

# Collective Bargaining Agreements and Chapter 9 Bankruptcy

by

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## I. INTRODUCTION

Collective bargaining agreements (CBAs) featured prominently in the recent wave of automotive and aviation bankruptcies. Collective bargaining obligations that seemed reasonable during the irrational exuberance of the 1990s became increasingly untenable under shifting market conditions and unfavorable workforce demographics. The combination of inefficient labor costs, unaffordable legacy benefits, increased market competition, and outright mismanagement pushed more than one company into bankruptcy. Not surprisingly, debtors such as United Airlines,<sup>1</sup> Delta Air Lines,<sup>2</sup> Northwest Airlines,<sup>3</sup> Tower Automotive,<sup>4</sup> Delphi,<sup>5</sup> and Dana Corporation<sup>6</sup> have used rejection or the threat of rejection to obtain significant concessions from their unions. A debtor's ability to rid itself of burdensome contractual obligations is one of the fundamental virtues of bankruptcy.<sup>7</sup>

The difficulties created by unmanageable CBAs are not limited to the private sector. Public sector unions have successfully obtained comparatively

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<sup>1</sup>See generally *In re UAL Corp.*, 468 F.3d 456 (7th Cir. 2006); *In re UAL Corp.*, 443 F.3d 565 (7th Cir. 2006); *In re UAL Corp.*, 408 F.3d 847 (7th Cir. 2005) (discussing United Airlines' efforts to reject its CBAs).

<sup>2</sup>*In re Delta Air Lines, Inc.*, 359 B.R. 468 (Bankr. S.D.N.Y. 2006); *In re Delta Air Lines, Inc.*, 351 B.R. 67 (Bankr. S.D.N.Y. 2006); *In re Delta Air Lines, Inc.*, 342 B.R. 685 (Bankr. S.D.N.Y. 2006).

<sup>3</sup>*In re Northwest Airlines Corp.*, 346 B.R. 307 (Bankr. S.D.N.Y. 2006).

<sup>4</sup>Official Comm. of Unsecured Creditors v. Tower Auto., Inc. (*In re Tower Auto., Inc.*), 241 F.R.D. 162 (S.D.N.Y. 2006) (discussing settlement agreement between debtor and unions negotiated in lieu of rejection).

<sup>5</sup>Motion for Order Under 11 U.S.C. § 1113(c) Authorizing Rejection of Collective Bargaining Agreements and Under 11 U.S.C. § 1114(g) Authorizing Modification of Collective Bargaining Agreements, *In re Delphi Corp.*, No. 05-44481 (Bankr. S.D.N.Y. Mar. 31, 2006), available at <http://www.delphidocket.com/Docket/SearchResults.asp?SH=1>; Jeremy W. Peters, *U.A.W. Votes to Authorize Strike at Delphi*, N.Y. TIMES, May 17, 2006, at C2 (discussing United Auto Workers' decision to strike if Delphi sought rejection of its CBAs).

<sup>6</sup>Dana's motion to reject its CBAs was filed under seal. See *In re Dana Corp.*, No. 06-10354 (Bankr. S.D.N.Y. Jan. 31, 2007), available at [http://docs.bmccorp.net/dana/docs/nysb\\_1-06-bk-10354\\_4672\\_0.pdf](http://docs.bmccorp.net/dana/docs/nysb_1-06-bk-10354_4672_0.pdf).

<sup>7</sup>11 U.S.C. §§ 365, 1113 (2006).

generous compensation and benefits packages even as the fortunes of American labor have continued to decline.<sup>8</sup> In particular, municipal pensions may jeopardize the fiscal survival of many public sector employers.<sup>9</sup> This dark forecast is further clouded by the increased probability of a near-term recession.<sup>10</sup>

Municipalities throughout the United States will face the very real prospect of bankruptcy.<sup>11</sup> The treatment of CBAs will play a significant role in this process. Obligations imposed through collective bargaining (generally referred to as Memoranda of Understanding (MOUs) in the context of public labor relations), may be the efficient cause of such filings. Such was the case when Bridgeport, Connecticut, attempted to file for bankruptcy in 1995 or when the San José Unified School District filed for bankruptcy in 1983.<sup>12</sup> Alternatively, the modification of an MOU may simply be the most effective means to restore the financial health of a municipality.<sup>13</sup> Typically, sixty to seventy percent of all municipal expenditures cover labor-related costs.<sup>14</sup> In any event, bankruptcy may be a necessary solution for municipal debtors burdened by untenable CBAs or insurmountable fiscal obligations.<sup>15</sup>

Statutory gaps, the absence of case law, and limited commentary raise serious questions as to how courts should treat CBAs in municipal bankruptcies.<sup>16</sup> The affairs of municipal debtors are governed by Chapter 9 of the

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<sup>8</sup>See generally Terry M. Moe, *Political Control and the Power of the Agent*, 22 J.L. & ECON. & ORG. 1, 5 (2006) ("It is the public sector unions, not the private sector unions, that are now driving the American labor movement." (internal citations omitted)); Keith N. Hylton, *Law and the Future of Organized Labor in America*, 49 WAYNE L. REV. 685 (2003).

<sup>9</sup>See, e.g., 1 STATE OF ILLINOIS, OFFICE OF THE AUDITOR GENERAL, Executive Summary of Performance Audit, Mass Transit Agencies of Illinois: RTA, CTA, Metra and Pace 37 (2007) (projecting actuarial liabilities for Chicago Transit Authority pension plan of approximately \$4.0BN by 2009); Mary Williams Walsh, *N.J. Pension Fund Endangered by Diverted Billions*, N.Y. TIMES, Apr. 4, 2007, at A1.

<sup>10</sup>See Edmund L. Andrews, *Few Expect Panacea in a Rate Cut By the Fed*, N.Y. TIMES, Sep. 3, 2007, at C1 (questioning the Federal Reserve Bank's ability to avoid a near-term recession via rate cuts).

<sup>11</sup>The Supreme Court has recently addressed one particularly novel way to stave off municipal collapse. See *Kelo v. City of New London*, 545 U.S. 469 (2005).

<sup>12</sup>*In re City of Bridgeport*, 129 B.R. 332, 339 (Bankr. D. Conn. 1991) ("Bridgeport claims that it is caught in an economic bind caused, on the one hand, by unaffordable employee union contracts and inadequate state aid and, on the other, by the practical reality that it can neither cut essential services nor raise taxes to pay for them."); Barry Winograd, *San José Revisited: A Proposal for Negotiated Modification of Public Sector Bargaining Agreements Rejected Under Chapter 9 of the Bankruptcy Code*, 37 HASTINGS L.J. 231 (1985) (discussing the San José Unified School District's bankruptcy filing caused by its inability to obtain cost reductions from its teachers' union).

<sup>13</sup>See *In re County of Orange*, 179 B.R. 177 (Bankr. C.D. Cal. 1995) (addressing Orange County's attempt to reject its MOUs in its Chapter 9 filing). *County of Orange* remains the lone published opinion addressing this issue.

<sup>14</sup>Vijay Kapoor, *Public Sector Labor Relations: Why it Should Matter to the Public and to Academia*, 5 U. PA. J. LAB. & EMP. L. 401, 401 (2003).

<sup>15</sup>See Michael W. McConnell & Randal C. Picker, *When Cities Go Broke: A Conceptual Introduction to Municipal Bankruptcy*, 60 U. CHI. L. REV. 425, 467-68 (1993).

<sup>16</sup>See Rachel E. Schwartz, *This Way to Egress: Should Bridgeport's Chapter 9 Filing Have Been Dis-*

## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 297

Bankruptcy Code.<sup>17</sup> Chapter 9 does not incorporate § 1113,<sup>18</sup> which governs the rejection of CBAs in Chapter 11. As a result, § 365 and the Supreme Court's opinion in *NLRB v. Bildisco & Bildisco*,<sup>19</sup> which was subsequently abrogated by § 1113, should govern the treatment of MOUs in municipal bankruptcy. *Bildisco* grants debtors broad discretion to reject their collective bargaining obligations—particularly when compared with the requirements imposed by § 1113.<sup>20</sup>

Despite the applicability of § 365 as a matter of bankruptcy law, concerns unique to the municipal debtor raise further issues regarding the proper treatment of such agreements in bankruptcy. First, it may be argued that judges should mandate the same sort of negotiated settlement otherwise imposed by § 1113 given the obvious statutory gap left by Congress's failure to incorporate that section into Chapter 9. Second, the constitutional status of the municipal debtor and its employees raises serious concerns as to whether the Constitution limits a municipal debtor's bankruptcy-specific rights under § 365.<sup>21</sup> Municipalities are, after all, subdivisions of the states. A bankruptcy court's jurisdiction over the municipal debtor may be limited by principles of state sovereignty. Such concerns caused *In re County of Orange*<sup>22</sup> to require compliance with the substantive provisions of California labor law as a prerequisite to the debtor's attempt to unilaterally modify its MOUs under § 365.<sup>23</sup> In addition, public employees may hold constitutionally-protected property interests in the terms and conditions of their employment.

There is no easy resolution to these issues, particularly considering the immense pressures that may bear on any judge asked to reject the CBAs of policemen, teachers, or firefighters. However, this Article concludes that the best means of balancing the diverse interests of debtor, union, creditor, and state should ultimately be resolved in light of the general goals of bankruptcy and Chapter 9 in particular.

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missed?, 66 AM. BANKR. L.J. 103, 120-21 (1992); W. Richard Fossey & John M. Sedor, *In re Copper River School District: Collective Bargaining and Chapter 9 Municipal Bankruptcy*, 6 ALASKA L. REV. 133 (1989); Winograd, *supra* note 12, at 231; David A. Roby, Jr., Note, *Municipal Bankruptcy: Will Labor Be Forced to Take the Proverbial Haircut?*, 26 GA. L. REV. 959 (1992); Note, *Executory Labor Contracts and Municipal Bankruptcy*, 85 YALE L.J. 957, 968 (1976) (hereinafter *Executory Labor Contracts*).

<sup>17</sup>11 U.S.C. §§ 901-46 (2006).

<sup>18</sup>11 U.S.C. § 1113 (2006).

<sup>19</sup>465 U.S. 513 (1984).

<sup>20</sup>11 U.S.C. § 365(a); *NLRB v. Bildisco & Bildisco* 465 U.S. 513, 527 (1984) (authorizing debtor to reject CBAs as executory contracts under § 365).

<sup>21</sup>See 11 U.S.C. § 903.

<sup>22</sup>179 B.R. 177 (1995).

<sup>23</sup>*Id.* at 183-84; see also Winograd, *supra* note 12, at 332 ("When a public employer is faced with collectively bargained labor costs in the context of severe budgetary shortfalls, the appropriate course is not unilateral contract modification under a bankruptcy shield, but renegotiation in accordance with state labor law.").

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Bankruptcy affords any debtor—including the municipal debtor—rights and privileges that are unique to the bankruptcy filing. Such rights are necessary to ensure that a debtor has the opportunity to regain its financial health, even though such rights may impose costs on third parties by displacing non-bankruptcy law or pre-existing contractual arrangements. This tradeoff is justified by the more fundamental assumption that interested constituencies will generally be better off in the long run by the reconfiguration of contractual rights and interests provided by the Bankruptcy Code.<sup>24</sup>

The availability of bankruptcy-specific rights is of heightened importance to the municipal debtor. Congress enacted Chapter 9 and its predecessors to provide an extraordinary remedy for distressed municipalities. History had shown that state law remedies were simply unable to provide relief. Yet reorganization under Chapter 9 is fundamentally different from reorganization proceedings elsewhere in the Bankruptcy Code. In Chapter 11, a reorganization is effectively a liquidation proceeding under which the estate may be transferred to creditors or other stakeholders.<sup>25</sup> Municipalities, on the other hand, can never be “sold” to satisfy creditors. A municipal reorganization is singularly focused upon the availability of discharge. Hence, the fiscal determinations of a municipal debtor may be entitled to greater deference to ensure its swift reorganization and emergence from bankruptcy since third-party rights are of secondary concern in Chapter 9.

There is no question that a bankruptcy court’s authority to supervise and restrict the activities of a municipal debtor—as opposed to a private debtor—may properly be subject to constitutional limitation.<sup>26</sup> But such limits should not extend so far as to limit a bankruptcy-specific right essential to reorganization, such as the assumption or rejection of executory contracts.<sup>27</sup> By consenting to the bankruptcy filing of its municipality—as it must—the state voluntarily limits its sovereignty for the benefits offered by the Bankruptcy Code.<sup>28</sup> In addition, the constitutionally-protected interests of state employees can be adequately protected by the bankruptcy judge who ensures that basic principles of fairness and due process are satisfied by the procedures normally at work in the assumption or rejection of any contract in bankruptcy.

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<sup>24</sup>See THOMAS H. JACKSON, *THE LOGIC AND LIMITS OF BANKRUPTCY LAW* 7-19 (Harvard Univ. Press 1986).

<sup>25</sup>Thomas H. Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain*, 91 *YALE L.J.* 857, 893-95 (1981) (“Reorganization proceedings provide nothing more than a method by which the sale of an enterprise as a going concern may be made to the creditors themselves.”).

<sup>26</sup>See U.S. CONST. amend. X; 11 U.S.C. §§ 903-04; *City of East St. Louis v. United States ex rel. Zebley*, 110 U.S. 321, 324 (1884).

<sup>27</sup>See *United States v. Bekins*, 304 U.S. 27 (1938).

<sup>28</sup>See 11 U.S.C. § 109(c)(2) (2006) (requiring state consent for municipal bankruptcy filing).

## II. COLLECTIVE BARGAINING OUTSIDE OF BANKRUPTCY

Collective bargaining holds a unique position in American law. Courts and lawmakers have shifted from a position of abject hostility in the nineteenth and early twentieth centuries to a broadly permissive view of collective bargaining within the federal regulatory system imposed by the National Labor Relations Act (NLRA) in 1935.<sup>29</sup> An important consequence of the NLRA was to remove such bargaining from the direct supervision of the judiciary or administrative agencies.<sup>30</sup> Federal courts have since become widely deferential to the rights of both labor and employer to bring all the weapons of “economic warfare” to bear on such negotiations.<sup>31</sup>

The uniform treatment of private sector bargaining imposed by the NLRA differs considerably from the public sector. The NLRA is inapplicable to public sector employers at the state level or below.<sup>32</sup> Hence, a balkanized field of law has arisen regarding the collective bargaining rights and obligations of public employers and employees across the fifty states. But the lack of federal regulation does not imply that regulation of collective bargaining in the public sector unions is exclusively a state prerogative. As discussed below, state labor law holds no position of constitutional significance unique to the states, and the federal government remains free to extend the NLRA’s reach to state and municipal employees.

## A. COLLECTIVE BARGAINING HISTORICALLY

Until the 1930s, the right of collective bargaining was not widely recognized at law or in practice. Employers often went to extreme lengths to prevent their employees from unionizing; where such organization had already occurred, employers would simply refuse to deal with independent unions.<sup>33</sup>

Courts also remained hostile to labor and pro-labor legislation throughout this period.<sup>34</sup> The federal injunction was a particularly effective method through which employers could thwart the collective action of labor,<sup>35</sup> and state courts shared the antagonism of their federal brethren. *Vegeahn v. Guntner*<sup>36</sup> is largely remembered for the dissent of Justice Holmes. That

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<sup>29</sup>Ch. 372 §§ 1-19, 49 Stat. 449 (1935) (codified as amended at 29 U.S.C. §§ 151-69).

<sup>30</sup>NLRB v. Jones & Laughlin Steel Corp., 301 U.S. 1 (1937).

<sup>31</sup>Duffy Tool & Stamping, L.L.C. v. NLRB, 233 F.3d 995, 996-97 (7th Cir. 2000) (discussing the general goals of federal labor law).

<sup>32</sup>29 U.S.C. § 152(2).

<sup>33</sup>Karl E. Klare, *Judicial Deradicalization of the Wagner Act and the Origins of Modern Legal Consciousness, 1937-1941*, 62 MINN. L. REV. 265, 287 & n.68 (1978).

<sup>34</sup>See, e.g., *Lochner v. New York*, 198 U.S. 45 (1905); see generally William E. Forbath, *The Shaping of the American Labor Movement*, 102 HARV. L. REV. 1109 (1989).

<sup>35</sup>Forbath, *supra* note 34, at 1148-65; see, e.g., *In re Debs*, 158 U.S. 564 (1895).

<sup>36</sup>167 Mass. 92 (1896).

dissent is of historical importance precisely because Justice Holmes rejected contemporary views on the illegality of unionization and collective bargaining.<sup>37</sup> The majority opinion reflected the dominant judicial view of union activity when it stated that:

An employer has a right to engage all persons who are willing to work for him, at such prices as may be mutually agreed upon, and persons employed or seeking employment have a corresponding right to enter into or remain in the employment of any person or corporation willing to employ them. These rights are secured by the constitution itself.<sup>38</sup>

In short, collective bargaining was historically viewed as an illicit encroachment on the so-called “freedom of contract,” if not a direct path towards communism—at least prior to 1935.

