⁰

The union, on the other hand, contended that a stricter "but for" necessity standard was closer to what Congress intended, citing as support the explanation of section 1113(b)(1)(A)'s statutory language offered by Representative Morrison, who was its co-author: "This language makes plain that the [debtor] must limit his proposal to modify a collective bargaining agreement to *only* those modifications that *must* be accomplished if the reorganization is to succeed. The key phrase is '*necessary*' modifications."¹³¹ Such strict interpretation would permit rejection only where, without it, reorganization could not succeed. Such interpretation, the union argued, is reflected as correct upon an examination of section 1113's legislative history.¹³² In support of its strict necessity argument, the union also relied upon the decision in *In re Fiber Glass Industries, Inc.*¹³³ where the court held that a showing of severe financial difficulty would not merit rejection under such a strict "but for" standard.¹³⁴ Under this strict necessity test, the union concluded that Wheeling-Pittsburgh's application for rejection "foundered at the threshold," as no modification of the existing agreement was necessary at the outset.¹³⁵

The crux of the union's appeal in light of the first two decisions in *Wheeling-Pittsburgh* was that such cases present a conflict between the long-term reorganization goals of Chapter 11 and the particular procedural standards set forth in section 1113. The difficulties in reconciling these objectives stem in large part from the difficulties which a debtor-in-possession faces in attempting to propose modifications to the existing agreement which will both permit reorgan-

130. *Wheeling-Pittsburgh*, 52 Bankr. at 1003.

131. Appellant's Brief, *supra* note 83, at 25.

132. *See id.*

133. 49 Bankr. 202 (Bankr. N.D.N.Y. 1985).

134. *Id.* at 208. The court stated: "Merely demonstrating a resultant savings to the debtor to justify a modification does not appear to meet the statutory standard without the additional showing that but for this particular savings reorganization cannot be achieved." *Id.* at 206.

135. *See* Appellant's Brief, *supra* note 83, at 26.

ization and meet with the approval of the union. This task oftentimes proves a difficult one for a company in dire financial straits which must make countless projections in a short period of time.¹³⁶ Such problems become more apparent when dealing with a company as large as Wheeling-Pittsburgh; for although courts may be reluctant to authorize rejection where the effect upon reorganization is minimal,¹³⁷ they might be more likely to apply a less stringent rejection test and necessity standard where the effects will be more pronounced.

Prior to the Third Circuit's decision, the courts appeared to have taken a patriarchal view, urging both sides to settle their differences for the greater goal of a common good: the survival of the company. Such sentiment was enunciated by the district court:

In actuality, this is not a typical adversary proceeding but rather a tense and imperative struggle for the survival of a company and the preservation of jobs generated by that company's normal operations. The Company and Union are both in the same boat faced with a serious and common problem that may well sink all who are aboard, including the equity holders and lenders. The response to the problem cannot be unfairly shifted to one group while the others sit by with a nonchalant claim of a preferred interest. The response needed is for all to bail water, pull together, throw overboard that portion of the heavy cargo that can be sacrificed, head for safe ground and try to weather the storm with the hope that all will not be lost. This is really what is involved and must be faced when a debtor in possession in Chapter 11 seeks to survive in the business world by a reorganization plan. Congress entrusted the supervision of the plan to the Bankruptcy Court and Congress cannot be charged with taking sides by setting standards which favor one of the boat's occupants over another.¹³⁸

136. See, e.g., Note, *What Does Congress Intend?*, *supra* note 9, at 720.

137. Although many factors distinguish the two cases, *American Provision* and *Wheeling-Pittsburgh* are excellent examples of how a court's interpretation of rejection standards might be influenced by the magnitude of the effect that will result. Whereas *American Provision's* collective bargaining agreement affected only two employees and if rejected would save the company \$1,185 per month; *Wheeling-Pittsburgh's* agreements affected over 8,500 employees, and rejection, so the lower courts believed, would save the company from an untimely liquidation. See *supra* notes 70, 76, & 81 and accompanying text.

