

Summer 1984

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Recommended Citation

Haggard, Thomas R. (1984) "The Appointment of Union Representatives to Creditors' Committees under Chapter 11 of the Bankruptcy Code," *South Carolina Law Review*. Vol. 35 : Iss. 4 , Article 3.

Available at: <https://scholarcommons.sc.edu/sclr/vol35/iss4/3>

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THE APPOINTMENT OF UNION REPRESENTATIVES TO CREDITORS' COMMITTEES UNDER CHAPTER 11 OF THE BANKRUPTCY CODE®

THOMAS R. HAGGARD*

When a company files for reorganization under Chapter 11 of the Bankruptcy Code,¹ the financial interests of its business creditors are suddenly and dramatically affected. When, how, and whether the debts owed creditors will be paid are no longer determined by the free play of market forces and the law of contracts, but rather by a "reorganization plan" that is subject to the approval of the bankruptcy court.

The interests of the debtor's employees and of any union representing them are also significantly affected by a Chapter 11 proceeding, albeit in a slightly different way. Although employees have interests like any other creditor with respect to back wages, accrued fringe benefits, and the like, they have an even more compelling interest in the Chapter 11 proceeding's effect upon their present and future relationship with the debtor-employer. While the Bankruptcy Code provides some degree of priority to wage and pension claims,² individual employees are essentially left to the mercy of the process. On the other hand, unions representing organized employees have made more vigorous attempts to vindicate employee and union interests in Chap-

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This article will appear as a chapter in a book on the relationship between bankruptcy and labor law, to be published by the Industrial Research Unit, Wharton School, University of Pennsylvania, in 1985.

1. 11 U.S.C. §§ 101-151326 (1984).

2. 11 U.S.C. § 507(a)(3), (4)(1984).

ter 11 reorganizations. Such interests, moreover, almost always derive, directly or indirectly, from a collective bargaining agreement between the union and the debtor-employer.

Initially, the unions argued that collective bargaining agreements, unlike other executory contracts, should be subject to rejection, *if at all*, only if continued observance would necessarily cause the reorganization to fail and thus force the debtor-employer into liquidation.³ The unions also argued that, until the bankruptcy court actually approves the rejection of the agreement, a debtor-employer should be required to keep the collective bargaining agreement in full force and effect, as purportedly mandated under the provisions of the Labor Management Relations (Taft-Hartley) Act (LMRA).⁴

The Supreme Court rejected both of these arguments in *NLRB v. Bildisco & Bildisco*.⁵ By concluding that the "liquidation" standard advocated by the unions was inappropriate, the Court went further than the "business judgment" test used to evaluate the "rejectability" of other commercial contracts in a Chapter 11 proceeding. With respect to collective bargaining agreements, the Court adopted an intermediate approach: the bankruptcy court must first determine if the agreement "burdens the estate";⁶ if it does, then the Court must balance all of the equities involved to determine whether they favor rejection over acceptance.⁷ The Court also held that between the filing of a petition and the ultimate approval of a reorganization plan, a collective bargaining agreement ceases to be an "enforceable contract" under the LMRA, a holding which justifies the debtor-employer's suspension of performance.⁸

Having lost on these two arguments, the unions immediately turned to Congress. In a last-minute compromise, Congress

3. This strict standard was adopted by the Second Circuit in *Brotherhood of Railway, Airline and Steamship Clerks v. REA Express, Inc.*, 523 F.2d 164 (2d Cir.), *cert. denied*, 423 U.S. 1017 (1975), *cert. denied*, 423 U.S. 1073 (1976).

4. The National Labor Relations Board had agreed with this argument by holding that a debtor-employer violates §§ 8(a)(5) and 8(d) of the Labor Management Relations (Taft-Hartley) Act, 29 U.S.C. § 158(a)(5), (d)(1982), when it unilaterally repudiates a collective bargaining agreement. *Bildisco & Bildisco*, 255 N.L.R.B. 1203 (1981), *enforcement denied*, 682 F.2d 72 (3d Cir. 1982), *aff'd*, 104 S. Ct. 1188 (1984).

5. 104 S. Ct. 1188 (1984).

6. *Id.* at 1196.

7. *Id.*

8. *Id.* at 1199.

modified the *Bildisco* approach slightly.⁹ Under the newly enacted provisions, a debtor-in-possession can alter or reject a collective bargaining agreement only after a hearing on the issue in bankruptcy court.¹⁰ Prior to the hearing, the employer must offer the union a proposal outlining the modifications in employee benefits and protections that the employer believes "are necessary to permit the reorganization of the debtor and assures [sic] that all creditors, the debtor and all of the affected parties are treated fairly and equitably."¹¹ The debtor-in-possession must also provide the union "with such relevant information as is necessary to evaluate the proposal,"¹² and then "meet, at reasonable times, with the authorized representative to confer in good faith in attempting to reach mutually satisfactory modifications of such agreement."¹³ The bankruptcy court can then approve a

9. 11 U.S.C. § 1113 (1984).