#### B. COLLECTIVE BARGAINING AND FEDERAL LAW

The NLRA wrought a fundamental change in the treatment of collective bargaining by recognizing those rights of collective action previously rejected by employers and the courts. First, the NLRA recognized the right of labor to organize independent (as opposed to employer-dominated) unions.<sup>39</sup> The effect of the NLRA in this respect must not be underestimated. As noted above, the NLRA was enacted at a time when courts were willing to treat unions as little more than illegal conspiracies.<sup>40</sup> “[I]t was not until the National Labor Relations Act became effective that the workers’ freedom of association was safeguarded by the imposition of a correlative duty on employers to refrain from interfering with or restraining the workers’ choice.”<sup>41</sup>

Second, the NLRA imposed affirmative obligations on employers to collectively bargain with those unions.<sup>42</sup> The collective bargaining process would be supervised under the auspices of the newly-created National Labor Relations Board (NLRB).<sup>43</sup> The duty to collectively bargain caused many employers to fear that substantive contractual terms would be reviewed—or imposed—by an activist NLRB.<sup>44</sup> Hence, the Supreme Court’s immediate jurisprudence sought to reaffirm the right to organize and collectively bargain

<sup>37</sup>*Id.* at 108-09 (Holmes, J., dissenting) (“[One should] abandon the idea that an organized refusal by workmen of social intercourse with a man who shall enter their antagonist’s employ is unlawful, if . . . made for the sole object of prevailing, if possible, in a contest with their employer about the rate of wages.”).

<sup>38</sup>*Id.* at 97.

<sup>39</sup>29 U.S.C. § 157 (2006).

<sup>40</sup>*See supra* notes 36-38 and accompanying text.

<sup>41</sup>Harry Shulman, *Reason, Contract, and Law in Labor Relations*, 68 HARV. L. REV. 999, 1000 (1955).

<sup>42</sup>29 U.S.C. § 158(a)(5).

<sup>43</sup>*See* 29 U.S.C. §§ 153-56.

<sup>44</sup>Klare, *supra* note 33, at 288.

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## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 301

while alleviating anxiety as to the federal government's role in this process.<sup>45</sup> The Court carefully emphasized that the NLRA would not be used to impose substantive obligations upon employers within the scope of collective bargaining. Indeed, the Court affirmed the constitutionality of the NLRA in *NLRB v. Jones & Laughlin Steel Corp.*,<sup>46</sup> even as it defined a procedural paradigm of private collective bargaining under the NLRA:

The act does not compel agreements between employers and employees. It does not compel any agreement whatever. It does not prevent the employer from "refusing to make a collective contract and hiring individuals on whatever terms" the employer "may by unilateral action determine." . . . The theory of the act is that free opportunity for negotiation with accredited representatives of employees is likely to promote industrial peace and may bring about the adjustments and agreements which the act in itself does not attempt to compel.<sup>47</sup>

In this manner, the Court determined that "the Act [was] disinterested in the substantive justice of the labor contract since it taught that not only would the wage-bargain not ordinarily be subject to substantive scrutiny, but also that the economic combat of the parties had replaced a 'meeting of the minds' as the moral basis of labor contractualism."<sup>48</sup>

During World War II, the NLRB departed from the procedural function promulgated by *Jones & Laughlin Steel*. The NLRB took an active role in negotiations and, in certain cases, imposed substantive terms upon parties. Congress reacted swiftly. In 1947, the Labor Management Relations (Taft-Hartley) Act,<sup>49</sup> made clear that the duty to collectively bargain was merely procedural and did not include an obligation to come to terms. Specifically, the Taft-Hartley Act amended the NLRA with section 8(d):

For the purposes of this section, to bargain collectively is the performance of the mutual obligation of the employer and the representative of the employees to meet at reasonable times and confer in good faith with respect to wages, hours, and other terms and conditions of employment, or the negotiation of an agreement, or any question arising thereunder, and the execution of a written contract incorporating any agreement reached if requested by either party, *but such ob-*

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<sup>45</sup>*Id.* at 293-310.

<sup>46</sup>301 U.S. 1 (1937)

<sup>47</sup>*Id.* at 45.

<sup>48</sup>Klare, *supra* note 33, at 302-03.

<sup>49</sup>Ch. 120, 61 Stat. 136 (1947) (amending various provisions of 29 U.S.C.).

*ligation does not compel either party to agree to a proposal or require the making of a concession . . .*<sup>50</sup>

As if section 8(d) were not sufficiently clear, the legislative history of Taft-Hartley sought to eradicate any lingering inclination of the NLRB to impose substantive obligations upon parties to the collective bargaining process. The Committee Report warned that “the duty to bargain is not to be construed as requiring either party to discuss or agree to any modification of the terms and conditions contained in a contract for a fixed period . . .”<sup>51</sup>

Federal courts and the NLRB have consistently adhered to this procedural vision of collective bargaining. Parties are required only to meet and negotiate. There is no obligation to adopt specific terms, nor is there even an obligation to come to terms. “There is no duty to agree . . . and if the parties deadlock (reach ‘impasse,’ in the jargon of labor law), the employer is free to operate his business as he did before bargaining began, and therefore he may alter the terms and conditions of the workers’ employment.”<sup>52</sup> Both unions and employers are largely free to use whatever economic leverage may be available to obtain the most favorable contract. Labor may strike.<sup>53</sup> Employers may lock out employees.<sup>54</sup> At impasse, an employer may unilaterally modify its contractual obligations.<sup>55</sup> In sum, the obligation to collectively bargain does not eliminate economic warfare, nor does it eliminate weapons available to the combatants.<sup>56</sup> Collective bargaining under federal law merely

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<sup>50</sup>29 U.S.C. § 158(d) (2006) (emphasis added).

<sup>51</sup>H.R. REP. NO. 80-510 (1947), reprinted in 1947 U.S.C.C.A.N. 1135, 1140-41; see also *NLRB v. Am. Nat’l Ins. Co.*, 343 U.S. 395, 408-09 (1952) (“Congress provided expressly that the Board should not pass upon the desirability of the substantive terms of labor agreements.”).

<sup>52</sup>*Duffy Tool & Stamping, L.L.C. v. NLRB*, 233 F.3d 995, 996 (7th Cir. 2000). But see *NLRB v. A-1 King Size Sandwiches, Inc.*, 732 F.2d 872, 877-78 (11th Cir. 1984) (holding that employer violated its duty to collectively bargain where it refused to budge from its initial bargaining position for over eighteen months).

<sup>53</sup>*NLRB v. Ins. Agents’ Int’l Union*, 361 U.S. 477, 489 (1960) (“The presence of economic weapons in reserve, and their actual exercise on occasion by the parties, is part and parcel of the system that the Wagner and Taft-Hartley Acts have recognized.”).

<sup>54</sup>*Am. Ship Bldg. Co. v. NLRB*, 380 U.S. 300, 309 (1965) (“The lockout may well dissuade employees from adhering to the position which they initially adopted in the bargaining, but the right to bargain collectively does not entail any ‘right’ to insist on one’s position free from economic disadvantage.”).

<sup>55</sup>*Duffy Tool & Stamping*, 233 F.3d at 996; *accord AFTRA v. NLRB*, 395 F.2d 622, 629 (D.C. Cir. 1968) (holding that post-impasse modifications are “legitimate economic weapons from the bargainers’ arsenal”); *Telescope Casual Furniture, Inc.*, 326 N.L.R.B. 588, 591 (1998) (Gould, Ch., concurring) (“[T]ough and sometimes distasteful tactics engaged in by employers and unions throughout the collective-bargaining process are frequently not unlawful under the National Labor Relations Act.”); see *Brown v. Pro Football, Inc.*, 518 U.S. 231, 238-39 (1996) (discussing conditions under which employer may unilaterally impose terms post-impasse).

<sup>56</sup>*First Nat’l Maint. Corp. v. NLRB*, 452 U.S. 666, 674 (1981) (“[B]oth employer and union may bargain to impasse over these matters and use the economic weapons at their disposal to attempt to secure their respective aims.”).



legitimizes the fight by channeling behavior into formalized procedure.<sup>57</sup>

### C. COLLECTIVE BARGAINING AND STATE LAW

The NLRA has largely preempted state labor law governing private employers.<sup>58</sup> But the NLRA does not apply to states and their sub-units as employers.<sup>59</sup> Each of the fifty states has been free to independently define the rights and duties of public employers and their employees. While some states have enacted regimes similar to the NLRA, wide variation exists among state laws governing public sector labor. Different jurisdictions also hold widely different views with respect to the “economic weapons” that employers and employees may use.

In Illinois, for example, public employers may refuse to negotiate with their unions in certain cases.<sup>60</sup> In California, public employees have the statutory right to organize, and employers are obliged to collectively bargain with their unions.<sup>61</sup> Such employees—other than firefighters—may strike even without a statutory right to that effect.<sup>62</sup> In contrast, the Supreme Court of South Carolina has determined that its “right to work” statute does not apply to public employees in the absence of an express statutory provision to the contrary.<sup>63</sup> Pennsylvania generally allows public employees to strike if collective bargaining reaches an impasse,<sup>64</sup> but prohibits strikes by employees such as “guards at prisons or mental hospitals, or employees directly involved with and necessary to the functioning of the courts of this Commonwealth . . . .”<sup>65</sup>

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<sup>57</sup>Klare, *supra* note 33, at 302-03.

<sup>58</sup>*See* *Wis. Dep't of Indus., Labor and Human Relations v. Gould*, 475 U.S. 282, 286 (1986) (“It is by now a commonplace that in passing the NLRA Congress largely displaced state regulation of industrial relations.”).

<sup>59</sup>29 U.S.C. § 152(2) (2006) (“The term ‘employer’ [under the NLRA] . . . shall not include the United States or any wholly owned Government corporation, or any Federal Reserve Bank, or any State or political subdivision thereof . . . .”).

<sup>60</sup>*Peters v. Health and Hosps. Governing Comm'n*, 430 N.E.2d 1128, 1130 (Ill. 1981) (“[W]e find no authority in statutory or case law which supports the position that a public body can be ordered to negotiate such an agreement. Indeed, under the National Labor Relations Act, a State or local governmental entity has the unequivocal right to refuse to enter into a collective bargaining agreement with its employees.”).

<sup>61</sup>*Meyers-Milias-Brown Act*, CAL. GOV'T CODE §§ 3500-10 (1995).

<sup>62</sup>CAL. LAB. CODE § 1962 (2003) (“[Firefighters] shall not have the right to strike, or to recognize a picket line of a labor organization while in the course of the performance of their official duties.”); *County Sanitation Dist. No. 2 v. L.A. County Employees' Ass'n.*, 699 P.2d 835, 849 (Cal. 1985) (“[T]he common law prohibition against public sector strikes should not be recognized in this state. Consequently, strikes by public sector employees in this state as such are neither illegal nor tortious under California common law.”).

<sup>63</sup>*Branch v. City of Myrtle Beach*, 532 S.E.2d 289, 292 (S.C. 2000) (“In light of the traditional construction of labor relations statutes, we believe that by not having a definition including public employment, the legislature’s intent was not to cover public employees.”).

<sup>64</sup>43 PA. STAT. ANN. § 1101.1003 (2006).

<sup>65</sup>*Id.* § 1101.1001.

In New York, public employees may unionize,<sup>66</sup> and public employers are required to bargain collectively with such unions.<sup>67</sup> But public sector employees are barred from striking<sup>68</sup>—a fact which did not affect the aggressive posture of the New York City municipal transit workers in 2005.<sup>69</sup>

The limited tools of economic warfare available to state employees reflect meaningful differences between collective bargaining in the public and private sectors. “In the private sector, unions are generally regarded as indispensable for a private negotiation system that both redresses the ‘unequal bargaining power’ postulated for the individual employee and that simultaneously gives employees a voice in the formation and administration of the web of rules surrounding the workplace.”<sup>70</sup> Hence, private sector unions require greater freedom of action to balance the comparative advantages traditionally held by employers at the bargaining table. At the same time, the militancy of private sector unions is, or at least should be tempered by the risk that such tactics could jeopardize the financial health of its employer and, by extension, the union itself.<sup>71</sup>

No economic forces directly align the interests of public sector unions with public sector employers.<sup>72</sup> Public sector unions are largely characterized by their immunity from market pressures.<sup>73</sup> Public sector unions tend to provide essential services traditionally monopolized by the state. There are no comparable private sector substitutes for police departments, fire departments, or mass-transit systems. But while a private sector employer can eliminate or reduce inefficient production methods or services, a municipality cannot terminate basic public services.<sup>74</sup> Hence, public sector unions may properly be denied access to certain negotiating tactics available to their public sector counterparts, such as the strike.<sup>75</sup>

Admittedly, public sector unions remain subject to indirect political control through elections and referenda. “When the employer is the government . . . the employer’s decisionmaking process becomes of central concern in both legal and political terms. The policies brought to the bargaining table

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<sup>66</sup>N.Y. CIV. SERV. LAW § 202 (1999).

<sup>67</sup>*Id.* § 203.

<sup>68</sup>*Id.* § 210.

<sup>69</sup>See Steven Greenhouse & Sewell Chan, *Transit Union Calls for Strike*, N.Y. TIMES, Dec. 20, 2005, at A1 (discussing transit workers’ union determination to strike notwithstanding statutory prohibition).

<sup>70</sup>Bernard D. Meltzer & Cass R. Sunstein, *Public Employees Strikes, Executive Discretion, and the Air Traffic Controllers*, 50 U. CHI. L. REV. 731, 733-34 (1983).

<sup>71</sup>*Id.* at 739.

<sup>72</sup>*Id.*

<sup>73</sup>LEO TROY, *THE NEW UNIONISM IN THE NEW SOCIETY* 31 (Geo. Mason Univ. Press 1994).

<sup>74</sup>*Id.*

<sup>75</sup>Meltzer & Sunstein, *supra* note 70, at 739. But see Clyde Summers, *Bargaining in the Government’s Business: Principles and Politics*, 18 U. TOL. L. REV. 265, 267-68 (1987) (arguing that the threat of public sector strikes may increase the efficiency of public sector employment).

## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 305

are governmental policies.”<sup>76</sup> But public sector unions have direct and immediate access to political decision-makers, whereas the electorate’s involvement is far more removed. “The union is able to deal with public decision-makers behind closed doors without other interests being heard, and to arrive at agreements which are politically difficult, if not legally impossible to change.”<sup>77</sup> Moreover, the “sharply focused interests” of public sector unions generate a narrow and politically active voting bloc that can trump larger, but less-focused municipal constituencies.<sup>78</sup>

Many state labor regimes have sought to balance the restrictions imposed on public sector unions by regulating the collective bargaining obligations of public sector employers. For example, state law may limit an employer’s ability to impose unilateral modifications to CBAs after impasse or termination.<sup>79</sup> Under New York and Connecticut law, a public employer is obliged to maintain existing terms and conditions of employment pending arbitration.<sup>80</sup> In California, home rule employers may unilaterally modify its MOUs only in “emergencies.”<sup>81</sup> Missouri law is silent as to the effect of an expired collective bargaining agreement, but at least one court has determined that an MOU remains in effect until it is replaced.<sup>82</sup> In Washington, employers may unilaterally modify the employment terms of “non-uniformed” employees only at one year after expiration of an MOU.<sup>83</sup> In Oregon<sup>84</sup> and Pennsylvania,<sup>85</sup> public sector employers may not unilaterally impose terms after an impasse,

<sup>76</sup>Clyde W. Summers, *Public Sector Bargaining: Problems of Governmental Decisionmaking*, 44 U. CIN. L. REV. 669, 670 (1975).

<sup>77</sup>Summers, *supra* note 75, at 267-68; see also R. Theodore Clark, Jr., *Politics and Public Employee Unionism: Some Recommendations for an Emerging Problem*, 44 U. CIN. L. REV. 680, 681 (1975).

<sup>78</sup>Meltzer & Sunstein, *supra* note 70, at 740; see also Summers, *supra* note 75, at 267-68; Clark, *supra* note 77, at 684 (“The political aspects of public sector collective bargaining enable public sector unions to, in effect, sit on both sides of the bargaining table.”).

<sup>79</sup>*Cf. Duffy Tool & Stamping, L.L.C. v. NLRB*, 233 F.3d 995, 996 (7th Cir. 2000) (permitting private sector employer to unilaterally impose contractual modifications post-impasse).

<sup>80</sup>N.Y. CIV. SERV. LAW § 209-a(1)(e) (1999) (“It shall be an improper practice for a public employer or its agents deliberately . . . (e) to refuse to continue all terms of an expired agreement until a new agreement is negotiated, unless the employee organization which is a party to such agreement has, during such negotiations or prior to such resolution of such negotiations, engaged in [a strike] . . . .”); CONN. GEN. STAT. § 5-278a (1998).

<sup>81</sup>*Sonoma County Org. of Pub. Employees v. County of Sonoma*, 591 P.2d 1 (Cal. 1979) (identifying factors to be used when determining if a municipal employer may unilaterally modify its collective bargaining obligations).

<sup>82</sup>See MO. ANN. STAT. § 105.520 (1997), *construed in Murray v. City of Jennings*, 639 S.W.2d 220, 224 (Mo. Ct. App. 1982).

<sup>83</sup>WASH. REV. CODE § 41.56.123(1) (2006). *But see Maple Valley Prof. Fire Fighters Local 3062 v. King County Fire Prot. Dist. No. 43*, 145 P.3d 1247 (Wash. Ct. App. 2006) (holding that arbitration clause in MOU of “uniformed” employees does not survive expiration).

