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Chapter 11 Liquidation and its Effect on Collective Bargaining Agreements

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Introduction

Sections 1113 and 1114 of title 11 of the United States Code (the "Bankruptcy Code") allow a debtor to reject its collective bargaining agreements and payment of retiree benefits, subject to certain statutory conditions being met.[1] These provisions apply to companies that employ unionized workers who receive compensation and benefits pursuant to a collective bargaining agreement. Both sections, however, only apply to a debtor that is "reorganizing." Moreover, courts have held that section 1114, which governs the payment of insurance benefits to retirees, permits modification of obligations under a statute, such as the Coal Industry Retiree Health Benefit Act of 1992 (the "Coal Act"). This memo discusses how contractual rejection and modification can be reconciled with obligations under the Coal Act and the implications of permitting modification of obligations under the Coal Act. Part I examines the holding of *In re Alpha Nat. Res., Inc.* Part II addresses how Coal Act obligations can be reconciled with modification in bankruptcy. Part III discusses holdings in Alabama and Kentucky on modification of Coal Act obligations and the implications that follow.

[1] 11 U.S.C. §§ 1113-1114 (2012).

I. Modification of Coal Act Obligations is Permitted

A. *Application of Sections 1113 and 1114 to a Liquidating Debtor*

In bankruptcy, section 1113 allows for a debtor to reject a collective bargaining agreement if certain conditions are met.[2] A debtor must first make a proposal to the authorized representative of the employees covered by the collective bargaining agreement and provide the representative with such relevant information as is necessary to evaluate the proposal.[3] The court will then approve an application for rejection if the authorized representative has refused the debtor's proposal without good cause and the balance of equities clearly favors rejection.[4]

In order to modify retiree benefit payments, section 1114 requires the trustee to first make a proposal to the authorized representative[5] of the retirees of the employer.[6] This proposal must be based on the most complete and reliable information available at the time and must also provide for the modifications that are necessary to permit the reorganization of the debtor.[7] Treatment of the debtor and all affected parties must be fair and equitable and the trustee must meet with the authorized representative of the retirees to confer in good faith in attempting to reach mutually satisfactory modifications of the retiree benefits.[8] Finally, a court will enter an order providing for modification if: (1) the trustee made a proposal that satisfies the requirements mentioned above; (2) the authorized representative of the retirees has refused to accept such proposal without good cause; and (3) such modification is necessary to permit the reorganization

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[2] 11 U.S.C. § 1113.
[3] 11 U.S.C. § 1113(b)(1).
[4] 11 U.S.C. § 1113(c).
[5] An authorized representative is the labor organization that is a signatory to the collective bargaining agreement under which retiree benefits are covered. 11 U.S.C. § 1114(c)(1) (2012).
[6] 11 U.S.C. § 1114.
[7] *Id.*
[8] *Id.*

of the debtor and assures that all creditors, the debtor and all of the affected parties are treated fairly and equitable, and is clearly favored by the balance of equities.[9]

In *In re Alpha*, Alpha Natural Resources ("Alpha") filed a motion to reject its collective bargaining agreement and modify its obligations under the Coal Act.[10] Alpha had filed the motion because it felt it was necessary to facilitate the reorganization.[11] This is so because Alpha's pre-petition lenders agreed to serve as a stalking horse for the sale of Alpha's core assets, but refused to assume any of Alpha's liabilities and obligations under the Coal Act.[12] Alpha's pre-petition lenders were refusing to close the sale unless it was able to receive Alpha's core assets free and clear of Alpha's obligations under Alpha's collective bargaining agreements.[13]

However, sections 1113 and 1114 both use the word "reorganizing" and neither of them use the word "liquidating." This would seem to imply that both sections do not apply to an entity that is liquidating. The bankruptcy court first determined whether sections 1113 and 1114 apply to Alpha because it is liquidating.[14] Alpha's creditors argued that Alpha was liquidating and sections 1113 and 1114 only apply to those who are reorganizing.[15] However, the Court refused to adopt this reasoning and followed other courts in determining that sections 1113 and 1114 include liquidating debtors.[16]