138. *Wheeling-Pittsburgh*, 52 Bankr. at 1004.

Despite the seemingly well-reasoned conclusions of the lower court decisions, the Third Circuit's "hard line" construction of the "necessary" standard and its painstaking review of the "fair and equitable" requirement may well be interpreted as providing some degree of clarification in the evolving interpretations of section 1113.¹³⁹ However, it might as easily be argued that the precedential value will be, by and large, limited to the facts of the case.¹⁴⁰ The decision of the Third Circuit appears to be the death knell for future Chapter 11 debtors seeking to reject collective bargaining agreements. Such concerns seem valid when one considers two particular points made by the court: first, that "necessary" may be construed as "essential,"¹⁴¹ and second, that all emphasis should be on the short-term reorganization, as opposed to long-term recovery.¹⁴² Although in many cases such strict construction of section 1113 might be merited,¹⁴³ in light of the size of Wheeling-Pittsburgh as well as the general malaise of the steel industry, it might be argued that public policy considerations should play some role in determining how strictly section 1113 should be construed.¹⁴⁴ The Third Circuit seemed to be rather oblivious to these concerns recognized by the lower courts.¹⁴⁵ Although, for example, the Court did state, "[W]e do not suggest that the general long-term viability of the Company is not a goal of the debtor's reorganization,"¹⁴⁶ the court did stress shorter term

139. The rather extensive consideration given by the Third Circuit to the legislative history of § 1113 may well serve to bolster the case as a guide to interpretation of the section.

140. This argument might be based on the fact that the Wheeling-Pittsburgh proposal was based on a worst-case scenario, over a five year period, with no "snap-back" provision to upgrade wages should the company fare better. Although these facts *might* arise in another situation, these three factors seemed to be those which the court found so inequitable as to unduly burden employees.

141. *Id.* at 1088.

142. *Id.* at 1089.

143. Such a strict construction is necessary, in many cases, to prevent abuses of the rejection option.

144. Such a concern was illustrated by Judge Bentz of the bankruptcy court, who stated:

It is apparent, and all parties must recognize, that the steel industry is in deep financial trouble, that this Company is in deep financial trouble, that the overcapacity in the industry may force some steel producers out of business, and that this Company may be forced into liquidation in the competitive process of reducing industry-wide capacity.

Wheeling-Pittsburgh, 50 Bankr. at 984.

145. See *supra* text accompanying notes 138, 144.

146. *Wheeling-Pittsburgh*, 791 F.2d at 1089.

goals, rather than considering such possibilities as the avoidance of liquidation.¹⁴⁷

Although it is not suggested that section 1113 be twisted in various directions with each case that arises, it is evident that different considerations should be stressed by the courts in such cases as *Wheeling-Pittsburgh* where the debtor is large, in a troubled industry, and where the possibility of liquidation is distinct.¹⁴⁸ To ignore such considerations may be to throw employees from the fire of wage-cuts into the frying pan of permanent unemployment.

VI. CONCLUSION

With the enactment of section 1113 came hopes that mutually satisfactory modifications in collective bargaining agreements could be reached through the combined efforts of the debtor and labor. It was expected that section 1113 would banish forever the unilateral rejection philosophy of *Bildisco* by permitting rejection only after negotiations had failed and after a strict necessity test was met. Until the recent decision in *Wheeling-Pittsburgh*, caselaw had union leaders seriously pondering the question, "Has section 1113 *really* changed *Bildisco*?" Labor may now be hopeful that section 1113 will bring the promised relief from rash rejections. The true precedential value of the Third Circuit decision will only become clear as subsequent courts attempt to unscramble the degrees of dos and don'ts embodied in section 1113. Though labor may be revelling now in the Third Circuit's response to the question, Has section 1113 *really* changed *Bildisco*? the recent decision no doubt has many financially troubled companies fearing they may never grasp the brass ring of economic recovery.

Marcia J. Massco

147. See *supra* note 144.

148. See *supra* note 140 and accompanying text.