10. 11 U.S.C. § 1113(f)(1984). This changes, with respect to collective bargaining agreements only, the general rule of bankruptcy law that a debtor-in-possession can suspend performance of an executory contract pending court approval of the rejection of that contract. That rule was the predicate of the Supreme Court's decision in *Bildisco* that such suspension was therefore not an unfair labor practice in violation of LMRA § 8(d), 29 U.S.C. § 158(d)(1982). It is unclear whether the effect of the amendment will now be to reactivate the unfair labor practice provisions of the LMRA. While this new provision does not expressly reject the judicial gloss *Bildisco* placed on LMRA § 8(d), the better reading of the two statutes would be to accept that gloss, thus making the Bankruptcy Code the exclusive source of law on the unilateral rejection issue. This reading is also consistent with 11 U.S.C. § 1113(e), which authorizes the bankruptcy court, prior to its final approval of the rejection, to order interim changes, if they are "essential to the continuation of the debtor's business," or necessary "in order to avoid irreparable damage to the estate," a process which would be severely impeded if the labor statute were also applicable.

11. 11 U.S.C. § 1113(b)(1)(A)(1984). This language was a compromise between the proposal of Senator Packwood, which required the debtor-employer to propose "the minimum modifications . . . that would permit the reorganization," DAILY LABOR REPORT (BNA) No. 103 at C-4 (May 29, 1984), and the proposal of Senator Thurmond, which on this point essentially codified the *Bildisco* test by merely requiring the debtor-employer to make "reasonable efforts to negotiate a change in the contractual terms," *id.* at C-3 (emphasis added). The requirement of § 1113(b)(1)(A)(1984) that the debtor-employer's proposals include those things "necessary to permit the reorganization" adds something to the *Bildisco* bargaining requirement. It is difficult to predict, however, how the courts will interpret this extremely ambiguous language.

12. 11 U.S.C. § 1113(b)(1)(B)(1984).

13. 11 U.S.C. § 1113(b)(2)(1984). The Court in *Bildisco* had similarly required that the debtor-employer make "reasonable efforts to negotiate a voluntary modification" before filing a petition for rejection. 104 S. Ct. at 1196. Apparently, the Court regarded efforts to negotiate not only as a condition precedent to a later rejection but also as a part of the debtor-employer's continuing duty under the LMRA to bargain with the union as the employees' representative, a duty which includes a "good faith" element.

contract rejection if it finds that the debtor has complied with these requirements, that the union refused to accept the employer's proposal "without good cause,"¹⁴ and that "the balance of the equities clearly favors rejection"¹⁵ of the collective bargaining agreement. The bankruptcy court has fourteen days within which to hold a hearing on the application for rejection¹⁶ and must rule on the application within thirty days after the commencement of the hearing.¹⁷

It is uncertain how much protection these new Code provisions will actually provide to employee and union interests under what is still an executory collective bargaining agreement.¹⁸ More importantly, it is also unclear how, as a practical matter, these contract rejection procedures will mesh with the normal Chapter 11 reorganization process or how they will affect the negotiations that the debtor conducts with an official committee of its unsecured creditors, a group whose role in the reorganization process is substantial. The matter is complicated further by the fact that unions are increasingly seeking additional protection of their interests by claiming "creditor" status and then petitioning for an appointment to the committee of creditors.¹⁹

The Court, however, seemed to believe that the two statutory schemes should remain separate and distinct. Recognizing that the bankruptcy court lacked labor law expertise, 104 S. Ct. at 1197, 1200, the Court apparently intended that the bankruptcy court merely determine that the debtor made a proposal and that the parties were in fact unable to agree. The new Code provision, however, seems to give the NLRB and the bankruptcy court concurrent jurisdiction over the "good faith" issue. Given the different time frames within which the court and the NLRB operate, this can only create an enormous amount of confusion. The statute is better construed as giving the bankruptcy court exclusive jurisdiction over the bargaining mandated by § 1113(b)(2)(1984), while maintaining NLRB jurisdiction over bargaining for any new collective bargaining agreement.

14. 11 U.S.C. § 1113(c)(2)(1984).

15. 11 U.S.C. § 1113(c)(3)(1984). This essentially codifies the *Bildisco* "balancing approach," 104 S. Ct. at 1196, although the word "clearly" in the statute may evidence a slight toughening of the *Bildisco* formula.

16. 11 U.S.C. § 1113(d)(1)(1984).

17. 11 U.S.C. § 1113(d)(2)(1984).

18. See *supra* notes 10-15. Attorneys for both labor and management concede that the language of the labor provision is so ambiguous that its real effect will depend heavily on how it is construed by the courts. See *House-Senate Conferees Resolve Disputes on Bankruptcy Bill; Approval is Expected*, Wall St. J., June 29, 1984, at 2, col. 3.

19. See generally *A Louder Union Voice in Settling Bankruptcies*, Bus. Wk., Dec. 8, 1980, at 87, 90.

Although such an appointment was affirmed by the Third Circuit in *In re Altair Airlines*,²⁰ the matter is not entirely free of doubt. This Article will explore the parameters of the problem, with particular emphasis on the effect of the new legislation upon the union's role in a Chapter 11 reorganization.