<sup>84</sup>*Wasco County v. Am. Fed. of State, County and Mun. Employees, Local 2752*, 613 P.2d 1067 (Or. Ct. App. 1980) (affirming decision of state Employee Relations Board to treat post-impasse unilateral modifications as per se unfair labor practice). *But see Medford Firefighters Ass’n, Local 1431 v. City of Medford*, 605 P.2d 289, 292 (Or. Ct. App. 1979) (holding municipal employer does not commit unfair

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though Massachusetts has adopted the opposite rule.<sup>86</sup> As a result, state law could severely curtail a municipal employer's ability to obtain wage or benefit reductions through rejection or modification of an MOU.

Despite this fractured legal environment—or perhaps because of it—public sector unions have thrived while their private sector brethren have suffered. At mid-century, public sector union membership was practically nonexistent.<sup>87</sup> As of 2000, approximately forty percent of public sector employees were union members, as compared to only nine percent of private sector employees.<sup>88</sup> This growth has been due in no small part to the general exemption of public sector employees from market pressures,<sup>89</sup> and the militant tactics adopted by public sector unions since the 1970s.<sup>90</sup> The recent New York transit strike suggests such militancy is not a thing of the past.<sup>91</sup>

It is unclear why Congress carved out an exemption for state and local employers under section 2(2)<sup>92</sup> of the NLRA. Congress may have been concerned with the constitutionality of the NLRA as applied to state employers under the more limited view of federal power at work during the 1930s. Supporting this view, the House Report discussing section 2(2) noted that “[the Act] does not apply to controversies or practices of purely local significance which do not presently or potentially burden or obstruct the free flow of commerce.”<sup>93</sup> This statement suggests that Congress felt its regulation of state employer/employees could have overstepped its authority under the Commerce Clause.<sup>94</sup>

On the other hand, section 2(2) may have been enacted to mirror the existing labor practices of public sector employers. In 1935, the majority of states and the federal government prohibited their employees from engaging

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labor practice by enacting ordinance excluding certain supervisory firefighters from collective bargaining unit after expiration).

<sup>85</sup>See *Cent. Dauphin Educ. Assoc. v. Cent. Dauphin Sch. Dist.*, 792 A.2d 691, 699 (Pa. 2001) (discussing employer's rights in the event of impasse).

<sup>86</sup>*Newton Branch of Mass. Police Assoc. v. City of Newton*, 484 N.E.2d 1326, 1329 (Mass. 1985); *Mass. Org. of State Eng'rs & Scientists v. Labor Relations Comm'n*, 452 N.E.2d 1117, 1122 (Mass. 1983) (“[U]nilateral action during the existence of a legitimate impasse is not a per se violation of the duty to bargain in good faith . . .”).

<sup>87</sup>See *infra* notes 95-97.

<sup>88</sup>Hylton, *supra* note 8, at 687.

<sup>89</sup>TROY, *supra* note 73, at 31; Hylton, *supra* note 8, at 690.

<sup>90</sup>See HUGH O'NEIL, *UNIONIZATION OF MUNICIPAL EMPLOYEES* 12-13 (Robert H. Connery & William V. Farr, eds. 1971).

<sup>91</sup>Sewell Chan & Steven Greenhouse, *M.T.A. Returns to Harder Line in Labor Talks*, N.Y. TIMES, Jan. 26, 2006, at A1.

<sup>92</sup>29 U.S.C. § 152(2) (2006).

<sup>93</sup>H.R. REP. NO. 1147, at 10 (1935), reprinted in 2 NLRB LEGISLATIVE HISTORY OF THE NATIONAL LABOR RELATIONS ACT, 1945, at 3046, 3057 (1935).

<sup>94</sup>U.S. CONST. art. I, § 8, cl. 3.

in precisely the type of behavior that the NLRA sought to legalize.<sup>95</sup> General antagonism to public sector unions in state law subsisted until the 1960s.<sup>96</sup> Federal employees were finally granted the ability to unionize only through the 1962 Executive Order of President Kennedy.<sup>97</sup> As recently as 2000, South Carolina exempted public employers from state labor law precisely because of the “traditional construction of labor relations statutes.”<sup>98</sup> In light of this record, section 2(2) looks less like an expression of constitutional limitation and more like a relic of historical fact.

Inquiry into the congressional intent guiding the constitutional necessity of section 2(2) may be largely academic. First, Congress does not make binding determinations with respect to the constitutionality of its laws.<sup>99</sup> Second, the NLRA was passed at a time when the regulatory powers of the federal government were considerably more limited. The NLRA was enacted in the face of a judiciary antagonistic towards expansive visions of federal regulation and cases such as *United States v. Carolene Products Company*<sup>100</sup> and *West Coast Hotel v. Parrish*<sup>101</sup> remained in the uncertain future.

More recent jurisprudence suggests that no constitutional bar prevents Congress from directly regulating the labor practices of state employers. Specifically, the Court’s opinion in *Garcia v. San Antonio Metropolitan Transit Authority*<sup>102</sup> allows Congress to extend the NLRA to state employers without overstepping its constitutional authority. In *Garcia*, the Court determined that federal minimum wage levels for transit employees preempted state law governing the wages and hours of San Antonio Municipal Transit Authority (SAMTA) employees. *Garcia* expressly overruled the Court’s earlier precedent in *National League of Cities v. Usery*<sup>103</sup>, which had severely

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<sup>95</sup>See *NLRB v. Natural Gas Util. Dist. of Hawkins County*, 402 U.S. 600, 604 (1971) (“The legislative history does reveal, however, that Congress enacted the [§ 152(2)] exemption to except from Board cognizance the labor relations of federal, state, and municipal governments, since governmental employees did not usually enjoy the right to strike.”); see generally RICHARD C. KEARNEY, *LABOR RELATIONS IN THE PUBLIC SECTOR* 39-43 (Marcel Dekker 1984).

<sup>96</sup>KEARNEY, *supra* note 95, at 39-41.

<sup>97</sup>*Id.* at 43.

<sup>98</sup>*Branch*, 532 S.E.2d at 292.

<sup>99</sup>*City of Boerne v. Flores*, 521 U.S. 507, 519 (1997) (noting that Congress does not hold the power “to determine what constitutes a constitutional violation”); *Marbury v. Madison*, 5 U.S. (1 Cranch) 137 (1803).

<sup>100</sup>304 U.S. 144, 153 n.4 (1938) (announcing the Court’s decision to subject to economic regulation to more relaxed standards of Constitutional review).

<sup>101</sup>300 U.S. 379 (1937).

<sup>102</sup>469 U.S. 528 (1985), *overruling* *Nat’l League of Cities v. Usery*, 426 U.S. 833 (1976); see generally TROY, *supra* note 73, app. A (discussing background and holding of *Garcia*).

<sup>103</sup>426 U.S. 833 (1976). *National League of Cities* had endorsed a strongly deferential approach to the states’ right to define the terms and conditions of employment: “One undoubted attribute of state sovereignty is the States’ power to determine the wages which shall be paid to those whom they employ in

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limited the exercise of Federal regulatory authority over the states. *National League of Cities* had distinguished between “traditional” and “non-traditional” areas of state action.<sup>104</sup> The latter could be subject to federal regulation. The former could not. *Garcia* found this distinction to be both unworkable and unrealistic in light of the realities of the modern regulatory state.<sup>105</sup>

The Court then determined that federal authority to regulate state employers *qua* employers was not restricted by the Tenth Amendment: “SAMTA faces nothing more than the same minimum-wage and overtime obligations that hundreds of thousands of other employers, public as well as private, have to meet.”<sup>106</sup> The Court deflected any claims that federal legislation had imposed an undue burden on the state by taking particular note of the billions of dollars in federal funds benefiting transit authorities such as SAMTA:

Congress . . . has provided substantial countervailing financial assistance . . . , assistance that may leave individual mass-transit systems better off than they would have been had Congress never intervened at all in the area. Congress’ treatment of public mass transit reinforces our conviction that the national political process systematically protects States from the risk of having their functions in that area handicapped by Commerce Clause regulation.<sup>107</sup>

*Garcia* implies that no constitutional limits preclude Congress from either eliminating the exemption created by section 2(2) of the NLRA or creating independent statutory regimes governing state employees.<sup>108</sup> Congress could therefore exercise its dormant Commerce Clause powers to create a unified

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order to carry out their governmental functions, what hours those persons will work, and what compensation will be provided where these employees may be called upon to work overtime.” *Id.* at 844. Thus, *National League of Cities* helped terminate a movement towards national public labor legislation that had gained momentum during the mid-1970s. See KEARNEY, *supra* note 95, at 49-53.

<sup>104</sup>See *United Haulers Assoc. v. Oneida-Herkimer Solid Waste Mgmt.*, 127 S. Ct. 1786, 1810 (2007) (Alito, J., dissenting) (discussing rejection of *National League of Cities* as “analytically unsound”).

<sup>105</sup>*Garcia*, 469 U.S. at 545-47.

<sup>106</sup>*Id.* at 554.

<sup>107</sup>*Id.* at 555. It should be noted that receipt of federal funds is not a condition precedent to federal regulation under *Garcia*. *Id.* at 555 n.21.

<sup>108</sup>*Id.* at 566 n.11 (1985) (Powell, J., dissenting) (“[I]t is unlikely that special interest groups will fail to accept the Court’s open invitation to urge Congress to extend [the NLRA] and other statutes to apply to the States and their local subdivisions.”); TROY, *supra* note 73, at 189 (“*Garcia* has opened the door for federal legislation to nationalize labor relations.”); Benjamin Aaron, *Unfair Labor Practices and the Right to Strike in the Public Sector: Has the National Labor Relations Act Been a Good Model?*, 38 STAN. L. REV. 1097, 1121 (1986) (“Whatever barriers *National League of Cities* may have erected against a federal preemptive law uniformly regulating labor relations between the states and their employees have thus been removed [by *Garcia*] . . .”).

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## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 309

field of federal public labor regulation.<sup>109</sup>

At least one congressman has sought to implement federal legislation governing the collective bargaining obligations of local governments and their employees. In 1987, Representative William Clay (D. Mo.) first proposed federal regulation governing the employment of local firefighters.<sup>110</sup> In 1989, Representative Clay introduced H.R. 2204,<sup>111</sup> which sought to guarantee the rights of firefighters employed by “the United States (and the political subdivisions thereof)” to bargain collectively and H.R. 2205,<sup>112</sup> which proposed analogous rights for law enforcement officers. Section 4(2) of H.R. 2204 defined “employer” to include “any political subdivision thereof, including any town, city, borough, [or] fire district.”<sup>113</sup> H.R. 2204 also sought to create a “Firefighters’ National Labor Commission” which would supervise labor disputes between firefighters and their employers.<sup>114</sup> Representative Clay’s efforts did not succeed.

Notwithstanding *Garcia*, the constitutional status of public employees remains different from their private sector counterparts in one important respect. Public sector employees may hold a property interest in their employment protected by procedural due process.<sup>115</sup> Hence, a public employee may be entitled to notice and an evidentiary hearing before the terms of employment governed by a bargaining agreement can be modified.<sup>116</sup>

An MOU may provide certain mechanisms through which the terms and conditions of employment might be constitutionally altered. For instance, the MOU can define notice provisions through which an employee may be dismissed or the terms of employment adjusted. Such terms may be sufficient to

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<sup>109</sup>See *United States v. Morrison*, 529 U.S. 598 (2000) (Souter, J., dissenting) (“[T]he Federal Government, when acting within a delegated power, may override countervailing state interests, whether these be described as governmental or proprietary in character.” (citation and internal quotation marks omitted)); cf. *Prudential Ins. Co. v. Benjamin*, 328 U.S. 408, 434 (1946) (“Congress may keep the way open, confine it broadly or closely, or close it entirely”).

<sup>110</sup>TROY, *supra* note 73, at app. B.

<sup>111</sup>H.R. 2204, 101st Cong. (1989) (proposing federal laws to govern labor disputes arising from MOUs between fire fighters and employers).

<sup>112</sup>H.R. 2205, 101st Cong. (1989) (proposing federal laws to govern labor disputes arising from MOUs between law enforcement officers and employers).

<sup>113</sup>H.R. 2204 § 4(2).

<sup>114</sup>*Id.* § 5.

<sup>115</sup>*Gilbert v. Homar*, 520 U.S. 924, 928-29 (1997) (“[P]ublic employees who can be discharged only for cause have a constitutionally protected property interest in their tenure and cannot be fired without due process . . . .”); *Cleveland Bd. of Ed. v. Loudermill*, 470 U.S. 532, 538-39 (1985); *Bd. of Regents of State Colls. v. Roth*, 408 U.S. 564, 577 (1972); *Perry v. Sinderman*, 408 U.S. 593, 596 (1972).

<sup>116</sup>See, e.g., *Ciambriello v. County of Nassau*, 292 F.3d 307, 314 (2d Cir. 2002) (“[A] collective bargaining agreement may give rise to a property interest in continued employment.”); *Chaney v. Suburban Bus Div. of Reg'l Transp. Auth.*, 52 F.3d 623, 629 (7th Cir. 1995) (“[D]ue process requires pre-termination notice and an opportunity to respond even where a CBA provides for post-termination procedures that fully compensate wrongfully terminated employees.”).

trigger the requirements of the Fourteenth Amendment, but they do not, in themselves, create a constitutionally sufficient standard.<sup>117</sup> Put another way, a constitutionally-protected property right may be created by an MOU,<sup>118</sup> but the extent of constitutional due process is not defined by the MOU. The Constitution alone determines whether process is sufficient.<sup>119</sup> The adequacy of process, in turn, will be analyzed with reference to the balancing test announced by the Court in *Mathews v. Eldridge*:<sup>120</sup> (1) the private interest that will be affected by the official action; (2) the risk of an erroneous deprivation of such interest through the procedures used, and the probable value, if any, of additional or substitute procedural safeguards; and (3) the government's interest, including the fiscal and administrative burdens that additional procedural requirements might entail.<sup>121</sup> Thus, the procedures for dispute resolution or the termination of employment defined in an MOU may or may not satisfy the requirements of due process.<sup>122</sup>

### III. CBAS IN CHAPTER 11

The assumption or rejection of CBAs in Chapter 11 is governed by § 1113 of the Bankruptcy Code. Section 1113 was a congressional response to the Court's opinion in *Bildisco*, in order to prevent employers from using bankruptcy as a "judicial hammer" to reduce burdens imposed by collective bargaining agreements.<sup>123</sup> Section 1113 does not achieve this goal by explicitly defining an enhanced test for rejection. Indeed, courts and commentators were quick to recognize that § 1113 provided little guidance for the proper treatment of CBAs post-*Bildisco*.

Rather, the genius of § 1113 is that its ambiguous procedural requirements permit judges to impose substantive obligations upon both debtor and employer as a condition of rejection. Thus, § 1113 is a radical displacement of non-bankruptcy law insofar as it requires—or at least permits—bankruptcy judges to engage in precisely the sort of conduct that is generally forbidden outside of bankruptcy.<sup>124</sup> Of course, § 1113 is inapplicable in

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<sup>117</sup>*Parrett v. City of Connersville*, 737 F.2d 690, 696 (7th Cir. 1984), *cert. denied*, 469 U.S. 1145 (1985).

<sup>118</sup>*Roth*, 408 U.S. at 577.

<sup>119</sup>*Ciambriello*, 292 F.3d at 319.

<sup>120</sup>424 U.S. 319 (1976).

<sup>121</sup>*Id.* at 335; *accord*, *Gilbert*, 520 U.S. at 931-32.

<sup>122</sup>*See Parrett*, 737 F.2d at 696.

<sup>123</sup>*N.Y. Typographical Union No. 6 v. Maxwell Newspapers, Inc. (In re Maxwell Newspapers, Inc.)*, 981 F.2d 85, 89 (2d Cir. 1992).

<sup>124</sup>*See* Christopher D. Cameron, *How 'Necessary' Became the Mother of Rejection: An Empirical Look at the Fate of Collective Bargaining Agreements on the Tenth Anniversary of Bankruptcy Code Section 1113*, 34 SANTA CLARA L. REV. 848, 873 (1994) ("[T]he statute stirs an unprecedented admixture of substantive as well as procedural elements into the bargaining process."); *cf. supra* Section II.B (discussing procedural paradigm of American labor law). *But see* DANIEL L. KEATING, *BANKRUPTCY AND EMPLOY-*



## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 311

Chapter 9.<sup>125</sup> But an understanding of how § 1113 actually modifies the Court's ruling in *Bildisco* provides a more accurate conception of a bankruptcy court's role when considering the treatment of collective bargaining obligations in Chapter 9.

A. *BILDISCO*

Under the NLRA, employers can neither terminate nor unilaterally modify collective bargaining agreements without first reaching an impasse.<sup>126</sup> Prior to the Court's decision in *Bildisco*, federal courts were split on the extent to which a bankrupt employer could seek to modify or reject an existing CBA. Some courts had determined that a debtor could only reject such agreements if clearly necessary to stave off liquidation.<sup>127</sup> Others had permitted debtors to reject CBAs where, on the whole, the equities of the particular case favored rejection.<sup>128</sup> *Bildisco* resolved this split by holding that collective bargaining agreements were executory contracts subject to rejection under § 365,<sup>129</sup> and such rejections did not constitute an unfair labor practice under the NLRA.<sup>130</sup>

It is worth asking whether the Court was correct in its more fundamental determination that CBAs are, in fact, executory contracts.<sup>131</sup> The unique history of collective bargaining suggests these agreements hold a special place in the field of contract law,<sup>132</sup> and commentators have consistently recognized that the unique dynamics at work in CBAs set such agreements apart from a traditional view of contract.<sup>133</sup> The Court had also used the *sui generis* nature of such agreements to uphold the validity of mandatory arbitra-

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MENT LAW § 2.6 (1995) (arguing that "§ 1113 more or less approximates the rules under nonbankruptcy law").

