SOME LESSONS FOR CONGRESS TO PONDER

ABOUT THE LABOR-BANKRUPTCY INTERSECTION

By Daniel Keating

INTRODUCTION

My name is Dan Keating and I am a faculty member at the Washington University School of Law in St. Louis. It has been 25 years since I last practiced bankruptcy here in Chicago, but in the intervening years I have taught bankruptcy and written about it, with a particular focus on the labor-bankruptcy intersection. Unlike many of the witnesses who testified at the labor-bankruptcy hearing before the commission in March, I can't offer to the commission the benefit of having participated personally in a recent bankruptcy case involving labor issues. Therefore, my testimony will be less specific to any particular case and instead will offer a view from 30,000 feet of someone who has thought about and followed this area closely for the last couple of decades.

I should add that I do have close personal connections to those currently being affected by this issue. Both of my parents are retired members of the Chicago Teachers Union who are waiting and wondering what will happen to their defined-benefit pensions and retiree medical benefits. The state of Illinois is likely to reduce their benefits without the state even having to file for bankruptcy, which I guess helps to reinforce my bigger-picture point below that these pension and retiree benefit problems are not bankruptcy-specific problems. Having parents in their late 70's facing this uncertainty also helps me to appreciate the pain, the fear and the anger felt by retirees who kept their promises but are now facing the prospect of their former employer reneging on their end of things.

At some level, having Congress use the bankruptcy process as a means for fixing labor-related problems is like rearranging the deck chairs on the Titanic. Amending the Bankruptcy Code might at best treat some of the symptoms of organized labor's increasing challenges, but history has shown that it rarely cures the underlying disease. Furthermore, when bankruptcy reform ends up as the prescription of choice for labor law's ills, such a cure can often bring with it some unintended side effects to the bankruptcy process itself, potentially compromising its effectiveness as a value-maximizing procedural device for all affected stakeholders.

There is of course no denying that employers have used and continue to use bankruptcy as a way to avoid labor obligations, whether they be pensions, retiree medical benefits, or collective bargaining agreements. For understandable reasons, however, organized labor may fail to appreciate that a debtor's use of bankruptcy for this purpose is nothing personal against labor. Debtors use the bankruptcy process to avoid all kinds of obligations, especially when those obligations are both large and lacking in any nonbankruptcy leverage against the debtor. Bankruptcy has been used to mitigate the effects of mass tort liabilities, large breach of contract judgments, burdensome executory contracts, and even unsecured bank loans. In short, bankruptcy can be a kind of "equal-opportunity destroyer."

Organized labor, then, is not alone in believing that its interests have not been adequately accounted for in the delicate balance that the Bankruptcy Code tries to achieve between promoting reorganizations and requiring debtors to honor commitments made to various pre-petition claimants. What makes organized labor perhaps unique among the various groups of creditors affected by the bankruptcy process is how frequently its members have been the victims of the Bankruptcy Code's legal sanctioning of a debtor-employer's failure to honor its pre-petition commitments. The other reason why workers and retirees arguably feel bankruptcy's pain even more acutely than other disappointed claimants is that so often the claim they have against their bankrupt employer is their sole source of income or medical benefits.

This nation's recent economic meltdown once again brought labor legacy costs to the forefront with high-profile labor-bankruptcy cases such as Chrysler, GM, Patriot Coal and Hostess Brands. Accordingly, it seems fitting to reflect on the lessons that might be gleaned from what has already transpired in the labor/bankruptcy arena since the last major round of legislative activity on this subject. They say that those who fail to study history are doomed to repeat it. In that spirit, I offer the following lessons for Congress to keep in mind as it considers what to do – or not do – with regard to bankruptcy law's treatment of labor-related obligations.