I. CREDITORS' COMMITTEES IN GENERAL

Under Chapter 11, the court must appoint a committee of creditors, "as soon as practicable,"²¹ to represent the interests of the general, unsecured creditors.²² This committee consists of the persons who hold the seven largest claims of this type, provided they are willing to serve in that capacity.²³ It is not necessary that these seven largest claimholders be representative of *all* of the different kinds of general, unsecured creditors, *i.e.* represent institutional and trade creditors in the exact proportion of those types of claims asserted against the debtor,²⁴ but some degree of balance is obviously desirable. Alternatively, members of the unofficial committee organized by the creditors before the order for relief may be appointed to the official committee if they were fairly chosen and are representative of the different kinds of claims against the debtor.²⁵

The functions of a Chapter 11 creditors' committee are broad and varied. Section 1103(c) provides, first, that the committee may "consult with the trustee or debtor in possession concerning the administration of the case."²⁶ Presumably, that ability will now include a right of consultation over the debtor-employer's prerejection proposal to the union. Normally, a

20. 727 F.2d 88 (3d Cir. 1984). The court of appeals cited several other instances in which labor organizations had been appointed to creditors' committees. *Id.* at 89 n.2. However, as the bankruptcy court in *Altair* earlier pointed out, "in those cases, the issue of the [union's] right to serve on the committees does not appear to have been considered by the courts. Certainly, there was no objection raised by the debtors as in the case at bench." *In re Altair Airlines, Inc.*, 25 B.R. 223, 225 (Bankr. E.D. Pa. 1982).

21. 11 U.S.C. § 1102(a)(1)(1984); *see also* 11 U.S.C. § 151102(a)(1984).

22. At the request of a "party in interest," the court may also appoint additional committees of creditors or equity security holders if necessary to assure adequate representation of their interest. 11 U.S.C. § 1102(a)(2)(1984).

23. 11 U.S.C. § 1102(b)(1)(1984).

24. *See DeNatale, The Creditors' Committee Under the Bankruptcy Code — A Primer*, 55 AM. BANKR. L.J. 43, 50 (1981).

25. 11 U.S.C. § 1102(b)(1)(1984).

26. 11 U.S.C. § 1103(c)(1)(1984).

debtor submits orders to the committee prior to submitting them to the court, and thus allows the committee to review the proposed actions and make its own determinations.²⁷ The legitimate purview of the committee would therefore extend to evaluating and commenting upon the debtor-employer's formal application to the bankruptcy court for permission to reject the contract.

The investigatory function of a creditors' committee is also very important in a Chapter 11 proceeding, particularly when the reorganization is large and complex. The Code provides that a committee may "investigate the acts, conduct, assets, liabilities, and financial condition of the debtor, the operation of the debtor's business, and the desirability of the continuance of such business, and any other matter relevant to the case or to the formulation of a plan."²⁸ This would seem to give the committee virtually carte blanche access to the debtor's financial records, a right considerably broader than that of the union under the recent Code's provision for "such relevant information as is necessary to evaluate the [employer's] proposal."²⁹

Finally, the committee is authorized to participate in the formulation of the debtor's reorganization plan and to solicit acceptances or rejections of that plan from various creditors.³⁰ If the debtor should lose its exclusive right to file a plan, the committee, or any other "interested party," may file one.³¹ As a practical matter, the negotiation of a reorganization plan is often the most important and complicated function the committee performs.

It is apparent, therefore, that the creditors' committee plays an important role in a Chapter 11 reorganization proceeding.³² Accordingly, it is not surprising that unions representing a debtor's employees seek to participate in the reorganization process through membership on such a committee.

27. See DeNatale, *supra* note 24, at 52.

28. 11 U.S.C. § 1103(c)(2)(1984).

29. 11 U.S.C. § 1113(b)(1)(B)(1984).

30. 11 U.S.C. § 1103(c)(3)(1984).

31. 11 U.S.C. § 1121(c)(1984).

32. See *In re Johns-Manville*, 26 B.R. 919, 925 (Bankr. S.D.N.Y. 1983).

II. PROBLEMS ASSOCIATED WITH THE APPOINTMENT OF UNION REPRESENTATIVES TO CREDITORS' COMMITTEES

In many respects, labor unions are unique institutions, in large part because of their unique relationship with both the employees they represent and with the employers with which they negotiate collective bargaining agreements. Most labor unions are, in a legal sense, "unincorporated associations";³³ membership in these employee associations is voluntary and is a matter of contract.³⁴ One of the usual terms of the membership contract is that the employee-member appoints the union as his or her agent to negotiate and agree upon the terms and conditions of the employee-member's employment with a particular employer.³⁵

A union's power to represent employees is, however, considerably broader than its ability to bargain on behalf of its actual members. Under federal law, once a union is selected as bargaining representative by a majority of employees in a particular employment unit, that union becomes the exclusive bargaining representative of *all* the employees in that unit, whether or not they are members of the union or individually consent to such representation.³⁶ At that point, the union has not only that *power*, but also the *duty* to provide "fair representation" to each employee for whom it is a statutory agent.³⁷ Unlike other business entities with which an employer might possibly contract, a union has the power under federal law to compel an employer to deal with it. Additionally, federal law dictates the subject matter and method of the bargaining process.³⁸ The result of the heavily

33. At common law unions could neither sue nor be sued in their own name. *See, e.g.,* *Baskins v. UMWA*, 150 Ark. 398, 234 S.W. 464 (1921); *Pickett v. Walsh*, 192 Mass. 572, 78 N.E. 753 (1906). Section 301 of the Labor Management Relations (Taft-Hartley) Act, 29 U.S.C. § 185(b)(1982), changed that as a matter of federal law, and most states have also recognized the "standing" of such associations. *See* A. THIEBLOT & T. HAGGARD, *UNION VIOLENCE — THE RECORD AND THE RESPONSE BY COURTS, LEGISLATURES, AND THE NLRB* (1983) 473 nn. 63 & 64.

34. *NLRB v. Allis-Chalmers Mfg. Co.*, 388 U.S. 175, 192 (1967).