<sup>125</sup>See 11 U.S.C. § 901 (2006); *In re County of Orange*, 179 B.R. 177, 182-83 (Bankr. C.D. Cal. 1995).

<sup>126</sup>29 U.S.C. § 158 (2006).

<sup>127</sup>KEATING, *supra* note 124, § 2.2.1.

<sup>128</sup>*Id.*

<sup>129</sup>NLRB v. *Bildisco & Bildisco*, 465 U.S. 513, 525-26 (1984). The Court noted that a "somewhat stricter standard" should be used to govern the rejection of CBAs. *Id.* at 524 (citing *In re Brada-Miller Freight Sys., Inc.*, 702 F.2d 890 (11th Cir. 1983); *In re Bildisco*, 682 F.2d 72 (3d Cir. 1982); *Local Joint Executive Bd. v. Hotel Circle*, 613 F.2d 210 (9th Cir. 1980); *Shopmen's Local Union No. 455 v. Kevin Steel Prods., Inc.*, 519 F.2d 698 (2d Cir. 1975)).

<sup>130</sup>*Id.* at 533-34.

<sup>131</sup>Interestingly, none of the parties to *Bildisco* raised this point, which was argued only by the United Mine Workers of America as *amicus*. See *id.* at 524 n.6.

<sup>132</sup>See *supra* Section II.A.

<sup>133</sup>See, e.g., Michael D. Sousa, *Reconciling the Otherwise Irreconcilable: the Rejection of Collective Bargaining Agreements Under Section 1113 of the Bankruptcy Code*, 18 LAB. LAW. 453, 458 (2003) ("[A] collective bargaining agreement more closely resembles a generalized code of industrial relations than it does a single voluntary exchange." (quoting Jeffrey D. Berman, *Rejection of Collective Bargaining Agreements Under the Bankruptcy Amendments of 1984*, 71 VA. L. REV. 983, 985 (1985))); Klare, *supra* note 33, at 294 ("[T]he collective bargaining agreement is a special kind of contract, with peculiar legal incidents . . ."); Shulman, *supra* note 41, at 1004.

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tion clauses in 1960.<sup>134</sup> Nor does a CBA fit neatly into the traditional definition of an executory contract as a matter of bankruptcy law—in which non-performance by one party would excuse performance by the other.<sup>135</sup> The paradigmatic example of such a contract is where a debtor simply rejects an unfavorable supply agreement.<sup>136</sup> Clearly, the “generalized code of conduct” enshrined in a CBA differs markedly in both degree and kind. Moreover, the consequences of rejecting an executory contract are typically the same in or out of bankruptcy—a creditor is left with a claim against the breaching party.<sup>137</sup> Yet *Bildisco*’s determination that rejection of a CBA could not constitute an unfair labor practice ensured that the effect of rejection would depend entirely on whether an employer was in bankruptcy.

But theoretical objections do not alter Supreme Court precedent. *Bildisco*’s holding that § 365 effectively preempted federal labor law with respect to the rejection or modification of CBAs remains law to the extent *Bildisco* has not been abrogated by § 1113. “Since the filing of a petition in bankruptcy under Chapter 11 makes the contract unenforceable, [NLRA] procedures have no application to the employer’s unilateral rejection . . . .”<sup>138</sup> The Court’s decision rested on a broad interpretation of the proper role of § 365 in Chapter 11. In the Court’s view, a debtor’s rights under § 365 were so essential to its reorganization that conflicting, non-bankruptcy statutes could not be permitted to restrict such rights: “[T]he authority to reject an executory contract is vital to the basic purpose to a Chapter 11 reorganization, because rejection can release the debtor’s estate from burdensome obligations that can impede a successful reorganization.”<sup>139</sup>

*Bildisco*’s decision to interpret § 365 in light of the “basic purpose” of Chapter 11 may be questioned. “Nothing in the Bankruptcy Code or its antecedents suggests that the power to reject turns on whether the debtor is liquidating or reorganizing. If it does not, then the debtor’s chances of reorganizing successfully should play no role in deciding the contours of § 365.”<sup>140</sup> *Bildisco* implicitly rejected this more limited conception of § 365 through its determination that § 365 should preempt conflicting legal regimes governing CBAs where such laws might otherwise ‘impede’ a debtor’s reorganization.<sup>141</sup>

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<sup>134</sup>*United Steelworkers of Am. v. Warrior and Gulf Navigation Co.*, 363 U.S. 574, 579 (1960) (“The collective agreement covers the whole employment relationship. It calls into being a new common law—the common law of a particular industry or of a particular plant.”).

<sup>135</sup>See generally DOUGLAS G. BAIRD, *THE ELEMENTS OF BANKRUPTCY* 126-52 (4th ed. 2006) (discussing executory contracts generally and their treatment under the Bankruptcy Code).

<sup>136</sup>*Id.* at 126-27.

<sup>137</sup>11 U.S.C. §§ 365(g), 502(g); BAIRD, *supra* note 135, at 127.

<sup>138</sup>*Bildisco*, 465 U.S. at 533.

<sup>139</sup>*Id.* at 528.

<sup>140</sup>BAIRD, *supra* note 135, at 140.

<sup>141</sup>See *Bildisco*, 465 U.S. at 533.

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## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 313

As a result, *Bildisco* leaves a debtor with significant discretion to assume or reject CBAs under § 365 insofar as such an action would facilitate the debtor's recovery.<sup>142</sup> *Bildisco* in fact reminded lower courts that collective bargaining requires that "employer and union reach their own agreements on terms and conditions of employment free from government interference."<sup>143</sup> A bankruptcy court's authority with respect to CBAs is thus limited only to its ability to permit or deny rejection of a collective bargaining agreement based on how such a rejection would affect the totality of the case—not the interests of any constituency in particular: "The Bankruptcy Code does not authorize free-wheeling consideration of every conceivable equity, but rather only how the equities relate to the success of the reorganization."<sup>144</sup>

Yet *Bildisco* is generally consistent with the NLRA's permissive approach to collective bargaining even if its holding displaces the specific provisions of that regime. As noted above, both employers and labor have wide discretion to utilize weapons of economic warfare when fighting for the best bargain.<sup>145</sup> If a union has the right to put an employer into bankruptcy through a strike, rights created by that bankruptcy are a permissible avenue through which the debtor employer may preserve its future as a going concern.<sup>146</sup> Bankruptcy—and the rights created through a bankruptcy filing—should remain open to a financially distressed employer confronted with unaffordable CBAs and a militant union. The specter of financially healthy employers using bankruptcy solely as a 'hammer' to break its unions is properly addressed through abstention<sup>147</sup> or dismissal<sup>148</sup>—not by denying debtors access to rights otherwise available under the Bankruptcy Code.

## B. SECTION 1113

*Bildisco* did not survive long without amendment. Congress quickly enacted § 1113,<sup>149</sup> which purported to limit a debtor's rights to reject CBAs. Though § 1113 was initially seen as a victory for organized labor,<sup>150</sup> its interpretation and application have been far more complex. The muddled text of

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<sup>142</sup>*Id.* at 525-26 (citing, inter alia, *Shopmen's Local Union No. 455 v. Kevin Steel Prods., Inc.*, 519 F.2d 698 (2d Cir. 1975)).

<sup>143</sup>*Bildisco*, 465 U.S. at 526.

<sup>144</sup>*Id.* at 527.

<sup>145</sup>See, e.g., *First Nat'l Maintenance Corp. v. NLRB*, 452 U.S. 666, 675 (1981) ("[B]oth employer and union may bargain to impasse over these matters and use the economic weapons at their disposal to attempt to secure their respective aims.").

<sup>146</sup>See *In re Horsehead Indus., Inc.*, 300 B.R. 573, 587 (Bankr. S.D.N.Y. 2003) ("[I]t makes little difference if the Debtors are forced out of business because of a union strike or the continuing obligation to pay union benefits to avoid one.").

<sup>147</sup>11 U.S.C. § 305 (2006).

<sup>148</sup>11 U.S.C. § 1112(b) (2006).

<sup>149</sup>Pub. L. 98-353, Title III, § 541(a) (July 10, 1984) (codified at 11 U.S.C. § 1113 (2006)).

<sup>150</sup>KEATING, *supra* note 124, § 2.1.

§ 1113 and conflicting legislative history have offered little guidance for the precise standard under which CBAs may be rejected. In practice, however, courts have used the procedural framework imposed by § 1113 to govern the substantive terms of post-petition collective bargaining.

1. *Section 1113 in theory*

Section 1113 resulted from competing legislation proposed in the wake of *Bildisco*. Proposals sought to: (1) codify *Bildisco*; (2) implement a standard under which a debtor could reject a CBA only to stave off liquidation; or (3) adopt a middle ground between these extremes.<sup>151</sup> There are no committee reports from either the House or the Senate with respect to § 1113.<sup>152</sup> There are no statements from its sponsors.<sup>153</sup> The legislative record is therefore limited to what the Tenth Circuit has accurately described as “self-serving statements by opposing partisans.”<sup>154</sup> The only source of agreement among legislators was that § 1113 enacted a higher standard than *Bildisco*, though significant disagreement remained as to the actual definition at work.<sup>155</sup>

The text of § 1113 reflects the congressional incongruity. “Courts and scholars alike have commented extensively on how poorly-drafted [§ 1113] is.”<sup>156</sup> First and foremost, Congress failed to enact a specific standard governing the rejection of CBAs. Congress shifted such responsibility back to the judiciary:

Section 1113 of the Bankruptcy Code embodies a compromise between the desires of organized labor and those of the business and creditor community. Because it is a compromise, it is loaded with terms of compromise. Interpretation of terms such as “necessary,” “fairly and equitably,” “good faith,” and “good cause,” naturally falls to the courts.<sup>157</sup>

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<sup>151</sup>See generally Bruce H. Charnov, *The Uses and Misuses of the Legislative History of Section 1113 of the Bankruptcy Code*, 40 SYRACUSE L. REV. 925 (1989).

<sup>152</sup>7 COLLIER ON BANKRUPTCY ¶ 1113.LH (Alan N. Resnick et al. eds., 15th ed. rev. 2006).

<sup>153</sup>*Id.*

<sup>154</sup>Sheet Metal Workers'Int'l Assoc. Local 9 v. Mile Hi Metal Sys., Inc. (*In re* Mile Hi Metal Sys., Inc.), 899 F.2d 887, 890 (10th Cir. 1990).

<sup>155</sup>See Charnov, *supra* note 151, at 969. The limited legislative history of § 1113 has provided at least one court with a foundation for its own construction of § 1113—however questionable such an approach might be. *Wheeling Pittsburgh Steel Corp. v. United Steelworkers of Am.*, 791 F.2d 1074, 1088 (3d Cir. 1986).

<sup>156</sup>*United Food & Commercial Workers Union, Local 211 v. Family Snacks, Inc.* (*In re* Family Snacks, Inc.), 257 B.R. 884, 891 (8th Cir. B.A.P. 2001); *accord In re Am. Provision Co.*, 44 B.R. 907, 909 (Bankr. D. Minn.1984) (“[Section] 1113 is not a masterpiece of draftsmanship.”).

<sup>157</sup>Joseph L. Cosetti & Stanley A. Kirshenbaum, *Rejecting Collective Bargaining Agreements Under Section 1113 of the Bankruptcy Code—Judicial Precision or Economic Reality?*, 26 DUQ. L. REV. 181, 183 (1987). *But see* Marc S. Kirschner et al., *Tossing the Coin Under Section 1113: Heads or Tails, the Union*

Thus, § 1113 only creates a procedural framework through which a court must ultimately make a decision regarding rejection.<sup>158</sup>

There are other gaps in § 1113. Section 1113 is the exclusive provision governing the rejection of CBAs,<sup>159</sup> but it does not create a claim for damages.<sup>160</sup> A union could then have no claim arising from rejection.<sup>161</sup> Nor does § 1113 determine what concessions—if any—a debtor must make following rejection.<sup>162</sup> Most relevant to this Article, Congress did not incorporate § 1113 into Chapter 9.<sup>163</sup>

Congress has not remedied the absence of a provision governing the rejection of CBAs in Chapter 9, though Congress has been willing to address other concerns unique to the municipal debtor.<sup>164</sup> Nor has Congress been totally unaware of this hole. In 1991, the Municipal Employee Protection Amendments Act was introduced to require that “the debtor which seeks approval of changes to a labor agreement has fully exhausted State law procedures for the bargaining, implementation, and amendment of a collective bargaining agreement . . . .”<sup>165</sup> This bill subsequently died in committee.

It should also be noted that the rejection of a CBA does not end matters with respect to a debtor’s relationship with its unions, or vice versa. “[F]ollowing rejection there will still be a union, and that union will remain the exclusive bargaining representative for its workers notwithstanding rejection.”<sup>166</sup> Rejection means only that a debtor has the opportunity to obtain different contractual terms from its union, which the union remains free to accept or reject. After all, a union’s right to strike remains largely unaffected

Wins, 23 SETON HALL L. REV. 1516 (1993) (“Section 1113 provides strict procedural and substantive requirements that a debtor must meet to reject a collective bargaining agreement.”).

<sup>158</sup>11 U.S.C. § 1113(b)-(d) (2006).

<sup>159</sup>*Id.* § 1113(a).

<sup>160</sup>*Cf.* 11 U.S.C. §§ 365(g), 502(g) (treating the rejection of an executory contract as a breach of contract giving rise to a claim for damages against the debtor’s estate).

<sup>161</sup>*In re Blue Diamond Coal Co.*, 131 B.R. 633 (Bankr. E.D. Tenn. 1991); *see also* United Food and Commercial Workers Union, Local 328 v. Almac’s Inc., 90 F.3d 1 (1st Cir. 1996) (holding that interim modifications under § 1113(e) do not give rise to claims). *But see* Michael St. Patrick Baxter, *Is There a Claim for Damages From the Rejection of a Collective Bargaining Agreement Under Section 1113 of the Bankruptcy Code?*, 12 BANKR. DEV. J. 703 (1996) (attacking *Blue Diamond*). *See generally*, KEATING, *supra* note 124, § 2.5.2.

<sup>162</sup>*See* New York Typographical Union No. 6 v. Maxwell Newspapers, Inc. (*In re Maxwell Newspapers, Inc.*), 981 F.2d 85, 91-92 (2d Cir. 1992) (conditioning rejection under § 1113 on debtor’s obligation to extend previous comprise offer to union) (discussed in Kirschner et al., *supra* note 157, at 1532-33); *accord In re Northwest Airlines Corp.*, 346 B.R. 307, 332 (Bankr. S.D.N.Y. 2006).

<sup>163</sup>*See* 11 U.S.C. § 901.

<sup>164</sup>*See* Pub. L. No. 100-597, 102 Stat. 3028 (1988) (amending 11 U.S.C. to provide certain protections for holders and issuers of industrial revenue bonds issued by municipal debtors), *reprinted in* 15 FEDERAL BANKRUPTCY LAW: A LEGISLATIVE HISTORY OF THE BANKRUPTCY REFORM ACT OF 1994, Doc. No. 278 (Bernard D. Reams, Jr. & William H. Manz, eds., 1998) (hereinafter Reams & Manz).

<sup>165</sup>H.R. 3949, 102d Cong. § 2(c) (1991), *reprinted in* 4 Reams & Manz, *supra* note 164, Doc. No. 87.

<sup>166</sup>KEATING, *supra* note 124, § 2.4.4.

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by virtue of the bankruptcy petition.<sup>167</sup> Hence, rejection does not spell doom for a union, nor does it create an absolute victory for a debtor.<sup>168</sup> The assumption or rejection of a collective bargaining agreement is but one step—albeit an important one—in a debtor’s reorganization.

## 2. Section 1113 in Practice

Courts quickly filled the gap created by Congress’s apparent refusal to define a clear standard governing the rejection of collective bargaining agreements. Perhaps unsurprisingly, the case law has reflected the congressional bipolarity regarding *Bildisco*.

The Third Circuit, in *Wheeling Pittsburgh Steel Corp. v. United Steelworkers of Am.*,<sup>169</sup> determined that a debtor’s obligation to propose “necessary modifications” under § 1113(b)(1)(A) as a condition precedent to rejection refers only to those modifications which were necessary to prevent a debtor’s short-term liquidation.

The “necessary” standard cannot be satisfied by a mere showing that it would be desirable for the trustee to reject a prevailing labor contract so that the debtor can lower its costs. Such an indulgent standard would inadequately differentiate between labor contracts, which Congress sought to protect, and other commercial contracts, which the trustee can disavow at will.<sup>170</sup>

Hence, a debtor could not reject a CBA unless and until the debtor had proposed to make only such modifications necessary to stave off liquidation.<sup>171</sup>

*Wheeling-Pittsburgh* was wrongly decided on multiple levels. First, *Wheeling-Pittsburgh* justified its standard through a self-serving view of a legislative history which is at best unclear.<sup>172</sup> Second, the *Wheeling-Pittsburgh* court could only achieve its outcome by conflating the standard for “necessary modification” under § 1113(b)(1) with the standard for interim modifications under § 1113(e): “We reject the hypertechnical argument that ‘necessary’ and ‘essential’ have different meanings because they are in different subsections. The words are synonymous.”<sup>173</sup> It is reasonable to assume that Congress would not have used different words if it wanted the same

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<sup>167</sup>See generally *id.* § 7.2.