Lesson No. 1: ***You cannot effectively fix a nonbankruptcy problem with a bankruptcy-specific solution.***

Exhibit No. 1 for this lesson is the enactment of section 1114 as a way to deal with the problem of unfunded retiree medical benefits. The true underlying problem with retiree medical benefits is that they represent promises of future benefits with no cash put aside by the employer to back them. That is not a bankruptcy problem; instead, it is what economists would call a classic "deferred maintenance" problem.[1] Certainly unfunded retiree medical benefits are a type of financial deferred-maintenance problem that will manifest itself when a company like LTV, which had a lopsided ratio of retirees to current workers, files Chapter 11 bankruptcy. At best,

[1]*See What is Deferred Maintenance?* at wisegeek.com ("Deferred maintenance is maintenance that should be performed, but is not, for reasons ranging from budgetary constraints to staffing limitations. The concern with deferred maintenance is that while it may not have long term consequences in some cases because it will be attended to eventually, it can increase the risk of creating a safety hazard, a breakdown or another problem which could cause a spike in costs.")

the section 1114 response by Congress was a better-than-nothing band-aid that helped some retirees in some circumstances to reap a higher return on their promised medical benefits than they otherwise might have.

Yet anyone who thinks that section 1114 "solved" the problem of unfunded retiree medical benefits is clearly kidding themselves. The only real solution to the retiree medical benefit debacle is the one that needed to take place decades ago: a serious pre-funding requirement, the failure of which would give rise to a super-priority for the covered retirees that would be effective against other creditors of the company both inside and outside of bankruptcy.

A good model of this type of legislation is the Fair Labor Standards Act's "hot goods" provisions.[2] Under that statute, an employer that fails to comply with federal minimum wage and overtime provisions can be enjoined from selling its goods in commerce until those provisions are met and the unpaid wages are paid. Thus, these provisions create the equivalent of a "super-priority" for outstanding minimum-wage and overtime claims that is effective both inside and outside of bankruptcy. The Supreme Court has made clear that even a secured creditor can be enjoined from selling goods that were produced by a debtor that violated the minimum wage and overtime provisions of the Fair Labor Standards Act.[3]

Ironically, the biggest determinant of what form of protection that a labor-law claimant ends up getting from Congress may be the happenstance of which high-profile company failure triggers the labor-law crisis. To put this point a different way, Congress tends to react very specifically to the particular case that highlights a given labor problem that it seeks to solve,

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[2]29 U.S.C. §§ 206(a)(1), 207(a)(1) & 215(a)(1).

[3]*See* Citicorp Industrial Credit, Inc. v. Brock, 483 U.S. 27, 39 (1987).

rather than stepping back and trying to see the broader scope of the underlying problem. So, for example, when the Studebaker company shut down its operations in the early 1960's and reneged on its defined-benefit pension promises without ever filing for bankruptcy,[4] Congress responded with a solution to the problem of underfunded pension plans that was not bankruptcy-specific: the enactment of ERISA.[5]

Ultimately, Congress chose not to include retiree medical benefits within the scope of ERISA’s vesting and pre-funding requirements, thus setting the stage for the next crisis for labor-related claims when LTV filed Chapter 11 in 1986. I often wonder what Congress would have done if LTV had simply announced that it was going out of business without even filing for bankruptcy, just liked Studebaker did. In such a nonbankruptcy business-failure scenario, the retirees would just as surely not have received their promised medical benefits, given the lack of pre-funding and the lack of any ongoing company to fund them in the future. Would that setting have prompted Congress to enact a broader protection for retiree medical benefits, perhaps bringing those benefits under the ERISA requirements of vesting and pre-funding?

The reason why I have my doubts whether even a Studebaker-like crisis would have

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[4]*See* Shelley Smith Curtis, *Potential for Crisis: Pension Benefit Insurance and the PBGC*, 39 Fed. Ins. & Corp. Couns. Q. 131, 131 (1989).