35. For an example of an authorization form used by a union, see J. SWANN, *NLRB ELECTIONS: A GUIDEBOOK FOR EMPLOYERS* (1980) 114-15.

36. 29 U.S.C. § 159(a)(1982); *see generally* R. GORMAN, *LABOR LAW* (1976) 374-81.

37. *Steele v. Louisville & N.R.R.*, 323 U.S. 192 (1944); *see generally* R. GORMAN, *supra* note 36, at 695-728.

38. 29 U.S.C. § 158(a)(5), (d)(1982); *see generally* R. GORMAN, *supra* note 36, at 399-531.

regulated bargaining process, a so-called "collective bargaining agreement," is itself something of an anomaly. Under the common law, there was serious doubt whether a collective bargaining agreement was an enforceable "contract," and if so, of what sort it was.³⁹ Section 301 of the LMRA⁴⁰ ultimately resolved the issue in favor of enforceability. Section 8(d)⁴¹ of the LMRA also makes an employer's mid-term repudiation of a collective bargaining agreement an unfair labor practice.

The Supreme Court in *Bildisco* held that collective bargaining agreements were subject to mid-term rejection under the Bankruptcy Code and that a Chapter 11 debtor-employer's unilateral suspension of performance, pending court approval of that rejection, was not an unfair labor practice. However, the Court also stated that federal labor laws otherwise continue to apply during the reorganization process, so that the debtor-in-possession remains legally "obligated to bargain collectively with the employees' certified representative over the terms of a new contract pending rejection of the existing contract or following formal approval of rejection by the bankruptcy court."⁴²

In sum, it is apparent that the nature and function of a labor union, and the statutory rights it has vis-a-vis the debtor, are radically different from those of other business entities that have an interest in Chapter 11 reorganizations. Further, the source of a union's purported interest in Chapter 11 proceedings, a collective bargaining agreement, materially differs from an ordinary commercial contract. It is therefore understandable that the appointment of labor union representatives to creditors' committees poses rather complex legal problems.

A. *The Union as a "Creditor"*

To be eligible for appointment to a creditors' committee, a union must first qualify as a "creditor." Unions generally base

39. See, e.g., Gregory, *The Collective Bargaining Agreement: Its Nature and Scope*, 1949 WASH. U.L.Q. 3, 11-13. Another leading author has noted that "[t]he collective agreement differs as much from a common contract as Humpty Dumpty differs from a common egg." Summers, *Judicial Review of Labor Arbitration or Alice Through the Looking Glass*, 2 BUFF. L. REV. 1, 17 (1952).

40. 29 U.S.C. § 185(a)(1982).

41. 29 U.S.C. § 158(d)(1982).

42. 104 S. Ct. at 1201.

their argument for creditor status on one of the following four types of claims: (1) claims for withheld union dues which the debtor-employer has not forwarded to the union; (2) claims for unpaid contributions to union pension and welfare plans; (3) claims for unpaid wages; and (4) claims for damages flowing from the debtor-employer's rejection of the collective bargaining agreement.

Section 101(9) defines a "creditor" as an "entity that has a claim against the debtor that arose at the time of or before the order for relief"⁴³ or which the law treats as having arisen at that time. A union can easily maintain that it is an "entity." Under section 101(14),⁴⁴ an "entity" includes a "person"; under section 101(33),⁴⁵ "person" includes a "corporation"; under section 101(3),⁴⁶ "corporation" includes an "unincorporated company or association"; and the legislative history clearly indicates that Congress intended for "unincorporated associations" to include labor organizations.⁴⁷

A labor union may have more difficulty, however, establishing that it has a "claim" against the debtor. Section 101(4) defines "claim" in terms of a "right to payment."⁴⁸ Certainly a labor union has a "right to payment" of the union dues which the employer is obligated to forward under an agreement. The other payments which the employer is obligated to make are actually owed to the individual employees (in the case of wages), to a pension fund administrator or plan (in the case of employer pension fund contributions), to an insurance carrier (in the case of insurance premiums), or to some other third party, and not to the union as an entity in its own right. With respect to these obligations, it is difficult to see how the union has a "right to payment." Indeed, failure to establish a "right to payment" was one of the reasons why the bankruptcy court in *In re Altair Air-*

43. 11 U.S.C. § 101(9)(1984).

44. 11 U.S.C. § 101(14)(1984).

45. 11 U.S.C. § 101(33)(1984).

46. 11 U.S.C. § 101(3)(1984).

47. H.R. REP. NO. 595, 95th Cong., 1st Sess. 309, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787, 6266; S. REP. NO. 989, 95th Cong., 2nd Sess. 22, reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5787. See also *In re Schatz Federal Bearings Co.*, 5 B.R. 543, 546 (Bankr. S.D.N.Y. 1980).

48. 11 U.S.C. § 101(4)(1984).

lines⁴⁹ declined to appoint a representative of the Air Line Pilots Association to the creditors' committee of Altair Airlines. Although the debtor airline owed the pilots, in the aggregate, \$676,120 in unpaid wages and fringe benefits, which was the second largest claim against it, the bankruptcy court concluded that the "right to payment" for these claims lay in the individual employees, and as a result, the Pilots Association did not qualify for membership on the creditors' committee.⁵⁰

The court also concluded that the Association lacked standing to assert a claim or to serve on the creditors' committee as the agent of the individual employees. While noting that under the old bankruptcy act the definition of "creditor" specifically included a "duly authorized agent, attorney, or proxy," the court observed that this language was omitted from the new Code. The court construed this omission as a clear manifestation of congressional intent to preclude the appointment of representatives to creditors' committees.⁵¹ In this regard, the court apparently believed that the Supreme Court's decision in *Nathanson v. NLRB*⁵² was implicitly superceded by certain provisions of the new Code.