<sup>168</sup>See *id.*

<sup>169</sup>791 F.2d 1074 (3d Cir. 1986).

<sup>170</sup>*Id.* at 1088.

<sup>171</sup>*Id.*

<sup>172</sup>Compare *id.* at 1082-89 with Section III.B.1.

<sup>173</sup>*Id.* at 1089.

standard to govern interim and permanent modifications.<sup>174</sup> One of the few points of consensus in § 1113's legislative history was that interim modifications to a CBA should be harder to obtain than permanent modifications.<sup>175</sup>

Third, *Wheeling-Pittsburgh* took a myopic view of "necessary" modifications in relation to the debtor's "reorganization" as defined by § 1113(b)(1)(A). The Third Circuit determined that "necessary" modifications only referred to those modifications which were necessary for the short-term rehabilitation of the debtor—as opposed to the debtor's long-term financial health.<sup>176</sup> Such a reading prevents a debtor from implementing more substantial and necessary changes to its overall cost structure. The *Wheeling Pittsburgh* approach also runs counter to § 1129(a)(11), which conditions plan approval on the court's determination that such a plan provides for the long-term survival of the debtor.

In *Truck Drivers Local 807 v. Carey Transportation Inc.*,<sup>177</sup> the Second Circuit endorsed a test that is more consistent both with the actual language of § 1113 and the goals of Chapter 11 generally.<sup>178</sup> *Carey Transportation* rejected any equation of "necessary" under § 1113(b)(1)(A) with "essential" under § 1113(e). The court observed that an alternative reading would effectively thwart any negotiation regarding the modifications in question:

Because the statute requires the debtor to negotiate in good faith over the proposed modifications, an employer who initially proposed truly 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.<sup>179</sup>

Instead, "the necessity requirement places on the debtor the burden of proving that the proposal is made in good faith, and that it contains necessary, but not absolutely minimal, changes that will enable the debtor to complete the reorganization process successfully."<sup>180</sup> The Second Circuit then adopted a highly discretionary series of factors through which a bankruptcy

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<sup>174</sup>*Cf.* *United Food and Commercial Workers Union, Local 328 v. Almac's Inc.*, 90 F.3d 1, 6 (1st Cir. 1996). ("[B]y providing different standards for the approval of 'rejections' and 'interim changes,' Congress clearly intended not to treat the latter as merely a category of the former.")

<sup>175</sup>Athanassios Papaioanou, *The Duty to Bargain and Rejection of Collective Bargaining Agreements Under Section 1113 by a Bankruptcy Airline: Trying to Reconcile R.L.A. With Bankruptcy Code*, 18 *TRANSP. L.J.* 219, 223-25 (1990); see Charnov, *supra* note 151, at 955.

<sup>176</sup>*Wheeling-Pittsburgh*, 791 F.2d at 1088-89; see Cosetti & Kirshenbaum, *supra* note 157, at 211.

<sup>177</sup>816 F.2d 82 (2d Cir. 1987).

<sup>178</sup>*See Bank of Am. Nat'l Trust and Savs. Assoc. v. 203 N. LaSalle St. P'Ship*, 526 U.S. 434, 453 (1999) (identifying the "the two recognized policies underlying Chapter 11" as "preserving going concerns and maximizing property available to satisfy creditors").

<sup>179</sup>*Carey Transportation*, 816 F.2d at 89.

<sup>180</sup>*Id.* at 90.

court might “balance the equities” as required by § 1113(c)(3).<sup>181</sup>

Under *Carey Transportation*, § 1113 is not a substantive rule protecting the interests of labor.<sup>182</sup> Rather, § 1113 is a procedural mechanism through which a bankruptcy judge may evaluate the proposed modifications and fairly balance all interests involved. “The purpose of [§ 1113(b)(1)(A)] . . . is to spread the burden of saving the company to every constituency while ensuring that all sacrifice to a similar degree.”<sup>183</sup> Thus, a debtor can seek the contractual modifications necessary to secure its long-term financial health, and the bankruptcy court is authorized to moderate this process.

*Carey Transportation* does not entirely fill the vacuum left by the ambiguous provisions of § 1113. *Carey Transportation* fails to identify the extent to which a particular union may be compelled to sacrifice on behalf of the reorganization as a whole.<sup>184</sup> In practice, this requires the bankruptcy judge to become an active participant in the negotiations mandated by the Bankruptcy Code in order to balance the equities at work. In other words, the judge must engage in precisely the sort of substantive review forbidden outside of bankruptcy by the NLRA.

The bankruptcy court’s actions in *In re Delta Air Lines*<sup>185</sup> are instructive. In *Delta Air Lines*, the debtor had already obtained certain wage and benefits concessions from its pilots’ and mechanics’ unions through consensual modification.<sup>186</sup> The debtor then sought “non-negotiable” wage concessions from its flight attendants’ union to meet its overall cost-savings goals. When the flight attendants refused, the debtor sought to reject their CBA under § 1113.<sup>187</sup> Judge Hardin determined that rejection was inappropriate since

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<sup>181</sup>*Id.* at 93. The non-inclusive series of factors adopted by *Carey Transportation* were: (1) the likelihood and consequences of liquidation if rejection is not permitted; (2) the likely reduction in the value of creditors’ claims if the bargaining agreement remains in force; (3) the likelihood and consequences of a strike if the bargaining agreement is voided; (4) the possibility and likely effect of any employee claims for breach of contract if rejection is approved; (5) the cost-spreading abilities of the various parties, taking into account the number of employees covered by the bargaining agreement and how various employees’ wages and benefits compare to those of others in the industry; and (6) the good or bad faith of the parties in dealing with the debtor’s financial dilemma. *Id.*

<sup>182</sup>*Cf. Wheeling-Pittsburgh*, 791 F.2d at 1088-89 (arguing that the legislative history of § 1113 demonstrates a “Congressional consensus” to enact a standard “more sensitive to the national policy favoring collective bargaining agreements”).

<sup>183</sup>*Carey Transportation*, 816 F.2d at 90 (quoting *Century Brass Prods., Inc. v. Int’l Union of United Auto., Aerospace, and Agric. Implement Workers of Am., Local 1604 (In re Century Brass Prods.)*, 795 F.2d 265, 273 (2d Cir. 1986)).

<sup>184</sup>See KEATING, *supra* note 124, § 2.5.1 (“Precisely how much better off the unsecured creditors must be made, and at what cost to the union workers whose cuts are enabling that result, are two questions that the word necessary and all of its interpretations thus far have yet to fully resolve.”).

<sup>185</sup>342 B.R. 685 (Bankr. S.D.N.Y. 2006); see also *In re Northwest Airlines Corp.*, 346 B.R. 307, 332 (Bankr. S.D.N.Y. 2006).

<sup>186</sup>*Delta Air Lines*, 342 B.R. at 689-90.

<sup>187</sup>*Id.* at 691.



## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 319

the requisite wage concessions would have wrung twenty-one percent of the projected total cost savings from the flight attendants, though they only composed ten and a half percent of total labor costs.<sup>188</sup>

It is not acceptable to say that [the debtor], by reaching agreement with the pilots and the machinists, can preempt for the flight attendants the Section 1113 process of proposal, good faith negotiations, and determinations by the Bankruptcy Court of all issues relating to necessity, fairness, good faith negotiations, good cause and balance of equities.<sup>189</sup>

The thrust of the Judge Hardin's ruling was to implicitly prescribe the terms of contractual modifications by requiring the debtor to achieve pro rata cost savings from all its unions. Indeed, the debtor was subsequently permitted to reject the CBA with its pilots' union when that union refused to grant the necessary concessions.<sup>190</sup> It is hard to imagine the NLRB dictating terms in this fashion.

Under the *Carey Transportation* standard, § 1113 departs from *Bildisco* by authorizing bankruptcy courts to require or implement substantive changes to CBAs through the negotiated process mandated by that section. *Bildisco* provides no authority for a bankruptcy court to engage in the sort of substantive actions of the *Delta Air Lines* court. Section 1113, in contrast, both enables and requires the court to condition acceptance or rejection of a CBA upon the imposition of substantive terms, and the court remains the sole arbiter of what constitutes "necessary," "fair," equitable," and the like.<sup>191</sup>

It may be argued, however, that bankruptcy court behavior would remain the same whether or not § 1113 was ever enacted. That is, one might claim that judges would "do equity" with respect to CBAs regardless of the court's statutory authority to do so. Dicta from *Bildisco* might also justify a bankruptcy court's equitable limitation of unilateral rejections.<sup>192</sup> Thus, judges

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<sup>188</sup>*Id.* at 698.

<sup>189</sup>*Id.* at 696 (emphasis added).

<sup>190</sup>*In re Delta Air Lines, Inc.*, 359 B.R. 469, 489 (Bankr. S.D.N.Y. 2006) ("It is the essence of a Chapter 11 reorganization that all economic constituencies of a debtor must make their appropriate and proportionate contribution to the debtor's reorganization in order that all may benefit from the continued viability and future success of the debtor.").

<sup>191</sup>See Cosetti & Kirshenbaum, *supra* note 157, at 183; Cameron, *supra* note 124, at 904 ("By virtually every measure, the substantive steps are relatively important to bankruptcy judges, while the procedural steps are relatively unimportant. This finding should come as a surprise to serious students of the institution of collective bargaining, which in its quintessential American form eschews government supervision of bargaining outcomes in favor of bargaining process.").

<sup>192</sup>See *Bildisco*, 465 U.S. at 524 ("We agree . . . that because of the special nature of a collective-bargaining contract, and the consequent 'law of the shop' which it creates, a somewhat stricter standard should govern the decision of the Bankruptcy Court to allow rejection of a collective-bargaining agreement." (internal citations omitted)).

could effectively require parties to accept substantive modifications to CBAs as a pre-condition of termination under § 365 much as judges are authorized to do by the broad language of § 1113.

This position is incorrect. There is a distinction between equitable powers authorized by statute and using general principles of equity to depart from the Bankruptcy Code.<sup>193</sup> One is permitted; the other is not. This distinction was recently observed in *Lamie v. United States Trustee*,<sup>194</sup> in which the Court addressed another gap in the Bankruptcy Code—created by an apparent drafting error in § 330(a). “There is a basic difference between filling a gap left by Congress’ silence and rewriting rules that Congress has affirmatively and specifically enacted.”<sup>195</sup> The procedural guidelines established by § 1113 grant the bankruptcy court discretionary authority to supervise negotiations between debtor and employer.<sup>196</sup> In the absence of § 1113, a bankruptcy court cannot invoke general principles of equity to craft a “fair” outcome.

*Bildisco* established that rejection of a CBA under § 365 is guided predominantly by whether such rejection could facilitate the reorganization of the debtor.<sup>197</sup> A bankruptcy court has no authority under § 365 to inject itself into negotiations between debtor and union regarding modifications to a CBA.<sup>198</sup> The bankruptcy court must permit rejection if such voluntary negotiations break down and a successful reorganization might otherwise be threatened.<sup>199</sup> To conclude otherwise would, in effect, treat the entirety of § 1113 as surplusage.<sup>200</sup>

This statutory principle is also reflected by the empirical data surrounding § 1113. The rate of rejection declined from sixty-seven percent between 1975–1984 to fifty-eight percent during the ten-year period following the enactment of § 1113.<sup>201</sup> “This is substantial, if not radical improvement in the prospects for the survival of collective bargaining agreements in Chapter

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<sup>193</sup>See, e.g., 11 U.S.C. §§ 105, 510(c) (2006); *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 206 (1988) (“[W]hatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code.”).

<sup>194</sup>540 U.S. 526 (2004).

<sup>195</sup>*Id.* at 538 (quoting *Mobil Oil v. Higginbotham*, 436 U.S. 618, 625 (1978)).

<sup>196</sup>See *supra* notes 185-190 and accompanying text.

<sup>197</sup>*Bildisco*, 465 U.S. at 527.

<sup>198</sup>*Id.* at 526.

<sup>199</sup>See *id.* (“At such a point, action by the Bankruptcy Court is required . . .”).

<sup>200</sup>It should be noted that 11 U.S.C. § 1114 imposes procedural requirements similar to § 1113 through which a debtor can modify benefits otherwise payable to retirees. See *In re Kaiser Aluminum Corp.*, 456 F.3d 328, 340 (3d Cir. 2006) (discussing similarity of § 1113 and § 1114). Section 1114, like § 1113, is not incorporated into Chapter 9. See 11 U.S.C. § 901. Hence, neither § 1114 nor § 1113 should have any applicability in Chapter 9. A more thorough discussion of the inapplicability of § 1114 in Chapter 9 is beyond the scope of this Article.

<sup>201</sup>Cameron, *supra* note 124, at 895-96.

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11.”<sup>202</sup> In short § 1113 has significantly affected the treatment of CBAs in comparison with the treatment of such agreements under § 365.

#### IV. CBAS IN CHAPTER 9

Since Chapter 9 does not incorporate § 1113, a municipal debtor’s motion to reject its CBAs should be governed by § 365 and the Court’s decision in *Bildisco*. A debtor should have discretion to reject a CBA without the sort of substantive intervention authorized by § 1113. In addition, *Bildisco* explicitly determined that labor laws cannot work to limit a debtor’s rights under § 365.<sup>203</sup> Thus, state law governing the effect of modification or rejection should not limit a debtor’s ability to reject an agreement any more than the NLRA could limit such rights.

However, the unique status of a municipal debtor raises two potential objections to this statutory analysis. First, did Congress intend for § 365 to displace an area of law specifically reserved for the states by the NLRA, notwithstanding Congress’s failure to enact legislation to the contrary? Second, does the constitutional status of the municipal debtor or its employees preclude the preemption of state labor law by the Bankruptcy Code?<sup>204</sup>

The correct answer to both objections should be the same. The legislative history of Chapter 9 provides no indication that Congress intended for a municipal debtor’s rights under § 365 to be limited by state labor law. If anything, the history of federal municipal bankruptcy law demonstrates Congress sought only to provide a clear avenue of relief for municipalities where state law proved insufficient. In addition, the sovereign status of a municipal debtor creates no impediment to rejection of a CBA. Certainly, a bankruptcy court’s jurisdiction over a municipal debtor may be subject to certain constitutional limitations, but these limits apply to the direct intervention by a bankruptcy court into the affairs of a municipal debtor. The intrusion of § 365 into state labor law offends no principles of state sovereignty since such law is not uniquely the province of the state legislatures. Any claims to state sovereignty are also waived by the state’s determination to allow its municipality to seek Chapter 9 relief. Furthermore, the due process rights of state employees can be sufficiently guarded by the procedures normally at work in the assumption or rejection of any executory contract in bankruptcy.

In contrast, the municipal debtor and, by extension, its employees could be irreparably damaged by denying the necessary relief available only through

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<sup>202</sup>*Id.* at 896.

<sup>203</sup>*Bildisco*, 465 U.S. at 533-34.

<sup>204</sup>U.S. CONST. amend. X; see Roby, *supra* note 16, at 974 (“Unless a state’s right to control municipal labor relations is protected by the United States Constitution, particularly the Tenth Amendment, a municipality may unilaterally impose new terms in accordance with a proper rejection of the collective bargaining agreement under Chapter 9 . . .”).

the exercise of its rights under the Bankruptcy Clause.<sup>205</sup> It cannot be forgotten that Chapter 9 is a venue of last resort for municipal debtors and their constituents. Section 109(c) imposes a series of hurdles which ensure that municipal debtors who obtain bankruptcy protection are already at the brink of collapse.<sup>206</sup> Unlike individual or corporate debtors, a municipality must obtain permission from the state to file for bankruptcy.<sup>207</sup> A municipality must negotiate with its creditors prior to bankruptcy.<sup>208</sup> Such negotiations will presumably include negotiations with municipal unions either as a matter of law if obligations are outstanding or in practice if a shortfall is imminent.<sup>209</sup> Municipalities are also the only debtors for whom insolvency is an express requirement.<sup>210</sup> The insolvency requirement, in particular, ensures that the municipal debtor who finally obtains Chapter 9 protection will be in dire financial straits: “[§ 109(c)(3)] postpones the day of reckoning while the city continues to pile on new debt at ever-increasing rates, further burdening the municipal budget and guaranteeing that each creditor will receive less value in bankruptcy.”<sup>211</sup>

Nor is the liquidation of a municipal entity a realistic possibility in most cases.<sup>212</sup> Rather, “the premise of municipal bankruptcy law is that the city will emerge from bankruptcy in the same form—with the same boundaries, resources, functions, and governing structure—with which it entered bankruptcy.”<sup>213</sup> Unlike Chapter 11, Chapter 9 is not primarily concerned with the efficient disposition of a debtor’s assets.<sup>214</sup> A bankruptcy court cannot

<sup>205</sup>U.S. CONST. art. I, § 8 cl. 4.