[5]*See* Rettig v. Pension Benefit Guar. Corp., 744 F.2d 133, 137 (D.C. Cir. 1984) (“Throughout the deliberations that culminated in the enactment of ERISA, Congress was inundated with tragic stories of pension plan failures in which thousands of employees saw the destruction of the small measure of retirement security they had built up through decades of forced savings and deferred compensation.”) ERISA created both a mandatory pre-funding and vesting requirement for defined-benefit pension plans. 29 U.S.C. §§ 1051, 1081. ERISA also created a new federal insurance corporation, the PBGC, to serve as a safety net for workers when companies failed to comply with their pre-funding obligations, or when employers’ plans were terminated before they had a chance to fund them. 29 U.S.C. § 1302.

caused Congress to expand ERISA to include retiree medical benefits is that such a solution, unlike the enactment of Bankruptcy Code section 1114, would have required additional federal funding. First, there would be the costs of additional staffing for the PBGC, the federal insurer of defined-benefit pensions that ERISA created. Second, besides new staffing costs, there would have been the additional insurance risk for unfunded retiree medical benefits that the PBGC would have needed to cover as part of its already hefty portfolio of underfunded pension plans, a risk that would ultimately be borne by the federal government itself if the PBGC were to become insolvent.

The beauty of the section 1114 solution to the retiree medical benefits crisis was that it was perceived to be costless – or, at least, costless to the federal government. If retirees in bankruptcy were going to be given an elevated priority that they heretofore did not enjoy, that new priority was clearly going to cost some other claimant in the zero-sum game that is bankruptcy. Conveniently enough for Congress, however, the particular parties who would bear the cost of this new bankruptcy-specific priority were yet to be determined.

Lesson No. 2: ***When you create large springing priorities that apply only in a particular kind of reorganization process, employers that are faced with those types of claims will seek to avoid that process.***

The GM and Chrysler cases were not the first examples of debtors-in-possession that bypassed a traditional Chapter 11 plan process in favor of a section 363 sale as a way to circumvent the effects that a large bankruptcy-specific priority of retiree medical benefits would otherwise have had on their ability to reorganize. The Horizon Natural Resources Company was an Illinois-based coal company that filed Chapter 11 and tried to sell its assets as a going-concern business that would continue to honor its collective bargaining agreements and its retiree medical benefit obligations.[6] Unfortunately, these labor obligations were so large relative to the value of the company that no buyer was willing to buy the company if such obligations were part of the deal.[7]

As a result, the debtor-in-possession in *Horizon* sought and received permission from the bankruptcy court to effect a section 363 sale free and clear of all claims, including the claims of the retirees to their promised medical benefits. The retirees' section 1114 rights to their benefits would have to be asserted against the proceeds of the section 363 sale, but those proceeds were largely encumbered by the claims of secured creditors.[8] The only silver lining in this sad tale was that the section 363 sale allowed some of the current workers to retain their jobs, albeit at a reduced wage rate. Even that small silver lining would probably not have been possible with a piecemeal liquidation of the company's assets, which would have yielded much less than the 363 sale of the assets as a going-concern.[9]

In support of its decision to allow the section 363 sale free and clear of retiree claims for

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[6]*See In re* Horizon Natural Resources Co., 316 B.R. 268 (Bankr. E.D. Ky. 2004).

[7]*Id*. at 274.

[8]*Id*. (noting that without the section 363 "free and clear" sale, the assets would not even generate enough proceeds to pay off post-petition lenders and administrative priority claims); *see also* James Dao, *Miners' Benefits Vanish With Bankruptcy Ruling*, N.Y. Times, October 24, 2004, at N20 (noting that the section 363 sale in this case caused nearly 3,800 coal workers, retirees and their dependents to lose health insurance).

[9]The wide divergence between the going-concern value and the piecemeal-liquidation value of a company is fairly typical. In *Chrysler*, for example, the court contrasted the $2 billion purchase price for the proposed asset sale under section 363 with the $800 million high-end estimate of a liquidation of Chrysler. *Chrysler LLC*, 405 B.R. 84, 96-97 (Bankr. S.D.N.Y. 2009).

medical benefits, the bankruptcy court in *Horizon* cited a similar case, *In re Leckie Smokeless Coal Co*.[10] In *Leckie*, the major legacy cost for the debtor was not section 1114 retiree benefit obligations, but rather Coal Act obligations totaling about $7 million. The problem was that the company's assets were only worth about $2 million free and clear of all claims.[11] The court in *Leckie* ultimately allowed the section 363 sale free of the Coal Act obligations on the theory that absent such a sale, the debtor would simply have to conduct a piecemeal liquidation of assets that would yield fewer dollars than could be realized if the assets were sold as a unit without those obligations.[12]