The *Nathanson* Court, citing the statutory definition of "creditor" which then included the "agent" of anyone to whom a debt was owed,⁵³ held that the National Labor Relations Board had standing to file proof of a claim for the back wages that the Board had ordered the bankrupt to pay its employees as a result of unfair labor practices. The Court noted that

[t]he Board is the public agent chosen by Congress to enforce the National Labor Relations Act. . . . A back pay order is a reparation order designed to vindicate the public policy of the statute by making the employees whole for losses suffered on account of an unfair labor practice. . . . Congress has made the Board the only party entitled to enforce the Act.⁵⁴

It is unclear whether the new Code overruled *Nathanson* on this narrow question; even if it did not, its facts are easily distin-

49. 25 B.R. 223 (Bankr. E.D. Pa. 1982).

50. *Id.* at 225.

51. *Id.* at 224-25.

52. 344 U.S. 25 (1952).

53. Current version codified at 11 U.S.C. § 101(9)(1984).

54. *Id.* at 27.

guished from a situation involving a labor union's claims of "creditor" status vis-a-vis debts that have accrued to employees under a collective bargaining agreement. The latter situation does not involve the enforcement of a federal statute; failure to pay wages under a collective bargaining agreement is merely the breach of a contract, not an unfair labor practice. A breach-of-contract award for back pay, although certainly consistent with federal labor policy, is essentially a matter of private relief and not the vindication of public rights. Unlike an NLRB back pay order, which can be enforced only by the Board, debts owed under a collective bargaining agreement may be enforced by individual employees.⁵⁵

The district court affirmed the bankruptcy court's decision in *Altair*. Although its order is unreported,⁵⁶ the district court apparently relied on language in *In re Schatz Federal Bearings Co.*⁵⁷ to support the conclusion that a union is not a creditor with respect to unpaid wage claims.⁵⁸ In *Schatz*, the union sought appointment to a creditors' committee by virtue of its claim to \$462,843 in unpaid pension fund contributions. The court recognized the union as the "creditor" with respect to these monies, noting that "*unlike wages, which are owed to and enforceable by the debtor's employees, the pension plan payments are funding contributions under a collectively bargained labor agreement.*"⁵⁹ The court in *Altair* interpreted this lan-

55. *Smith v. Evening News Ass'n*, 371 U.S. 195 (1962); *In re Cortland Container Corp.*, 30 B.R. 715 (Bankr. N.D. Ohio 1983). *Contra In re Braniff Airways, Inc.*, 33 B.R. 1 (Bankr. N.D. Tex. 1983), where the court unequivocally stated, in connection with a suit over alleged improprieties in the administration of a collective bargaining agreement pension plan, that "[t]he individual workers have no standing to assert claims based on alleged violations of a collective bargaining agreement." *Id.* at 3. The court, however, was undoubtedly mistaken. The authority cited by the court, *Ramsey v. Signal Delivery Serv., Inc.*, 631 F.2d 1210, 1212 (5th Cir. 1980), stands for the proposition that individual employees cannot be sued for their breaches of the collective bargaining agreement, a correct conclusion. See *Atkinson v. Sinclair Ref. Co.*, 370 U.S. 238 (1962). The court in *Braniff* erred in assuming that the converse of that is also true.

56. See *In re Altair Airlines, Inc.*, 727 F.2d 88, 88 (3d Cir. 1984).

57. 5 B.R. 543 (Bankr. S.D.N.Y. 1980).

58. 727 F.2d at 89 (the court of appeals indicated that the district court had relied on *Schatz*).

59. 5 B.R. at 545 (emphasis added). The distinction drawn by the court in *Schatz* is unconvincing. First, unpaid wages are usually no less an obligation "under a collective bargaining agreement" than are unpaid pension contributions. Second, the wage provisions of a collective bargaining agreement are as "enforceable" by a union as they are by individual employees. Finally, pension payments are not usually paid to the union any

guage as implying that a union would *not* qualify as a "creditor" with respect to unpaid wages, and as a result the court rejected the union's claim. On appeal, the debtor-employer in *Altair* thus characterized the test in terms of a union's right to actually "collect" the debt, in contrast to serving merely as a conduit through which the payment is made. The Third Circuit Court of Appeals found this distinction "entirely too metaphysical."⁶⁰ The court noted that the Bankruptcy Code recognizes estates and trusts as entities capable of having claims against debtors, and that "[t]he representative capacity of such fiduciaries is essentially no different, for purposes of participation in a creditors' committee, than the representative capacity, under federal common law, of a labor organization."⁶¹

The court of appeals in *Altair* adopted a different test for determining whether an entity like a labor union has a "right to payment," and is therefore a "creditor" with a "claim" against the debtor, thus making the union eligible to serve on a creditors' committee, by focusing on the entity's standing to bring the claim. Under the *Altair* analysis, an entity with standing to sue on a claim is necessarily a "creditor" with respect to that claim. Noting that federal law permits a labor union to enforce the terms of a collective bargaining agreement in the federal courts, including suits for unpaid wages and vacation pay, the court apparently concluded that, as a matter of logic, a union is a "creditor" with respect to those wage claims.⁶² The notion that having the right to sue to enforce the contract under which a debt arises makes one a "creditor" in the statutory sense was explored more fully by the bankruptcy court in *Schatz*. *Schatz*, in fact, adopted the standing test as controlling with respect to unpaid pension

more than are wage payments. Indeed, in *Schatz*, the pension payments were to be made to a specific insurance company, a company which the debtor had correctly listed as a "creditor" in the case. *But cf.* *Johnson v. England*, 356 F.2d 44, 51 (9th Cir. 1966), *cert. denied*, 384 U.S. 961 (1966) (identifying the employees as "creditors" with respect to unpaid pension fund contributions).