<sup>206</sup>See McConnell & Picker, *supra* note 15, at 455; see generally Eric W. Lam, *Municipal Bankruptcy: The Problem With Chapter 9 Eligibility—A Proposal to Amend 11 U.S.C. § 109(c)(2)*, 22 ARIZ. ST. L.J. 625 (1988).

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<sup>207</sup>11 U.S.C. § 109(c)(2) (2006) (municipal debtor must be authorized by state law or equivalent to file for bankruptcy); see *In re Westport Transit Dist.*, 165 B.R. 93 (Bankr. D. Conn. 1994) (discussing municipal debtor’s authority to file for bankruptcy under Connecticut law); *In re City of Wellston*, 43 B.R. 348 (Bankr. E.D. Mo. 1984) (discussing municipal debtor’s authority to file for bankruptcy under Missouri law).

<sup>208</sup>11 U.S.C. § 109(c)(5).

<sup>209</sup>See, e.g., Fossey & Sendor, *supra* note 16, at 134-36 (describing bankruptcy of Copper River School District after failure to obtain wage concessions from its teachers’ union); Winograd, *supra* note 12, at 231 (describing bankruptcy of San José Unified School District after its inability to obtain wage concessions from its teachers’ union).

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<sup>210</sup>11 U.S.C. § 109(c)(3); see *In re City of Bridgeport*, 129 B.R. 332 (Bankr. D. Conn. 1991) (discussing § 109(c)(3)).

<sup>211</sup>McConnell & Picker, *supra* note 15, at 457.

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<sup>212</sup>The liquidation of municipalities is generally the province of state law. See 6 COLLIER ON BANKRUPTCY, *supra* note 152, ¶ 901.04[36][a]. Hence, a bankruptcy court has no authority to order or compel the liquidation of a municipal debtor. See 11 U.S.C. § 943(b)(4) (2006).

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<sup>213</sup>McConnell & Picker, *supra* note 15, at 470 (“[M]unicipal bankruptcy is based on the idea of the fresh start rather than the efficient reconfiguration of assets.”).

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<sup>214</sup>Compare *id.* with *Jackson*, *supra* note 25, at 894.

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order a municipal debtor to dispose of any particular asset at all.<sup>215</sup> The goal of any municipal reorganization is to provide swift and sure relief to a debtor for whom no other avenues of relief are open.<sup>216</sup> In this sense, *Bildisco's* recognition that a debtor “is empowered by virtue of the Bankruptcy Code to deal with its contracts and property in a manner it could not have done absent the bankruptcy filing”<sup>217</sup> fits squarely within the basic purpose of Chapter 9: allowing municipal debtors to return to the business of serving its citizens.

#### A. THE LEGISLATIVE HISTORY OF CHAPTER 9 AND CBAs

Municipal debtors did not obtain the ability to reject executory contracts until 1976.<sup>218</sup> Perhaps because of this relative novelty, it has been argued through legislative history that Congress did not intend for municipal debtors to unilaterally reject their collective bargaining agreements without also being subject to the terms and obligations otherwise imposed by state labor law.<sup>219</sup> Under this view, a debtor may be permitted to reject an MOU as a matter of bankruptcy law, but the debtor should remain bound by the substantive obligations of state law, such as an obligation to maintain pre-rejection contractual terms during negotiations.<sup>220</sup> This argument is buttressed by constitutional limitations upon the scope of a bankruptcy court’s authority over the municipal debtor, now codified at §§ 903 and 904.<sup>221</sup>

Reliance on legislative history is misplaced. No congressional consensus ever emerged as to whether state law either could or should limit a debtor’s ability to reject an MOU. The legislative history is only conclusive of Congress’s recognition that a municipal debtor could reject its MOUs by virtue of its general ability to reject executory contracts. Nor has Congress ever imposed additional requirements upon the municipal debtor despite its awareness that no specific provision, such as § 1113, is applicable to Chapter 9.

##### 1. *The 1976 Amendments*

In 1975 and 1976, a spate of municipal fiscal crises—notably the financial woes of New York City—motivated Congress to implement substantial changes to Chapter IX of the Bankruptcy Act (1976 Amendments).<sup>222</sup> The

<sup>215</sup>See 11 U.S.C. § 904(2).

<sup>216</sup>See McConnell & Picker, *supra* note 15, at 469-71.

<sup>217</sup>*Cf.* NLRB v. Bildisco & Bildisco, 465 U.S. 513, 528 (1984).

<sup>218</sup>See *infra* note 226.

<sup>219</sup>Winograd, *supra* note 12, at 278.

<sup>220</sup>See *supra* Section II.C. (discussing state public sector collective bargaining law).

<sup>221</sup>See *infra* notes 281-286 and accompanying text.

<sup>222</sup>Pub. L. No. 94-260, 90 Stat. 315 (amending former 11 U.S.C.); see H.R. REP. NO. 94-686, at 3 (1976), reprinted in 1976 U.S.C.C.A.N. 539, 541 (discussing purpose of 1976 Amendments); 121 CONG. REC. 39,408 (daily ed. Dec. 9, 1975) (statement of Rep. Murphy) (“The recent developments in New York

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1976 Amendments form the basis of Chapter 9 as enacted by the Bankruptcy Reform Act of 1978.<sup>223</sup>

Generally, the 1976 Amendments sought to make bankruptcy an available forum through which municipalities could seek financial health, particularly given the unique restrictions imposed on municipal debtors:

Chapter IX provides essentially for Federal court supervision of a settlement between the petitioner municipality and a majority of its creditors. A municipal unit cannot liquidate its assets to satisfy its creditors totally and finally. Therefore, the primary purpose of a Chapter IX is to allow the municipal unit to continue operating while it adjusts or refinances creditor claims with a minimum (and in many cases, no) loss to its creditors.<sup>224</sup>

Part of this solution was to give municipal debtors increased flexibility with respect to the management of their financial obligations.<sup>225</sup>

One of the major changes imposed by the 1976 Amendments was to permit municipal debtors to assume or reject executory contracts on the same basis as private debtors under the newly-created section 82(b)(1).<sup>226</sup> This provision was intended to give municipalities much-needed powers to restructure beleaguered finances. In doing so, Congress understood that such a power could allow a municipal debtor to reject its collective bargaining obligations.<sup>227</sup> Yet nothing in the 1976 Amendments explicitly limited the effect of section 82(b)(1) with respect to CBAs,<sup>228</sup> though certain unions apparently lobbied Congress for such an exception.<sup>229</sup>

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City show the need for a workable procedure for municipalities which find themselves in a financially distressed situation.”)

<sup>223</sup>See S. REP. NO. 95-989, at 9 (1978) *reprinted in* 16 ALAN N. RESNICK & EUGENE M. WYPYSKI, *BANKRUPTCY REFORM ACT OF 1978: A LEGISLATIVE HISTORY* (William S. Hein & Co. 1979) (“Since [the 1976 Amendments] there have been no developments in municipal arrangement proceedings to require any new revision of the law. Thus, the bill tracks the provisions of Public Law 94-260 with stylistic changes to conform to the title.”).

<sup>224</sup>H.R. REP. NO. 94-686, at 6 (1976), *reprinted in* 1976 U.S.C.C.A.N. 539, 543.

<sup>225</sup>H.R. REP. NO. 94-686 at 12, *reprinted in* 1976 U.S.C.C.A.N. 539, 549 (“The bill gives broad discretion to the petitioner and the court in developing and approving the plan.”).

<sup>226</sup>Pub. L. No. 94-260, 90 Stat. 315, 316 (1976) (amending former 11 U.S.C.); see H.R. REP. NO. 94-686, at 8, *reprinted in* 1976 U.S.C.C.A.N. 539, 546 (“The bill grants the court . . . powers which a bankruptcy court has under Chapters X and XI, and under section 77, but which had not previously been granted under Chapter IX. The first is the power to permit the petitioner to reject executory contracts.”).

<sup>227</sup>H.R. REP. NO. 94-686 at 8, *reprinted in* 1975 U.S.C.C.A.N. 539, 546.

<sup>228</sup>Kenneth W. Bond, *Municipal Bankruptcy Under the 1976 Amendments to Chapter IX of the Bankruptcy Act*, 5 *FORDHAM URB. L. J.* 12 (1976) (“New Chapter IX has no special provisions for handling the rejection of executory contracts with municipal labor unions.”).

<sup>229</sup>Supplemental Views of Messrs. Butler, Kindness, Hutchinson, McClory, Moorhead of California, and Hude, with Mr. Wiggins Concurring in Part and Dissenting in Part, *reprinted in* 1976 U.S.C.C.A.N. 577, 578 (“We understand that conversations took place between certain members of the Committee staff

Different interpretations emerged as to the scope of section 82(b)(1) with respect to collective bargaining agreements.<sup>230</sup> The House majority agreed that a municipal debtor could be entitled to reject its CBAs under the same standard by which private debtors might reject such agreements.<sup>231</sup> The House Report endorsed private sector cases such as *Shopmen's Local Union No. 455 v. Kevin Steel*<sup>232</sup> and *Brotherhood of Railway Employees v. REA Express, Inc.*<sup>233</sup> as examples of how a municipal debtor may be able to reject its CBAs.<sup>234</sup> Of course, *REA Express* and *Kevin Steel* are "two different formulations of a standard for rejecting collective bargaining agreements."<sup>235</sup> Indeed, *Bildisco* refused to infer legislative intent to create a heightened standard governing the rejection of a collective bargaining specifically because of this confusion. "[T]he [House Report] indicates no preference for either formulation. At most, the House Report supports only an inference that Congress approved the use of a somewhat higher standard than the business judgment rule when appraising a request to reject a collective-bargaining agreement."<sup>236</sup>

The House Report also suggests that state law may impose additional burdens post-rejection:

[I]f a collective bargaining agreement had been rejected, applicable law may provide a process or procedure for the renegotiation and formation of a new collective bargaining agreement. A rejection would also be sufficiently similar to a termination of such a contract so that again, applicable law, if any, would apply to the rights of the other contracting

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and representatives of one or more municipal employee unions of the City of New York in an unsuccessful effort to obtain an agreement to exclude by amendment collective bargaining agreements from those executory contracts which may be rejected.").

<sup>230</sup>But see Winograd, *supra* note 12, at 278 ("The 1976 reforms evidence Congressional solicitude for state interests"). Professor Winograd's contention that the legislative history of the 1976 Amendments implies that a municipal debtor's right to terminate an MOU may be limited by state law relies heavily on the opinion of the House majority and floor statements of Representative Herman Badillo (D. N.Y.). See *id.* at 279-80. As discussed below, neither source is conclusive with respect to the legislative intent guiding the proper limits of section 82(b). The reliability of Representative Badillo's statement as to the legislative intent of section 82(b)(1), in particular, may be questioned. See *infra* notes 249-250 and accompanying text.

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<sup>231</sup>See H.R. REP. NO. 94-686, at 17-18, *reprinted in* 1976 U.S.C.C.A.N. 539, 555.

<sup>232</sup>519 F.2d 698 (2d Cir. 1975).

<sup>233</sup>523 F.2d 164 (2d Cir. 1975).

<sup>234</sup>H.R. REP. NO. 94-686, at 18, *reprinted in* 1976 U.S.C.C.A.N. 539, 555.

<sup>235</sup>*NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 525 (1984).

<sup>236</sup>*Id.* See *Bildisco*, 465 U.S. at 524 ("[B]ecause of the special nature of a collective-bargaining contract, and the consequent 'law of the shop' which it creates, a somewhat stricter standard should govern the decision of the Bankruptcy Court to allow rejection of a collective-bargaining agreement. (internal citation omitted)).

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party between rejection and conclusion of the bargaining process.<sup>237</sup>

This statement implies that “applicable” state law could still bind a debtor to the substantive terms of a CBA—even after rejection.<sup>238</sup> Professor Lawrence King, for one, viewed this approach as the proper outcome for the rejection of a CBA under section 82(b)(1).<sup>239</sup> Yet the House Report makes no conclusive statements as to the effect of rejection. The Report does not state that a debtor should or must be obliged to maintain existing terms post-rejection, as would be the case under New York law. The Report addresses only how state law could determine the procedure by which a new contract might be formed. Nor are CBAs really “sufficiently similar” to executory contracts generally.<sup>240</sup>

The House Report may have also misunderstood the proper scope of a debtor’s power to reject an executory contract. The Report’s citation to both *Kevin Steel* and *REA Express* suggests the House had difficulty coming to terms with the extent of a debtor’s rights under section 82(b)(1). Moreover, it is hard to believe that the House would consciously authorize debtors to reject CBAs and yet allow state law to bind debtors to the pre-rejection terms of such agreements.<sup>241</sup> This outcome would effectively eliminate the right to reject CBAs and was precisely why *Bildisco* determined that rejection under § 365 could not constitute an unfair labor practice under the NLRA.<sup>242</sup>

The ambiguity of the House Report motivated certain House members to amend the legislative history of the 1976 Amendments with their “Supplemental Views.”<sup>243</sup> In contrast to the indefinite language of the House majority, the Supplemental Views spoke in the most direct terms possible:

The Committee report indicates that even though executory collective bargaining agreements may be rejected, certain col-

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<sup>237</sup>H.R. REP. NO. 94-986 at 9, *reprinted in* 1976 U.S.C.C.A.N. 539, 546.

<sup>238</sup>*See, e.g.*, N.Y. CIV. SERV. LAW § 209-a(1)(e) (1999).

<sup>239</sup>Lawrence P. King, *Municipal Insolvency: Chapter IX, Old and New; Chapter IX Rules*, 50 AM. BANKR. L.J. 55, 62 (1976) (“The labor law is an exercise of the governmental power. Additionally, if such law requires that current conditions of employment be maintained during the bargaining process, that requirement would, presumably be enforceable under Chapter IX.”).

<sup>240</sup>*See supra* Section II.

<sup>241</sup>*Cf. In re Sanitary & Improvement Dist.*, No. 7, 98 B.R. 970, 974 (Bankr. D. Neb. 1989) (“To create a federal statute based upon the theory that federal intervention was necessary to permit adjustment of a municipality’s debts and then to prohibit the municipality from adjusting such debts is not, in the point of view of this Court, a logical or necessary result.”).

<sup>242</sup>*Bildisco*, 465 U.S. at 528; *see also Executory Labor Contracts*, *supra* note 16, at 969.

<sup>243</sup>*See* Supplemental Views of Messrs. Butler, Kindness, Hutchinson, McClory, Moorhead of California, and Hude, with Mr. Wiggins Concurring in Part and Dissenting in Part, *reprinted in* 1976 U.S.C.C.A.N. 577, 577.



## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 327

lective bargaining agreements may have to be renegotiated pursuant to State law and existing terms and conditions of employment would have to be maintained subsequent to rejection subsequent to rejection because of certain provisions of State law. Nothing could be further from the truth. No evidence was taken or memoranda of law submitted to the Committee for discussion on that point. No discussion of this matter took place in the Subcommittee or the full Committee.<sup>244</sup>

Under the view of these representatives, state law could not be used as a means of limiting a debtor's ability to terminate a CBA.<sup>245</sup>

Though the Conference Committee Report<sup>246</sup> to the 1976 Amendments makes no reference to either the Supplemental or the House Majority view, the Senate seems to have adopted the view of the House minority. Senator Quentin Burdick (D. N.D.), a Senate manager for the 1976 Amendments, addressed the issue point-blank in floor debate with Senator Roman Hruska (R. Neb.), a fellow manager of the 1976 Amendments:

In any case where the labor laws conflict with the powers of the petitioner under this Act, it is the intent of the legislation that the Federal, State, and local labor laws should be overridden. . . . I want to make it clear that [the bankruptcy court] will not be obligated to follow state or local law in that regard.<sup>247</sup>

Conversely, floor debate on the same day saw Representative Herman Badillo (D. N.Y.), a House manager of the 1976 Amendments, take a decidedly different view on the application of state law with respect to section 82(b)(1). In Representative Badillo's view, a municipal debtor's collective bargaining obligations imposed by state law would subsist even after rejection.<sup>248</sup> But the reliability of Representative Badillo's statements as indicia of legislative consensus may be questioned. The bulk of Representative Badillo's statement was comprised of a memorandum analyzing the 1976 Amendments prepared by the law firm of Fried, Frank, Harris, Shriver &

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<sup>244</sup>*Id.* at 577-78.

<sup>245</sup>*See id.* at 578.

<sup>246</sup>H.R. REP. NO. 94-938, at 15-16 (1976), *reprinted in* 1976 U.S.C.C.A.N. 583, 585-86.

<sup>247</sup>122 CONG. REC. 8217 (daily ed. Mar. 25, 1976) (statement of Sen. Burdick). This statement occurred in a debate between Senator Burdick and Senator Hruska largely devoted to the collective bargaining issue. The relevant portion of the debate is reproduced in the Appendix.

<sup>248</sup>*See id.* at 7971 (statement of Rep. Badillo) ("The pension provisions of collective bargaining agreements affecting the Retirement Systems are implemented by New York State law, and entrenched by the State Constitution . . .").