Lesson No. 3: ***If you make a particular type of employee benefit more expensive for an employer, then fewer employers will give the benefit.***

This is a lesson that has implications for both bankruptcy and nonbankruptcy legislation alike. On the bankruptcy side of things, one way for Congress to make a benefit more expensive for an employer is to engraft a bankruptcy-specific priority onto the benefit, thus adding another hurdle to an employer's ability to reorganize in bankruptcy.

With both defined-benefit pension plans and retiree medical benefits, we have seen a steady decline during the past few decades in the number of employers that offer those particular

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[10]*Horizon*, 316 B.R. at 279 (citing In re Leckie Smokeless Coal Co., 99 F.3d 573, (4th Cir. 1996)).

[11]*Leckie*, 99 F.3d at 586 ("[T]he Bankruptcy Court found that $1.9 million represented a fair and reasonable price for the debtors' assets; the debtors' accrued Coal Act obligations, though, stand at about $7 million.").

[12]*Id*. at 586-87 ("If a free and clear order could not be issued, the assets would almost inevitably have to be sold piecemeal, thereby generating fewer funds with which to satisfy the claims of the Fund, the Plan, and the debtors' other creditors.")

benefits. From 1980 to 2008, the proportion of private-sector employees that were participating in a defined-benefit pension plan fell from 38 percent to 20 percent.[13] Between 1997 and 2010, the percentage of private-sector employers offering retiree health benefits to early retirees dropped from 28.9 percent to 17.7 percent.[14]

It was easy enough for employers to offer generous defined-benefit pension plans and retiree health benefits back in the days when pension plans did not have to be pre-funded and when retiree medical benefits obligations did not even need to be shown on an employer's balance sheet. In those days, the ability to make these type of promises to employees in lieu of higher current wages was like an unlimited unsecured line of credit for employers, if not a de facto Ponzi scheme on the backs of the workers to whom the future benefits were promised.

The challenge for ERISA, even from the very inception of that statute, has been to ensure that employers will ultimately pre-fund their defined-benefit pension promises without making the employers either eliminate such benefits altogether or go bankrupt in the process of pre-funding these legacy costs. The fundamental problem for ERISA in this regard is that by the time ERISA was enacted, most companies that offered defined-benefit pension plans had already made significant defined-benefit promises. Realistically, these future promises could not be funded immediately, and thus employers were allowed by ERISA to pay these already accrued

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[13] Barbara A. Butrica et al., *The Disappearing Defined Benefit Pension and Its Potential Impact on the Retirement Incomes of Baby Boomers*, 69 Social Security Bulletin No. 3 (2009).

[14] Paul Fronstin and Nevin Adams, *Employment-Based Retiree Health Benefits: Trends in Access and Coverage, 1997-2010*, Issue Brief No. 377 at ebri.org, the Employee Benefit Research Institute (October 2012).

pension liabilities over a period of many years.[15]

Even the more recent ERISA overhaul legislation, the Pension Protection Act of 2006[16] (PPA), faced this same fundamental tension: The firms that posed the greatest financial risk to the PBGC due to the firms' underfunded pension liabilities were often the very same firms that could least afford to remedy the problem quickly. In light of this reality, it was perhaps not as ironic as it might otherwise have seemed that the PPA, which was specifically designed to strengthen the balance sheet of the PBGC, would include special exemptions for the very industry (airlines) that was probably the worst underfunded-pension offender.[17]

The defining moment for the fate of retiree medical benefits came not through federal legislation, which even today does not require pre-funding of such benefits, but instead through a change in the Financial Accounting Standards. When FASB Statement No. 106 was issued in 1990 and became effective in 1993, private firms could no longer hide the cost of their future retiree medical benefit liabilities from their balance sheets.[18] This FASB-generated requirement on a firm to show the cost of its future retiree medical benefit liability for all the world to see, including shareholders and lenders, certainly served to accelerate what had already been a marked trend among private employers towards the phasing out of such benefits.