B. *Coal Act Obligations are "Retiree Benefits"*

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[9] *Id*.
[10] *See In re Alpha Nat. Res., Inc.,* 522 B.R. 314, 318 (Bankr. E.D. Va. 2016).
[11] *See id.* at 322.
[12] *Id.*
[13] *Id.*
[14] *Id.* at 325.
[15] *Id.*
[16] *Id.*

Under the Coal Act, employers are required to continue providing health benefits coverage to retirees and the retirees' eligible beneficiaries as long as the employers remain in business.[17] In addition, a benefit plan known as the United Mine Workers of America 1992 Benefit Plan was created, which is funded by coal industry employers.[18]

The *Alpha* Court determined that obligations under the coal act are "retiree benefits" under § 1114.[19] The court did this by breaking down the term "retiree benefits" into three components: "(i) benefit payments to retirees; (ii) made under any plan, fund or program; (iii) maintained in whole or in part by a debtor."[20] Alpha's creditors argued that Coal Act obligations are not maintained in whole or in part by Alpha because it was created by Congress.[21] The court looked at a decision in a Kentucky court that addressed this issue.[22] The Kentucky court in *In re Horizon Nat. Res. Co.* determined that obligations under the Coal Act are within the meaning of "retiree benefits" under section 1114.[23] The court reasoned that Alpha contributes to the fund created by the Coal Act and therefore maintains it at least in part.[24] In doing so, the court also rejected the argument brought by Alpha's creditors that said that Congress meant for the definition of retiree benefits to apply only to private obligations.[25]

The court also had to determine whether Alpha's rejection motion was necessary to facilitate Alpha's reorganization.[26] Alpha had an immediate need to reduce its spending and

[17] 26 U.S.C. § 9711 (2012).
[18] 26 U.S.C. § 9704.
[19] *Id.* at 326.
[20] *Id.* at 327.
[21] *Id.*
[22] *Id.*
[23] *See In re Horizon Nat. Res. Co.* 316 B.R. 268 (Bankr., E.D. Ky. 2004).
[24] *Alpha*, 522 B.R. at 328.
[25] *Id.*
[26] *Id.* at 332.

balance its cash flow.[27] Reducing Alpha's obligations under the Coal Act helped to accomplish those goals while not reducing the obligations could cause Alpha to fail to timely confirm a chapter 11 plan of reorganization.[28] Therefore, the court found it was necessary to facilitate a reorganization.[29]

II. Reconciling Bankruptcy Law and Labor Law

Because Alpha was ultimately able to reject its collective bargaining agreements and modify its obligations under the Coal Act, it would appear that the Bankruptcy Code supersedes obligations under the Coal Act when modification is necessary to permit reorganization. If it is deemed necessary to facilitate reorganization, a debtor can reject collective bargaining agreements.[30] Although bankruptcy law seems to conflict with labor law, the two can be reconciled.

The rejection of a collective bargaining agreement is permitted because it is necessary to facilitate the bankruptcy proceeding. Facilitating the proceeding allows the debtor to either liquidate or reorganize, thereby putting the debtor in a much better position than it was before bankruptcy. This allows the debtor to potentially restructure its business and continue to operate, thereby keeping at least some of its employees. Thus, a business that successfully navigates through bankruptcy can eventually become a profitable business.

Conversely, if a debtor was unable to reject collective bargaining agreements in a bankruptcy case, such inability can potentially prevent a debtor from confirming a plan. Preventing a debtor from confirming a plan can lead to many negative effects, such as the debtor

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[27] *Id.* 333.
[28] *Id.*
[29] *Id.*
[30] *The Bankruptcy Law's Effect on Collective Bargaining Agreements,* 81 COLUM. L. REV. 391, at 393.

going out of business. The employer going out of business in turn harms the union members as they would become unemployed and would not be able to receive any form of compensation from the debtor as the debtor would no longer be a business entity and would also have no money to give. The ultimate result of not confirming a plan fails to serve one of the purposes behind labor law: providing just compensation for an employee's work.