Jacobson (Fried Frank).<sup>249</sup> Fried Frank prepared this memorandum on behalf of the American Federation of State, County and Municipal Employees.<sup>250</sup>

In the final analysis, the legislative history of the 1976 Amendments cannot justify any limitation on a debtor's ability to reject an MOU imposed by state law. The House majority seems to have taken the view that state law might govern the effect of rejection, but the House Report included no obligatory language to that effect, nor did the Report even define a clear standard governing rejection. This ambiguity is contrasted by the unequivocal views of dissenting House members, and the leading proponents of the 1976 Amendments in the Senate. Against this jumbled history must also be weighed Congress's failure to enact specific limitations on a debtor's rights under section 82(b)(1) though it knew municipal debtors could use such rights to reject MOUs.

## 2. Legislative History post-1976

The 1976 Amendments form the basis of Chapter 9 as it currently exists under the Bankruptcy Code,<sup>251</sup> and the Bankruptcy Reform Act of 1978 incorporated section 82(b)(1).<sup>252</sup> Though the House Report to the Bankruptcy Reform Act did not address the issue of rejection and collective bargaining, the Senate provided the following gloss in its section-by-section analysis of Chapter 9:

Within the definition of executory contracts are collective bargaining agreements between the city and its employees. Such contracts may be rejected despite contrary State laws. Courts should readily allow the rejection of such contracts where they are burdensome, the rejection will aid the municipality's reorganization and in consideration of the equities of each case. On the last point, "[e]quities in favor of the city in chapter 9 will be far more compelling than the equities in favor of the employer in chapter 11. Onerous employment obligations may prevent a city from balancing its budget for some time. . . ." Rejection of the contracts may require the municipalities to renegotiate such contracts by state collective bargaining laws. It is intended that the power to reject collective bargaining agreements will pre-empt state termina-

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<sup>249</sup>*Id.*

<sup>250</sup>*Id.*

<sup>251</sup>See *supra* note 223 and accompanying text.

<sup>252</sup>H.R. REP. NO. 95-595, 395 (1977), reprinted in 13 Resnick & Wypyski, *supra* note 223 ("The applicability of section 365 incorporates the general power of a bankruptcy court to authorize the assumption or rejection of executory contracts or unexpired leases found in other chapters of the title. This section is comparable to section 82(b)(1) of current law.").

tion provisions, but not state collective bargaining laws. Thus, a city would not be required to maintain existing employment terms during the renegotiation period.<sup>253</sup>

It seems the Senate adhered to its previous view that a municipal debtor’s ability to reject collective bargaining agreements could not be limited by the operation of state labor laws. State law might provide the procedural mechanisms by which such contracts might be re-negotiated, but state law could not require a municipality to “maintain existing terms.”

And, as noted above, the Municipal Employee Protection Amendments Act of 1991 was a failed attempt to compel municipal debtors to “fully exhaust[ ] State law procedures for the bargaining, implementation, and amendment of a collective bargaining agreement.”<sup>254</sup> The implication of the Municipal Employee Protection Amendments is that the substantive or procedural requirements of state law do not limit a debtor’s rights under Chapter 9 in its present form.<sup>255</sup>

B. THE CONSTITUTIONAL STATUS OF THE CHAPTER 9 DEBTOR AND ITS EMPLOYEES

A Chapter 9 bankruptcy may impose unique constitutional restrictions on a debtor’s rights in bankruptcy, or, more accurately, a bankruptcy court’s authority to supervise the affairs of a municipal debtor. These constitutional concerns are currently reflected by §§ 903 and 904, but these sections embody a legal tradition that pre-dates the Bankruptcy Code.<sup>256</sup> The Court’s recent jurisprudence suggests that constitutional guarantees of state sovereignty are not violated by a municipal debtor’s independent exercise of bankruptcy-specific rights.<sup>257</sup>

<sup>253</sup>S. REP. NO. 95-989, at 112 (1978), reprinted in 16 Resnick & Wypinski, supra note 223 (emphasis added) (alteration in original) (quoting *Executory Labor Contracts*, supra note 16, at 965). Professor Winograd notes that the Senate Report “mischaracterizes” the cited article. Winograd, supra note 12, at 281 (“Rather than a preemption analysis, the commentator proposed using [a] ‘new entity’ theory to justify construction of state laws so that a duty to bargain would continue, but post-rejection maintenance of terms would not be required.”). This criticism is valid but irrelevant. A debtor would not be obliged to maintain pre-rejection contractual obligations on a post-rejection basis under either the commentator’s approach or its characterization by the Senate Report. See *Executory Labor Contracts*, supra note 16, at 973 (“State law would then present no bar to a city’s unilateral alteration of employment terms after rejection.”).

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<sup>254</sup>H.R. 3949, 102d Cong. § 2(c) (1991), reprinted in 4 Reams & Manz, supra note 164, at Doc. No. 278.

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<sup>255</sup>See *In re County of Orange*, 179 B.R. 177, 183 n.15 (Bankr. C.D. Cal. 1995) (“This section would have forced a Chapter 9 debtor to comply with its collective bargaining agreement; however, it was never enacted into law.”).

<sup>256</sup>McConnell & Picker, supra note 15, at 435, 446.

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<sup>257</sup>See *Cent. Va. Cmty. Coll. v. Katz*, 546 U.S. 356, 362 (2006) (“[Bankruptcy] does not implicate States’ sovereignty to nearly the same degree as other kinds of jurisdiction.” (citing *Tenn. Student Assistance Corp. v. Hood*, 541 U.S. 440, 450-51 (2004))).

As early as 1884, the Supreme Court had determined that federal courts could not make fiscal determinations on behalf of municipal debtors in *City of East St. Louis v. United States ex. rel. Zebley*.<sup>258</sup> In *Zebley*, the debtor municipality had been ordered by the court to levy certain taxes and to use the proceeds to pay its creditor.<sup>259</sup> The Supreme Court held that the district court lacked jurisdiction to issue such an order. Federal courts could not become the de facto mayors of state municipalities: “[T]he question, what expenditures are proper and necessary for the municipal administration, is not judicial; it is confided by law to the discretion of the municipal authorities. No court has the right to control that discretion, much less to usurp and supersede it.”<sup>260</sup>

In 1934, Congress enacted its first statute governing municipal bankruptcies in response to the fiscal crises and municipal defaults created by the Great Depression.<sup>261</sup> The 1934 Act was held unconstitutional on grounds similar to *Zebley* in *Ashton v. Cameron County Water Improvement District No. 1*.<sup>262</sup> In *Ashton*, the bankrupt municipality had sought to adjust its pre-bankruptcy debts through a reorganization plan authorized by the 1934 Act.<sup>263</sup> The Court, in a 5-4 opinion written by Justice McReynolds, determined that the Act improperly interfered with the affairs of a sovereign state entity. Specifically, the Act afforded rights to the state entities that would be unavailable outside of bankruptcy:

The especial purpose of all bankruptcy legislation is to interfere with the relations between the parties concerned—to change, modify, or impair the obligation of their contracts. The statute before us expresses this design in plain terms. It undertakes to extend the supposed power of the federal government incident to bankruptcy over any embarrassed district which may apply to the court.<sup>264</sup>

In the majority’s view, this represented an unconstitutional intrusion into the affairs of a state creature: “If obligations of States or their political subdivisions may be subjected to the interference here attempted, they are no longer free to manage their own affairs; the will of Congress prevails over

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<sup>258</sup>110 U.S. 321 (1884)

<sup>259</sup>*Id.* at 322-23; *cf.* 11 U.S.C. § 904(1) (barring a bankruptcy court from interfering with “any of the political or governmental power of [a] debtor”).

<sup>260</sup>*Zebley*, 110 U.S. at 324.

<sup>261</sup>Pub. L. No. 251, 48 Stat. 798 (1934); *see generally* McConnell & Picker, *supra* note 15, at 427-29 (discussing evolution of federal municipal bankruptcy law).

<sup>262</sup>298 U.S. 513 (1936).

<sup>263</sup>*Id.* at 523-24.

<sup>264</sup>*Id.* at 530.

## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 331

them.”<sup>265</sup>

Justice Cardozo, writing in dissent, argued that any concerns for state sovereignty were outweighed by both the compelling public interest in permitting municipalities to obtain bankruptcy protection<sup>266</sup> and the federal government’s constitutional mandate to create uniform bankruptcy laws.<sup>267</sup> Justice Cardozo also delivered a strong reminder of bankruptcy’s unique status within our federal system: “To read into the bankruptcy clause an exception or proviso to the effect that there shall be no disturbance of the federal framework by any bankruptcy proceeding is to do no more than has been done already with reference to the power of taxation by decisions known of all men.”<sup>268</sup>

By comparison, Justice McReynolds’ logic is “exceptionally weak.”<sup>269</sup> The *Ashton* majority provided no justification for its choice to set aside the federal government’s constitutional authority to create “uniform Laws on the subject of Bankruptcies throughout the United States”<sup>270</sup> in favor of vague notions of state sovereignty. There is no question that a bankruptcy court—as in *Zebley*—goes too far when it makes policy determinations on behalf of the debtor: setting the levels of taxation, determining expenditures, and so forth.<sup>271</sup> No such constitutional limits are implicated where a bankruptcy court permits a debtor to independently exercise rights inherent to its bankruptcy petition.<sup>272</sup> The difference may be one of degree—but such degrees cannot be overlooked.<sup>273</sup>

Congress responded to *Ashton* by enacting a second municipal bankruptcy act in 1937 (1937 Act).<sup>274</sup> The Court was asked to address the constitutionality of the 1937 Act less than a year later in *United States v. Bekins*.<sup>275</sup> *Bekins* involved a proposed reorganization plan through which a municipality sought to refinance its pre-petition debts through revenues from the debtor’s tax authority.<sup>276</sup> Certain creditors claimed the Act violated the

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<sup>265</sup>*Id.*

<sup>266</sup>*Id.* at 533 (Cardozo, J., dissenting).

<sup>267</sup>*Id.* at 534.

<sup>268</sup>*Id.* at 538.

<sup>269</sup>McConnell & Picker, *supra* note 15, at 451.

<sup>270</sup>U.S. CONST. art. I § 8, cl. 4.

<sup>271</sup>*See, e.g., In re Sanitary & Improvement Dist. No. 7*, 96 B.R. 966, 967 (Bankr. D. Neb. 1989) (holding bankruptcy court has no jurisdiction to rule on municipal debtor’s use of revenues).

<sup>272</sup>*See id.* (“The debtor is vested with its property and is subject to state law concerning its distribution. This Court may not approve or disapprove of its disposition, except in contemplation of plan confirmation.”).

<sup>273</sup>*Cf. Int’l News Serv. v. Assoc. Press*, 248 U.S. 215, 247-48 (1918) (Holmes, J., dissenting) (“It is a question of how strong an infusion . . . is necessary to turn a flavor into a poison.”).

<sup>274</sup>Pub. L. No. 302, 50 Stat. 653 (1937).

<sup>275</sup>304 U.S. 27 (1938).

<sup>276</sup>*Id.* at 45-46.

Fifth and Tenth Amendments.<sup>277</sup>

Though the 1937 Act was largely identical to its predecessor,<sup>278</sup> Chief Justice Hughes made it quite clear that rights made available to a municipality in bankruptcy did not offend state sovereignty where those rights were exercised with respect to the debtor's reorganization:

The statute is carefully drawn so as not to impinge upon the sovereignty of the State. The State retains control of its fiscal affairs. The bankruptcy power is exercised in relation to a matter normally within its province and only in a case where the action of the taxing agency in carrying out a plan of composition approved by the bankruptcy court is authorized by state law.<sup>279</sup>

Though the majority made no mention of *Ashton*, the case was clearly overruled in substance if not in form.<sup>280</sup>

When viewed through the spectrum created by *Zebley*, *Ashton*, and *Bekins*, the correct conclusion is that a bankruptcy court improperly intrudes upon state sovereignty only where it directly involves itself in the day-to-day operations of the municipality.<sup>281</sup> A bankruptcy court cannot tell a debtor which debts to pay or which streets to sweep. Indeed, a court could not tell a debtor which agreement to reject or the extent of permissible modifications—as might be possible in Chapter 11.<sup>282</sup> But a debtor can exercise all those rights independently.

These constitutional principles are presently reflected by the general reservation of municipal power codified at § 903 and the specific provisions at work in § 904.<sup>283</sup> For instance, a bankruptcy court that sought to make budgetary determinations on behalf of the municipal debtor would clearly

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<sup>277</sup>*Id.* at 46.

<sup>278</sup>*McConnell & Picker*, *supra* note 15, at 452; *Winograd*, *supra* note 12, at 272.

<sup>279</sup>*Bekins*, 304 U.S. at 51.

<sup>280</sup>*See* *McConnell & Picker*, *supra* note 15, at 452 (“In his argument before the Court, Solicitor General Robert Jackson all but admitted that the sections of the statute applicable to political subdivisions of the State would be unconstitutional under *Ashton*, but quoted a member of Congress to the effect that ‘it was not only the right, but the duty of Congress to present the question once more to this Court, since the decision, if allowed to stand, threatened grave impairment to the powers of the States.’” (citation omitted)).

<sup>281</sup>*See* 6 COLLIER ON BANKRUPTCY, *supra* note 152, ¶ 904.01[2].

<sup>282</sup>*Cf. In re Delta Air Lines*, 342 B.R. 685 (Bankr. S.D.N.Y. 2006) (refusing to permit rejection of CBA where debtor had not sought pro rata concessions from its unions).

<sup>283</sup>*In re Addison Cmty. Hosp.*, 175 B.R. 646, 649 (Bankr. E.D. Mich. 1994) (“The foundation of § 904 is the doctrine that neither Congress nor the courts can change the existing system of government in this country. . . . [C]hapter 9 was created to give courts only enough jurisdiction to provide meaningful assistance to municipalities that require it, not to address the policy matters that such municipalities control.” (internal citations omitted)).

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## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 333

violate the constitutional limitations articulated by § 904(2).<sup>284</sup> Indeed, §§ 903 and 904 ensure that a municipal debtor can maintain profligate spending habits even in bankruptcy.<sup>285</sup> A Chapter 11 debtor-in-possession, by comparison, could be divested of such rights through a bankruptcy court's power to appoint a trustee.<sup>286</sup>

State sovereignty is not implicated where state labor law is displaced by § 365. State labor law holds no special position of constitutional significance following the Court's opinion in *Garcia*,<sup>287</sup> (with the exception of the procedural rights of state employees, discussed below). Congress may eliminate the exemption for state employers carved out by section 2(2)<sup>288</sup> of the NLRA or create independent legislation governing the CBAs of state employers.<sup>289</sup>

Any attempt to limit a debtor's rights under § 365 through recourse to state sovereignty must also be weighed against the filing requirements unique to Chapter 9. As noted above, a state must consent to the bankruptcy of its municipality as a condition precedent to the filing.<sup>290</sup> Such a requirement should eliminate any objection to rights available under the Bankruptcy Code predicated on state sovereignty. Since the state must consent to a bankruptcy filing under § 109(c)(2), the state consents to the displacement of its own law in order to obtain the benefits uniquely available under the Bankruptcy Code. This principle was recognized by *Bekins*:

The bankruptcy power is competent to give relief to debtors in such a plight and, if there is any obstacle to its exercise in the case of the districts organized under state law it lies in the right of the State to oppose federal interference. The State steps in to remove that obstacle. The State acts in aid, and not in derogation, of its sovereign powers.<sup>291</sup>

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<sup>284</sup>See *In re County of Orange*, 179 B.R. 195, 200 (Bankr. C.D. Cal. 1995) (holding that § 904(2) bars a court from ordering a debtor to make interim payments to professionals); accord *In re Castle Pines North Metro. Dist.*, 129 B.R. 233, 233 (Bankr. D. Colo. 1991) (noting that it is "fairly obvious" that § 904(2) would be violated if the Court ordered the District to make interim payments to counsel for the Creditors' Committee since "it would be interfering with the revenues of the District, at least insofar as it could or would affect its cash flow"). But see *In re E. Shoshone Hosp. Dist.*, 226 B.R. 430 (Bankr. D. Idaho 1998).

<sup>285</sup>McConnell & Picker, *supra* note 15, at 462.

<sup>286</sup>*Id.* (citing 11 U.S.C. § 1104(a) (2006)).

<sup>287</sup>See *supra* Section II.B. But see *Winograd*, *supra* note 12, at 317-18 (arguing that *Garcia* should not eliminate discretionary efforts "to reconcile federal bankruptcy law with state negotiating requirements").

<sup>288</sup>29 U.S.C. § 152(2) (2006).

<sup>289</sup>See, e.g., *supra* notes 110-114 and accompanying text (discussing efforts of Representative Clay to enact federal legislation governing the collective bargaining rights of firefighters).

<sup>290</sup>11 U.S.C. § 109(c)(2) (2006).