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[15]I.R.C. § 412(b)(2)(B) (requiring amortization periods of between five and 30 years for employers to fund already-accrued defined-benefit pension obligations).

[16]Pub. L. No. 109-280, 120 Stat. 780 (2006).

[17]*See* Pension Protection Act of 2006 § 402 (describing special rules for airlines that allow additional time for airlines to amortize past underfunding of plans).

[18]*See* Summary of Statement No. 106, Employers' Accounting for Postretirement Benefits Other Than Pensions, at fasb.org.

Lesson No. 4: ***A piecemeal liquidation can eviscerate even the most powerful priority.***

As I have followed the tragic stories for the past two decades of the many promises that were broken by employers to their union workers and retirees, I've often wondered if there would have been any way to give a truly ironclad guarantee to workers concerning their collective bargaining agreements and to retirees concerning their promised medical benefits. As a thought experiment along those lines, I've considered what might be the consequence of federal legislation that simply prohibited the rejection of collective bargaining agreements under any circumstances or that prohibited the modification of retiree benefits under any circumstances.

In this hypothetical world, unions and retirees could of course voluntarily agree to modifications to the original terms that they were promised by their employer. This would happen, though, only in cases where the affected workers or retirees were convinced that the changes being proposed were truly necessary based on real financial exigencies of their employer. In effect, this "no modifications" rule would shift the decision-maker on the "necessary" question from the bankruptcy judge to the unions and retirees themselves. This would clearly represent a reallocation of bargaining power from the employer to its employees and retirees as compared to our current system. The more intriguing question is whether such a change would necessarily represent a reallocation of actual wealth.

That second question is one that I cannot answer with any confidence. The reason for my uncertainty is that even in a "no modifications" regime, the employer would always hold the final leverage of a piecemeal liquidation. If the company goes out of business, then even "ironclad guarantees" end up not being worth much.[19] As noted above, the bargaining dynamics would change. Even with these changed bargaining dynamics, however, would we end up with the same number of negotiated resolutions as we see now, except with a more favorable result for employees and retirees than we currently see? Or would we simply see more liquidations as the result of brinksmanship, as unions attempt to use their newfound leverage to compel employers to honor in full the promises that employers are currently allowed to modify with court approval?

The answer to these unknown questions would largely come down to the level of trust between the two parties at the negotiating table. If the trust level is like what we saw in last year's round of negotiations between Hostess Brands, Inc., and its unions, then the prognosis for such a brave new world would not be optimistic. In Hostess, the debtor-in-possession made what it said was its "final offer" to its unions to preserve a reorganization possibility, but the union either did not believe the debtor or simply decided that it would rather have no deal than to continue working under the much-reduced terms that were offered. In the end, Hostess converted its case from a reorganization to a liquidation, and those union workers were forced to look for

[19] As the Sixth Circuit observed in approving the pre-bankruptcy VEBA trust that GM negotiated with the UAW for the company's retirees, "If we decided for the sake of argument that the retirees were likely to win the debate [on vesting], any such victory would run the risk of being a Pyrrhic one because the cost of insisting on irreversible healthcare benefits might well be – and indeed almost certainly would be – the continuing downward spiral of the companies' financial position." UAW v. GM Corp., 497 F.3d 615, 632 (6th Cir. 2007). Along the same lines, one UAW negotiating-committee member admitted that a VEBA was not the union's ideal outcome for retirees, "but we really didn't have much of a choice. If we didn't get our jobs, we lose everything and it wouldn't matter. We took what they gave us." K.O. Jackson, *Retirees Consider Effects of Chapter 11: Medicare Benefits Top List of Labor Concessions*, Kokomo Trib., May 1, 2009, 2009 WLNR 8280497.

other work.[20]

Short of the federal government putting new money on the table, the tragedy of the workers' and retirees' plight in these labor-bankruptcy scenarios is that the promises that were once made to them are only as good as the financial health of the employer that made the promises. Once upon time, the federal government did put new money on the table in order to insure the defined-benefit pension promises that it was now undertaking to regulate. So how likely is it that Congress would agree today to expand the scope of the government's insurance umbrella to include additional labor-related obligations? To paraphrase Sarah Palin, and with the benefit of hindsight, the answer to that question may best be found in the question itself: "So how's that pension-insurance thing workin' out for ya?"