60. 727 F.2d at 90.

61. *Id.* The court's analogy, however, ignores certain distinctions. Trusts and estates are entitled to "collect" debts owed the beneficiary or deceased, and payment to the trust or estate discharges the debt. P. HASKELL, PREFACE TO THE LAW OF TRUSTS 107 (1975); RESTATEMENT (SECOND) OF TRUSTS, § 177 (1959). In contrast, a union has no right to collect or to receive the wages due an employee, and any such payment would certainly not discharge the employer's debt to the employee.

62. 727 F.2d at 90.

fund contributions.⁶³ This standing-equals-creditor analysis, however, is flawed. Under federal law, many entities, including the Secretary of Labor,⁶⁴ have authority to enforce an employer's contractual obligation to fund a pension plan. Not all of these entities, however, have a "claim" against the debtor in the sense that they have a "right to payment."⁶⁵ Additionally, the *Schatz/Altair* approach fails to account for the difference between a "right to payment" and a "right to compel payment." Although the triangular employer/union/employee relationship and the collective bargaining agreement regulating it are unique in many respects, the closest common law analogy is to a third party beneficiary arrangement. In the simplest example of a third party beneficiary arrangement, A, for adequate consideration, makes a promise to B to pay C \$100. If A fails to perform and C's rights under the contract have vested, then C may sue to recover the \$100. C, in other words, has a "right to payment" of \$100; C has a "claim" against A; and C is thus a "creditor" under the Code. B, of course, would also have a cause of action, because A has breached the contract. B could thus sue to compel A to make payment to C. B's suit, however, would have to be in the form of an equitable action for specific performance; under the Bankruptcy Code, a right to an equitable remedy does not give rise to a "claim" unless the breach could also be translated into monetary damages.⁶⁶ Certainly the original obligee of a third party beneficiary contract may suffer monetary damages when the obligor fails to make payment to the beneficiary. However, the measure of those damages is not the amount the obligor promised to pay to the beneficiary; it is the economic injury that the original obligee suffered as a consequence of the breach. With respect to those damages, the obligee B clearly has a "right to payment" or a "claim" against the obligor A in that amount,

63. 5 B.R. at 547-48. The court concluded that although the union had no right to sue under the Employee Retirement Income Security Act of 1974 (ERISA), 29 U.S.C. §§ 1001-1461 (1982), it could sue under § 301 of the Labor Management Relations (Taft-Hartley) Act, 29 U.S.C. § 185(a)(1982), because the employer's funding obligation under the pension plan had been incorporated by reference into the terms of the collective bargaining agreement.

64. 29 U.S.C. § 1132(a)(5)(1982).

65. See Soble, Eggerstsen & Bernstein, *Pension Related Claims in Bankruptcy*, 56 AM. BANKR. L.J. 155, 174 (1982).

66. 11 U.S.C. § 101(4)(b)(1984); see 2 COLLIER ON BANKRUPTCY ¶ 101.04 at 101-16.2 (15th ed. 1983).

and is thus a "creditor" who, if the amount of that claim is among the top seven claims, is entitled to sit on the creditors' committee.

The right of the union representative to be a member of the creditors' committee should be evaluated in a similar fashion. If a debtor-employer has breached its duty under a collective bargaining agreement to pay its employees wages or to contribute to a pension or welfare fund, then the union which has suffered a breach of contract is certainly a "creditor" under the Bankruptcy Code with respect to any damages that flow to it from that breach. The ranking that the union enjoys as a creditor must be determined, however, not by reference to the total amount of payments owed to third parties (*i.e.* payments owed to employees, pension fund administrators and others), but rather by reference to whatever incidental damages the union suffers as a result of the breach.⁶⁷

A union's status as the statutory "agent" of the employees does not improve its position as a would-be "creditor." This lack of creditor status does not result because agents necessarily lack standing under the Code, notwithstanding the contrary implications of *Altair*. The omission of any reference to "agents" in the Code's definition of "creditors" is more readily explained by the redundancy of any such inclusion: if a person is qualified to file a claim, then that person's agent is necessarily similarly qualified. The agent's status does not necessarily result in creditor status because being the agent of 100 creditors who each have a \$100 "claim" against a debtor does not make that agent a \$10,000 "creditor" under the Bankruptcy Code, whether the individual creditors are small businesses and tradesmen, or individual employees.

In sum, if the term "creditor" is given its ordinary and intended meaning, then it would be a rare case indeed in which a labor union would be legally entitled to sit on a creditors' committee. Moreover, even if the right to bring a lawsuit is sufficient to qualify the union as a creditor, there are still other reasons why an entity of this nature should not be appointed to a creditors' committee.