III. Interpretations and Implications

A. *Application in Alabama and Kentucky*

The Kentucky court in *In re Horizon Nat. Res. Co.* addressed the same Coal Act issue as the one in *In re Alpha*.[31] The creditors in *In re Horizon* argued that "retiree benefits" includes only benefits received pursuant to contract.[32] The Kentucky court did not adopt this reasoning as section 1114 does not make a distinction between contractual and non-contractual benefits.[33] The Kentucky court went on to say that "§ 1114 clearly contemplates the modification of non-contractual obligations, because it authorizes the appointment of a committee of retirees 'to serve as the authorized representative . . . of those persons receiving any retiree benefits not covered by a collective bargaining agreement.'"[34] This language on its face includes benefits to retirees received outside of collective bargaining agreements. Thus, the Kentucky court held that Coal Act obligations are within the meaning of "retiree benefits."[35]

In a more recent decision in Alabama, obligations under the Coal Act were also defined as "retiree benefits."[36] The Bankruptcy Court for the Northern District of Alabama adopted the reasoning in *In re Horizon* and also cited the court's reconciliation of the Coal Act with the

[31] *See generally In re Horizon Nat. Res. Co.*, 316 B.R. 268.
[32] *Id.* at 275.
[33] *Id.*
[34] *Id.*
[35] *Id.*
[36] *In re Walter Energy, Inc.*, 542 B.R. 859, 884 (U.S. Bankr., N.D. Ala., 2015).

Bankruptcy Code.[37] The court noted that the Coal Act and section 1114 do not contradict each other and that section 1114 only governs the modification of retiree benefits in chapter 11 cases and only to the extent necessary to facilitate reorganization.[38] Furthermore, the Coal Act "covers a more generalized spectrum in that it does not specify whether the former employer is or is not a debtor in possession."[39] With this understanding, Coal Act obligations would not be modifiable in situations outside of Chapter 11 or when the debtor cannot satisfy the requirements of § 1114.[40]

B. *Implications*

The implications of allowing Coal Act obligations to fall under the umbrella of "retiree benefits" within section 1114 permits debtors to avoid being bound by statutory obligations. In *In re Alpha* this avoidance was necessary to facilitate reorganization because Alpha's stalking horse bidder refused to close the deal if Alpha was unable to modify its obligations under the Coal Act. Similarly, the debtors in *In re Horizon* and *In re Walter* needed modification in order to facilitate reorganization. The interpretation that all three jurisdictions have adopted allow for debtors to hurdle a potential obstacle when confirming a plan in bankruptcy.

Conversely, those jurisdictions that choose to exclude Coal Act obligations from "retiree benefits" place a large obstacle in front of debtors who have Coal Act obligations. This obstacle can prevent plans from being confirmed and potentially cause problems for debtors in bankruptcy. As a result, bankruptcy would become a less effective process for debtors that have Coal Act obligations.

Conclusion

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[37] *Id.* at 882.
[38] *Id.*
[39] *Id.*
[40] *Id.*

The holding in *In re Alpha* appears to be the most practical and the Alabama and Kentucky courts seem to agree. The Kentucky court found that the statutory language in section 1114 clearly includes benefits not covered by a collective bargaining agreement. Those benefits would have to include benefits received under the Coal Act. The Alabama court noted how the Coal Act and section 1114 are not contradictory and modification is only allowed in chapter 11 cases to facilitate reorganization. The statutory language also allows for Coal Act obligations to fall under the meaning of "retiree benefits." Under this statutory interpretation, debtors with Coal Act obligations have a greater chance of confirming a plan and facilitating their reorganization.