The sad reality of bankruptcy, or even of companies failing outside of bankruptcy, is that we are always dealing at that point with an array of least-worst outcomes. When Delta airlines sought to terminate its defined-benefit pension plans, the retirees who would be affected by such a termination were understandably angry, and they expressed their frustration in a meeting with then-Chief Executive Gerald Grinstein. Grinstein told the retirees in response, "It's a choice between what we propose and no company at all. We have no ability to borrow additional money. What we have is what we have."[21]

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[20]*See A Strike Ended Operations as Hostess; New Buyer Won't Have Unions*, abcnews.go.com, April 26, 2013 (noting that the new buyer of the bankrupt assets of Hostess Brands, Inc., plans to hire at least 1,500 workers for the reopened plants, but the workers will not be unionized).

[21]Russell Grantham, *Delta's Grinstein Faces Retiree Groups*, Atlanta Journal and Constitution at A1, October 29, 2005. Yet another succinct and powerful statement concerning the least-worst nature of choices in bankruptcy was made by the bankruptcy judge in the United Airlines case when he allowed the airline to dump a defined-benefit pension plan onto the PBGC

Lesson No. 5: ***A lender's willingness to lend, both inside and outside of bankruptcy, can be affected by the creation of new priorities.***

I have a second thought experiment concerning the protection of labor obligations that are owed by a failing company. Suppose that in addition to a rule that prohibited any forced modification of benefits or any rejection of collective bargaining agreements, the federal government added a "hot goods" protection to such claims similar to what the Fair Labor Standards Act currently provides for minimum-wage claims and overtime wage claims. In other words, this thought experiment would create a super-priority for all labor-related claims, effective both inside and outside of bankruptcy, that would trump even the claims of secured creditors. What would be the consequences of such a change?

One positive consequence for organized labor is that labor claims would move to the front of the line, even in a case where an employer was forced into a piecemeal liquidation. That's the "good news" part. The bad news, however, is that the creation of such a large super-priority claim would cause lenders to shy away from lending in the first place to any firms that were likely to have large claims of this type. Because lenders can choose to whom they wish to lend, they will generally choose borrowers that have either sufficient collateral or reliable cash flow to make the lender comfortable about its prospects for eventual repayment of its loan.

Even the federal government itself, when it assumed the role of debtor-in-possession lender in the GM and Chrysler cases, did everything it could to bolster its priority position in

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that was underfunded by $6.6 billion: "Bankruptcy generally involves choosing the least bad of a number of unfortunate choices. The least bad choice keeps the airline functioning, keeps people employed, and is an alternative to the worst choice, which is a shutdown of the company." Mary Wisniewski, *Judge Allows United to Drop Pension Plan; Calls It "Least Bad of a Number of Unfortunate Choices,"* Chi. Sun-Times, May 11, 2005 at 77.

advance of lending, even if meant subordinating existing and sympathetic priority claimants. Most notably, in both of these cases the U.S. Treasury insisted that the originally agreed-to VEBA arrangements the two automakers had structured with their retirees to cover future medical benefits had to be significantly restructured in a way that took money away from the retirees.[22] The irony, of course, was that the main reason these retirees were getting the VEBA trusts in the first place was that a *different* branch of the federal government – Congress – had given the retirees a special bankruptcy priority to these benefit claims some two decades earlier.

With its own money now on the line, however, the federal government was willing to reduce – indeed, insisted on reducing – the effectiveness in these cases of the priority that Congress had itself created. From the retirees' vantage point, it probably felt like they were being told, "We're from the government, and we're here to hurt you." Of course, in reality it was nothing personal against the retirees.[23] That's just how lenders are, even if they are sometimes from the government.