67. See Soble, Eggerstsen & Bernstein, *supra* note 65, at 174.

B. *The "Conflict of Interest" Problem*

Under the old bankruptcy act, the most common disqualification of a creditor from membership on the creditors' committee was the existence of conflicts of interest between that creditor and others.⁶⁸ Because of the increased importance of the creditors' committee under the Bankruptcy Code, it is believed that the pre-Code conflict-of-interest rules will continue to apply, perhaps even more strictly.⁶⁹ Assuming that under a broad definition of the term, a labor union somehow qualifies as a "creditor" whose claim is of sufficient size to make it otherwise eligible for membership on the creditors' committee, considerable conflict-of-interest problems remain.

The most obvious conflict arises from the fact that the union's primary interest in representing the employees often will not be the collection of the debt which qualified the union as a "creditor," but rather the immediate preservation of jobs. This interest, however, may conflict with the interests of the other creditors in reducing the workforce or liquidating the business in order to preserve the debtor's estate.⁷⁰

This conflict-of-interest argument, made to both the bankruptcy court in *Schatz* and the Third Circuit in *Altair*, was not successful in either case. The court in *Altair* responded that "[s]uch conflicts of interest are not unusual in reorganizations. Materialman creditors, for example, may sometimes prefer to forego full payment for past sales in hopes of preserving a customer, while lenders may prefer liquidation and prompt payment."⁷¹ Moreover, one of the functions of the creditors' committee is to study the debtor's business and "the desirability of the continuance of such business."⁷² The court further reasoned that if the voice of the creditor most interested in continuance is

68. Meir & Brown, *Representing Creditors' Committees Under Chapter 11 of the Bankruptcy Code*, 56 AM. BANKR. L.J. 217, 219 (1982).

69. *Id.* The House Report referred to creditors' committees as "representative bodies which must speak for groups of creditors with similar interests." H.R. REP. No. 595, 95th Cong., 2nd Sess. 235 (1977), reprinted in 1978 U.S. CODE CONG. & AD. NEWS 5963 (emphasis added). See also *In re Johns-Manville Corp.*, 26 B.R. 919, 924-25 (Bankr. S.D.N.Y. 1983).

70. See Soble, Eggerstsen & Bernstein, *supra* note 65, at 174.

71. 727 F.2d at 90. See also 5 B.R. at 548.

72. 727 F.2d at 90 (quoting 11 U.S.C. § 1103(c)(2)).

not heard, the committee cannot make a fair and reasoned decision on that issue.⁷³ The *Altair* court's reasoning is unpersuasive. First, it simply assumes that materialman creditors would likewise not be subject to disqualification due to divergency of their interests from those of other creditors.⁷⁴ Indeed, in such a situation, two committees might be appropriate.⁷⁵ Further, the union's interest in being heard can be served in other ways. The Code itself contemplates the right of a "party in interest" to be heard on the merits of a reorganization plan.⁷⁶ More specifically, Bankruptcy Rule 2018(d) provides:

In a Chapter 9 or 11 case, a labor union or employees' association, representative of employees of the debtor, shall have the right to be heard on the economic soundness of a plan affecting the interests of the employees but it may not appeal from any judgment, order, or decree in the case unless otherwise permitted by law.⁷⁷

Alternatively, it has been suggested that a union representative be appointed as an ex officio, nonvoting member of the creditors⁷⁸ or otherwise asked to participate informally in some of the committee's functions.⁷⁹ Either approach would allow due recognition to the union's primary interest in the preservation of jobs, while preventing that recognition from conflicting with the other creditors' primary interests in collecting their debts.

There are, however, additional conflict-of-interest problems. One problem arises when the union's status as a "creditor" is

73. *Id.* at 90-91. It should be noted that as soon as the bankruptcy court in *Schatz* approved the sale of the debtor's business to a third party, with whom the union then negotiated a new labor contract, the union sought and obtained the court's permission to withdraw from the committee. Such a course of conduct may be taken as evidence of the narrowness of the union's interest in these matters. *In re Schatz Federal Bearings Co.*, 11 B.R. 363 (Bankr. S.D.N.Y. 1981).

74. See generally 5 COLLIER BANKRUPTCY PRACTICE GUIDE ¶ 83.03[2] (1984) (the existence of possible adverse interests should not automatically bar an unsecured creditor from serving on a creditors' committee).

75. See 5 COLLIER ON BANKRUPTCY ¶ 1102.02 at 1102-14 (15th ed. 1983) ("where there are significant groups of creditors or equity security holders with conflicting claims which are likely to be affected by the plan of reorganization, the court should authorize the appointment of additional committees").

76. 11 U.S.C. § 1109(b)(1984); see *Soble, Eggerstsen & Bernstein, supra* note 65, at 174 n. 113.

77. Bankr. Rule 2018(d).

78. DeNatale, *supra* note 24, at 57 n.71.

79. 5 COLLIER BANKRUPTCY PRACTICE GUIDE ¶ 83.04[1] (1984).

allegedly based on the debtor-employer's unpaid contributions to a pension plan. As the surrogate creditor, the union would be expected to represent all of the intended beneficiaries of the plan, including active employees *and* retirees. The two groups, however, do not have concurrent interests. Active employees are usually more interested in preserving their jobs than they are in providing full funding to the pension plan, while pensioners have the opposite interest.⁸⁰ Moreover, the union is not free to compromise or accommodate these two interests. Under the LMRA, the union has a combined right/duty (with the emphasis here upon the element of "duty") to represent the interests of *active* employees within a collective bargaining unit.⁸¹ In *Allied Chemical & Alkali Workers v. Pittsburgh Plate Glass Co.*,⁸² the Supreme Court, in an analogous situation, held that this duty of representation precluded the union from attempting to bargain on behalf of the retired employees over certain changes the employer had made to health benefits. Similarly, if a union attempts to serve as the "representative creditor" of the beneficiaries of a pension plan, it would seem that there is a high probability of its violating one of two different fiduciary duties, either that owed under the Bankruptcy Code to all beneficiaries, including retirees, or that owed under the LMRA only to active employees within the bargaining unit.