<sup>291</sup>*Bekins*, 304 at 54; accord *In re Columbia Falls, Special Improvement Dist. No. 25*, 143 B.R. 750, 760 (Bankr. D. Mont. 1992) ("Far from interfering with the ability of the state of Montana to control its municipalities, it is concluded Montana has affirmed that its municipalities may avail themselves of the

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The Court's recent opinion in *Central Virginia Community College v. Katz*<sup>292</sup> further suggests that any lingering tension between principles of state sovereignty and federal authority to enact "uniform Laws on the subject of Bankruptcies" should be resolved in favor of the Bankruptcy Code. *Katz* determined that the Eleventh Amendment does not permit a state to assert sovereign immunity against suits initiated by a bankruptcy trustee. In the Court's view, ratification of Article I, § 8 cl. 4 effectively waived sovereign immunity with respect to the rights and privileges created by federal bankruptcy law. "In ratifying the Bankruptcy Clause, the States acquiesced in a subordination of whatever sovereign immunity they might otherwise have asserted in proceedings necessary to effectuate the *in rem* jurisdiction of the bankruptcy courts."<sup>293</sup>

If the states *implicitly* abrogated their sovereign immunity through ratification of the Bankruptcy Clause, state collective bargaining law cannot interfere with the Bankruptcy Code where a state has *explicitly* consented to the bankruptcy filing of its municipality. In this sense, *Katz* recognizes the principle of bankruptcy law made explicit by *Beckins* and Justice Cardozo's dissent in *Ashton*. Namely, bankruptcy is an extraordinary constitutional provision which may properly preempt rights and privileges normally at work outside of bankruptcy.<sup>294</sup> But the predominance and uniformity of the federal bankruptcy power with respect to conflicting state law is itself a benefit sought after by the states.<sup>295</sup> Hence, "[t]he power granted to Congress by [Article I, § 8, cl. 4] is a unitary concept rather than an amalgam of discrete segments."<sup>296</sup> As such, the "uniform" nature of the federal bankruptcy power may preempt objections to the application of bankruptcy law predicated on state sovereignty.<sup>297</sup>

It might still be argued that considerations regarding the uniform application of federal bankruptcy law should still yield to principles of state sovereignty given the unique dynamics at work in public sector collective bargaining.<sup>298</sup> Indeed, it may be asserted that *Garcia* was wrongly decided and that state labor law should retain some position of constitutional signifi-

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benefits of the federal bankruptcy process, including the modification and termination of these sorts of debts, and such does not interfere with the power of the State of Montana to control a municipality or in the exercise of the political or governmental powers of such municipality.").

<sup>292</sup>546 U.S. 356 (2006).

<sup>293</sup>*Id.* at 378.

<sup>294</sup>See Randolph J. Haines, *The Uniformity Power: Why Bankruptcy is Different*, 77 AM. BANKR. L.J. 129, 174 (2003) ("[T]he power granted to Congress by the Framers did not merely override the states' reserved legislative authority, as did the Supremacy Clause, but completely alienated . . . all of the states' sovereignty with respect to that body of law." (internal quotation marks omitted)).

<sup>295</sup>See *Katz*, 546 U.S. at 376-77.

<sup>296</sup>*Id.* at 369.

<sup>297</sup>See Haines, *supra* note 294, at 196.

<sup>298</sup>See *supra* Section II.C.



## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 335

cance singularly protected from federal intrusion by the Tenth Amendment. Under this view, state law provisions governing the modification or rejection of MOUs must remain in effect notwithstanding a bankruptcy petition or subsequent rejection. Of course, any theory of state sovereignty predicated on ignoring Supreme Court precedent may be of little practical assistance to the bankruptcy judge required to rule on a motion to reject such an agreement.

Even if the Court returns to its *National League of Cities* jurisprudence<sup>299</sup>—or if one believes that the dynamics of public sector collective bargaining distinguish *Garcia*—the fact remains that a municipality can only file for bankruptcy with the consent of the state.<sup>300</sup> Federal bankruptcy law does not impose itself over the objections of the state or interfere with a specific state policy; the bankruptcy is itself a state policy.<sup>301</sup> As *Bekins* observed, the state

invites the intervention of the bankruptcy power to save its agency which the State itself is powerless to rescue. Through its cooperation with the national government the needed relief is given. We see no ground for the conclusion that the Federal Constitution, in the interest of state sovereignty, has reduced both sovereigns to helplessness in such a case.<sup>302</sup>

A state could prevent a municipality from filing for bankruptcy where it has failed to seek good faith modifications or concessions from its unions prior to bankruptcy. A municipality would presumably be required to seek such modifications as a prerequisite to its filing under § 109(c)(5) (which requires pre-petition negotiations with creditors as a condition precedent to a Chapter 9 filing) if unpaid obligations have created a claim in favor of the unions.<sup>303</sup> But, by permitting the municipality to seek relief under Chapter 9, the state has unequivocally authorized the debtor to exercise those rights created by the filing.<sup>304</sup>

Nor can it ever be forgotten that that Chapter 9 and its predecessors

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<sup>299</sup>See *United Haulers Assoc., Inc. v. Oneida-Herkimer Solid Waste Mgmt. Auth.*, 127 S.Ct. 1786, 1810 (2007) (Alito, J., dissenting) (discussing rejection of *National League of Cities* as “analytically unsound”).

<sup>300</sup>11 U.S.C. § 109(c)(2).

<sup>301</sup>*Cf. National League of Cities v. Usery* 426 U.S. 833, 852 (1976) (“[I]nsofar as the challenged amendments operate to directly displace the States’ freedom to structure integral operations in areas of traditional governmental functions, they are not within the authority granted Congress by Art. I, § 8, cl. 3.”).

<sup>302</sup>*United States v. Bekins*, 304 U.S. 27, 54 (1938).

<sup>303</sup>See 11 U.S.C. § 101(10) (2006) (defining “creditor” as any entity holding a claim against a debtor).

<sup>304</sup>6 COLLIER ON BANKRUPTCY, *supra* note 152, ¶ 903.02[4] (“If a state has specifically authorized a municipality to file under chapter 9, that authorization should be construed as an expression of state policy

were specifically enacted to provide an extraordinary remedy of last resort for the states and their distressed subdivisions.<sup>305</sup> The 2005 strike of the New York City transit workers—notwithstanding the illegality of such action under New York law<sup>306</sup>—provides at least some indication of the extent to which state law may be unable to address extraordinary financial crises.<sup>307</sup> A Chapter 9 filing itself suggests that state law collective bargaining regime is no longer a working mechanism through which a debtor might restructure collective bargaining obligations. It is improbable that a municipal debtor would take the extraordinary step of filing for bankruptcy—let alone being permitted to file under § 109(c)(2) or § 109(c)(5)—without first seeking a negotiated, consensual settlement with its unions. Bankruptcy is more likely to be the result of failed negotiations rather than a lack of negotiations.<sup>308</sup>

And, as noted above, a municipal debtor is only eligible to file for bankruptcy when it is actually insolvent.<sup>309</sup> Requiring a municipal debtor to comply with state law as a prerequisite to rejection would be likely to drive the municipality deeper into insolvency. As listed above, many states compel a public employer to maintain pre-existing contractual terms during the course of negotiation.<sup>310</sup> Any subsequent modifications would thus become more painful for all parties involved, including the employees themselves.

Again, this is not to say that a bankruptcy court holds the same jurisdiction over a municipal debtor as it could over a Chapter 11 debtor. The *Zebly*, *Ashton* and *Bejins* trilogy clearly demonstrates that the Tenth Amendment prevents the bankruptcy court from serving as a de facto trustee over the affairs of a municipal debtor. However, the Tenth Amendment does not preclude the municipal debtor from independently availing itself of the rights and privileges attendant to an authorized filing. Section 904 would in fact prevent a bankruptcy court from imposing the substantive modifications and conditions in the fashion of the *Delta Air Lines* court. Moreover, requiring a municipality to comply with state law after the municipality has made the governmental decision to reject a CBA under § 365 would seem to violate § 904's prohibition on interference with the governmental discretion of the municipal debtor.<sup>311</sup>

It may still be argued that state law must play a necessary role to pre-

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that the benefits of chapter 9, and the application of the substantive provisions of chapter 9, are more important than any restriction on state law that might arise by reason of application of chapter 9.”)

<sup>305</sup>See *supra* Section IV.A.

<sup>306</sup>N.Y. CIV. SERV. LAW § 210 (1999).

<sup>307</sup>See *supra* note 69.

<sup>308</sup>See Winograd, *supra* note 12, at 237-40.

<sup>309</sup>See *supra* Section II.C.

<sup>310</sup>See, e.g., N.Y. CIV. SERV. LAW § 209-a(1)(e) (1999) (requiring public sector employers to maintain pre-existing payment terms pending resolution of collective bargaining negotiations).

<sup>311</sup>6 COLLIER ON BANKRUPTCY, *supra* note 152, ¶ 901.04[9][a] (“[S]uch an importation of state law

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serve the unique constitutional rights of municipal employees. As noted above, a public sector employee may hold a constitutionally-protected property interest in their job. This interest cannot be disturbed without triggering procedural due process under the Fourteenth Amendment. In this sense, requiring a debtor to comply with state law as a precursor to rejection becomes an attractive alternative to the unilateral rights afforded by § 365. Existing state law collective bargaining procedures could protect the constitutional rights of such employees. Hence, *County of Orange's* recourse to California law may have implicitly protected the due process rights of its employees, though the court did not explicitly consider this constitutional dimension in its opinion.<sup>312</sup> There is also a significant interest in preserving the pre-bankruptcy expectations of municipal employees where they are denied the same the same collective bargaining rights available to their private sector counterparts.<sup>313</sup>

But recourse to state law is an inappropriate means of protecting the interests of state employees for three reasons. First, state law or the notice provisions imposed by an MOU are not coextensive with the requirements of due process. “[A]lthough state law and practice determine the existence of a protected interest, the Constitution sets minimum procedural safeguards for such an interest that state action may not undermine.”<sup>314</sup> Second, wholesale importation of state law into the Bankruptcy Code is unnecessary to ensure compliance with the requirements of due process. The Court has consistently reminded us that the standard of procedural due process is a flexible one.<sup>315</sup> The requirements of the Fourteenth Amendment can be satisfied by any procedure which provides notice and a hearing regarding any modification to the terms or conditions of employment for a public employee. There is no reason why the notice procedures through which a court would rule on a motion to reject under § 365 could not satisfy the Fourteenth Amendment.<sup>316</sup>

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potentially runs afoul of section 904 which prohibits the court from interfering with ‘any of the political or governmental powers of the debtor.’”).

<sup>312</sup>*In re County of Orange*, 179 B.R. 177, 184 (Bankr. C.D. Cal. 1995).

<sup>313</sup>See *supra* notes 60-68 and accompanying text.

<sup>314</sup>Richard Wallace, Comment, *Union Waiver of Public Employees' Due Process Rights*, 8 INDUS. REL. L.J. 583, 593-94 (1986).

<sup>315</sup>*Cleveland Bd. of Educ. v. Loudermill*, 470 U.S. 532, 545 (“[T]he formality and procedural requisites for the hearing can vary, depending on the importance of the interests involved and the nature of the subsequent proceedings.”); *Mathews v. Eldridge*, 424 U.S. 319, 334 (1976) (“Due process is flexible and calls for such procedural protections as the particular situation demands.” (quoting *Morrissey v. Brewer*, 408 U.S. 471, 481 (1972))); see J. Michael McGuinness, *Procedural Due Process of Public Employees: Basic Rules and a Rationale for a Return to Rule-Oriented Process*, 33 NEW ENG. L. REV. 931, 935 (1999) (“Historically, the Supreme Court has emphasized a flexible procedural due process standard by employing a balancing test on a case-by-case basis to determine what process is due in a particular situation.”).

<sup>316</sup>See FED. R. BANKR. P. 6006, 9014.

Third — and most importantly — forcing a municipal debtor to comply with state law provisions governing an MOU improperly disregards the costs imposed on a municipal debtor. Any analysis into the sufficiency of procedural due process must consider affected government interests.<sup>317</sup> *Mathews* requires a comparison of the costs borne by the government and the benefits provided to employees when examining the necessity for additional process.<sup>318</sup> By definition, a municipal debtor is financially imperiled.<sup>319</sup> Forcing compliance with state law could perpetuate the debtor's financial exhaustion while failing to provide necessary relief.<sup>320</sup> Conversely, forcing a municipal debtor to comply with state collective bargaining law post-rejection would provide no incentive for public sector unions to reach any compromise in (or out) of bankruptcy. Rejection of an MOU would mean—at worst—more of the same.

## V. CONCLUSION

As noted at the outset, the absence of a well-defined body of law regarding collective bargaining agreements in municipal bankruptcy leaves serious questions as to how such agreements should be treated. This Article has attempted to answer some of those questions.<sup>321</sup> Outside of bankruptcy, federal law grants parties significant discretion to bring tools of economic warfare to bear on the collective bargaining process. In contrast, state law may impose considerable restrictions on the rights of public sector employers and employees.

Inside bankruptcy, the landscape is changed. From a statutory perspective, collective bargaining agreements are executory contracts subject to assumption or rejection. Congress enacted § 1113<sup>322</sup> of the Bankruptcy Code in order to mollify labor-specific hardships that might have arisen from the Court's opinion in *Bildisco*. This provision has authorized bankruptcy judges to play an active role in the negotiated process that now characterizes the treatment of collective bargaining agreements in Chapter 11. But Congress has not incorporated § 1113 into Chapter 9. A municipal debtor's decision to reject CBAs remains governed by § 365 and the standard promulgated by

<sup>317</sup>*Mathews*, 424 U.S. at 334.

<sup>318</sup>*Parrett v. City of Connersville*, 737 F.2d 690, 696 (7th Cir. 1984).

<sup>319</sup>See 11 U.S.C. § 109(c)(3) (2006).

<sup>320</sup>*Cf.* N.Y. CIV. SERV. LAW § 209-a(1)(e) ("It shall be an improper practice for a public employer or its agents deliberately . . . (e) to refuse to continue all terms of an expired agreement until a new agreement is negotiated, unless the employee organization which is a party to such agreement has, during such negotiations or prior to such resolution of such negotiations, engaged in [a strike] . . .").

<sup>321</sup>*Cf.* *Ashton v. Cameron County Water Improvement Dist. No. 1*, 298 U.S. 513, 535 (1936) (Cardozo, J., dissenting) ("The history [of bankruptcy] is one of an expanding concept. It is, however, an expanding concept that has had to fight its way.").

<sup>322</sup>11 U.S.C. § 1113.

## 2007) COLLECTIVE BARGAINING IN CHAPTER 9 339

*Bildisco*. This outcome is consistent with Congress's efforts to provide a clear avenue of relief for financially distressed state entities through the discharge-oriented focus of Chapter 9. To hold otherwise would be to burden the municipality with the selfsame obligations it was unable to restructure prior to bankruptcy. As *Bildisco* correctly observed, denying the rights available under § 365 by requiring compliance with an existing labor law regime could thwart the very purpose of the bankruptcy filing.

Certainly, the constitutional status of the municipal debtor and its employees raise additional questions regarding the treatment of the collective bargaining obligations. But this Article has argued that state sovereignty is not offended where state labor law is displaced by § 365. The Tenth Amendment, properly understood, prevents the bankruptcy court from replacing the executive and legislative discretion of the municipality. The Tenth Amendment does not prevent the municipality from independently exercising those rights and privileges created by virtue of its bankruptcy filing—particularly since state labor law holds no especial position of constitutional significance post-*Garcia*. Even if one concedes that *Garcia* was incorrectly decided, lingering tensions created by the Tenth Amendment should be resolved in favor of the Bankruptcy Code by virtue of the state's necessary consent to the bankruptcy of its municipality.<sup>323</sup> In addition, the procedures normally at work in bankruptcy should be sufficient to satisfy the flexible procedural requirements of the Fourteenth Amendment without wholesale recourse to state law.

Admittedly, the foregoing analysis suggests that a municipality's need to restructure its finances must come at the expense of its unions. This may undermine the significant interest in upholding the bargained-for expectations of municipal employees, since state collective bargaining law will often deny such employees the same rights available to their private sector counterparts. But a municipal debtor may have few choices when reducing costs—particularly where labor costs may comprise up to seventy percent of the municipal budget.<sup>324</sup> Moreover, the long-term interest of municipal unions as employees and as citizens of a bankrupt municipality should be better served by a swift reorganization affected through the remedies made available under the Bankruptcy Code. Any decision governing the assumption or rejection of a municipal debtor's collective bargaining obligations should be guided by this fact.

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<sup>323</sup>11 U.S.C. § 109(c)(2).

<sup>324</sup>Kapoor, *supra* note 14, at 401.

## APPENDIX

Floor Debate between Sen. Burdick and Sen. Hruska, March 25, 1976<sup>325</sup>

Mr. Hruska: The conference report and statement of managers are silent on the rejection of a collective bargaining agreement by a municipality. Could you explain the intent of the legislation in that regard?

Mr. Burdick: Yes. The Senate report in its version of the bills makes this clear on page 15. The house report has similar language on pages 8-9. The bill provides in section 82(b)(1) that the court shall have the power to permit the rejection of executory contracts by the petitioner. It is contemplated that all continuing obligations of the petitioner including collective bargaining agreements will be considered executory contracts.

Mr. Hruska: But does not the House report imply that local laws, such as those governing the negotiation and renegotiation of collective bargaining laws, might apply in such a case.

Mr. Burdick: I am familiar with the language to which you refer. To use an example, it is my understanding that some States have laws which require the negotiation or renegotiation in good faith of all collective bargaining agreements . . . . It is the intent of this legislation that any such laws should not be allowed to frustrate the purposes of the bankruptcy proceedings.

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Mr. Burdick: In any case where the labor laws conflict with the powers of the petitioner under this Act, it is the intent of the legislation that the Federal, State, and local labor laws should be overridden. . . . I want to make it clear that [the bankruptcy court] will not be obligated to follow state or local law in that regard.

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<sup>325</sup>122 CONG. REC. 8215-17 (1976).