CONCLUSION

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[22]In the GM case, the U.S. Treasury insisted that GM pay at least half of the $20 billion that GM was obligated to pay to the retiree-benefit VEBA under the pre-bankruptcy settlement in common stock, rather than in cash, as was originally promised to the retirees. *GM Corp*., 407 B.R. 463, 478 (Bankr. S.D.N.Y. 2009). In Chrysler, the U.S. government told Chrysler before it filed Chapter 11 that in order for Chrysler to get a $6 billion pre-bankruptcy bailout loan, at least 50% of the funding for the retiree-benefit VEBA had to come from New Chrysler's equity, which again represented a reduction in funding from what retirees had originally negotiated. *Chrysler LLC*, 405 B.R. at 92 (Bankr. S.D.N.Y. 2009).

[23]Indeed, if the government had not come to the rescue with its bailout loans, it is far from clear that the automakers had any other viable route to avoid liquidation, which obviously would not have been in the interests of the retirees.

As a new bankruptcy-labor bill gets introduced in Congress to address the latest round of high-profile bankruptcies that have occasioned millions of dollars in lost retiree benefits and in broken collective bargaining agreements, it is hard not to feel a sense of deja vu. This is where we were 25 years ago, and sections 1113 and 1114 were supposed to be the answers to these types of tragedies. Given that these twin Code sections have not worked as effectively as organized labor had originally hoped, it is only natural that those representing worker and retiree interests might look to Congress again for a new generation of legislative solutions to the vexing intersection of labor and bankruptcy law.

Perhaps the last round of bankruptcy reforms did not go far enough in creating a level playing field for labor in its ongoing struggles with management. That is an understandable story for organized labor to tell its members, especially in light of several recent big-stakes bankruptcy cases where union workers or retirees have ended up seeing labor promises being broken by a bankrupt employer yet again. For my part, I don't pretend to know enough about this difficult and complex area to say with confidence that labor's interpretation of events, and its proposed remedy for this latest round of bankruptcy setbacks for its members, is necessarily wrong.

What I do wish to accomplish in this testimony is to offer an alternative story, and one that Congress ought to at least consider as it perhaps gears up for another round of labor-bankruptcy fixes. I proposed five lessons for Congress to keep in mind about the labor-bankruptcy intersection, but I think that the heart of my observations from following this area for a couple of decades can actually be summed up in two "meta-lessons."

First, just because a crisis manifests itself in the bankruptcy forum does not necessarily mean that the crisis is a bankruptcy problem that can be solved with a bankruptcy solution. This first meta-lesson would suggest that if Congress wants to fix a perceived labor-bankruptcy problem, it ought to at least consider giving its favored claimants a form of leverage that will not be limited to the bankruptcy forum. That way, such a fix will not create a perverse incentive for companies to avoid using bankruptcy as a way to reorganize a struggling enterprise.

Second, any new action that Congress triggers in a largely zero-sum game such as bankruptcy will have an equal and opposite reaction. When you give more relative wealth to one party in a setting like bankruptcy, then you take away wealth from another. At some point, if that other party has a choice, it will opt for another process or find another route to achieve the same ends that bankruptcy might have. This second meta-lesson, I believe, helps to explain the rise of section 363 sales over traditional plans of reorganization. Outside of bankruptcy, it also helps to explain the movement of employers away from offering defined-benefit pension plans and open-ended retiree medical benefits.

My fear is that if Congress ignores these meta-lessons, any new "reform" in this area will simply be a variation of what failed to do the job the last time. Even more troubling is the prospect that an additional layer of bankruptcy-specific priorities will further erode the overall effectiveness of the bankruptcy forum as an efficient vehicle for preserving the going-concern value of struggling businesses. If that is the end result of the next labor-bankruptcy reform effort – not really helping labor that much, but in fact hurting the bankruptcy process – then that could prove to be an even worse outcome than my opening metaphor of rearranging deck chairs on an already-sinking ship.