This conflict would not, however, preclude a union representative from serving on a creditors' committee in the capacity of a union-appointed trustee of a jointly administered Taft-Hartley Act trust.⁸³ In such a capacity, the union representative's real interests may still lie in favor of active employees, but the conflict of interest has already been resolved: the labor-law duty of fair representation is subordinated *by federal statute* to the duties of the plan trustee. The Employee Retirement Income Security Act (ERISA)⁸⁴ dictates that the union-appointed repre-

80. Soble, Eggerstsen & Bernstein, *supra* note 65, at 175; DeNatale, *supra* note 24, at 57-58.

81. *See supra* note 37.

82. 404 U.S. 157 (1971).

83. *See generally* Soble, Eggerstsen & Bernstein, *supra* note 65, at 175-77 (discussing the priority that plan trustees must place upon the interests of the plan participants, as required by ERISA).

84. 29 U.S.C. §§ 1001-1461 (1982).

sentatives serve the interests of all plan participants.⁸⁵ The courts have held that this fiduciary duty is breached when the exclusive interests of the union or of its active members are given priority.⁸⁶ Similar statutory protection of all plan participants is lacking, however, when a union attempts to gain creditor status in its own right rather than as a plan trustee.

The union's duty, under federal labor law, to represent vigorously the interests of bargaining unit employees may conflict with its duties as a member of the creditors' committee in yet another way. Under the recently enacted Code provisions, the debtor-employer is required to propose contract modifications that "assure that *all creditors*, the debtor and all of the affected parties are treated fairly and equitably."⁸⁷ Presumably, if the proposal meets that requirement, the members of the creditors' committee must view it favorably. As a member of that committee, a union representative would have the duty to support such a proposal or, at least, to refrain from active, partisan opposition. A proposal that is fair to "all creditors" and to other "affected parties," including equity stockholders, is not necessarily a proposal that is in the best interests of the employees as a separate class. Yet, in its capacity as the statutory bargaining representative of these employees, the union is compelled by federal law to represent only the employer's special interests, even at the expense of the interests of other creditors.⁸⁸ In short, the union's duties as a member of the creditors' committee are inherently inconsistent with its duties as a bargaining representative.

Moreover, while bargaining over the debtor-employer's proposed modifications, the union *apparently* retains the right to strike. The new Code provision certainly does not prohibit it. Although the bankruptcy court, under its broad section 105 eq-

85. 29 U.S.C. § 1104(a)(1982).

86. See, e.g., *Blankenship v. Boyle*, 329 F. Supp. 1089, 1094-95 (D.D.C. 1971).

87. 11 U.S.C. § 1113(b)(1)(A)(1984).

88. Presumably, a union's refusal to accept proposed modifications that are fair to all of the creditors as a class would be deemed "without good cause," thus freeing the court to approve the debtor-employer's rejection of the contract. That, however, is not the end of the union's influence, as it can still use economic power to prevent the debtor-employer from putting the rejection into effect. See *infra* notes 89-92 and accompanying text.

uity powers,⁸⁹ would otherwise have the power to enjoin such an egregious interference with the reorganization process, in analogous contexts the courts have held that the anti-injunction provisions of the Norris-LaGuardia Act control. For example, unions have been allowed to strike to compel continued adherence to the terms of a contract even after a bankruptcy court has approved its rejection⁹⁰ and to strike in support of its demands for a new contract.⁹¹ Although such conduct may not be affirmatively illegal under the Bankruptcy Code, it is certainly inconsistent with the fiduciary duties of a member of the creditors' committee. Such a strike not only puts the union at an unfair advantage vis-a-vis the other creditors, but, more importantly, it may frustrate the entire reorganization process, driving the debtor into an otherwise unnecessary liquidation.⁹²

This conflict between a union's duty under the federal labor laws to represent vigorously the special interests of the debtor's employees and its fiduciary duties as a member of a creditors' committee is somewhat analogous to the conflict that arose in *In re Johns-Manville Corp.*⁹³ There, an attorney for an asbestos claimant continued a state court legal action even after Manville had filed under Chapter 11 and the automatic stay against such actions had come into effect. The attorney apparently acted on the theory that the bankruptcy court lacked jurisdiction. The court not only found the attorney in contempt, but also disqualified him from further membership on the creditors' committee. The court noted the critical role of the members of a creditors' committee in negotiating a plan of reorganization, in supervising the debtor, and in protecting their constituents' interests:

Accordingly, the individuals constituting a committee should

89. 11 U.S.C. § 105(a)(1984).

90. See, e.g., *Crowe & Assocs. v. Bricklayers Local 2*, 713 F.2d 211 (6th Cir. 1983); *Petrusch v. Teamsters Local 317*, 667 F.2d 297 (2d Cir. 1981), cert. denied, 456 U.S. 974 (1982); *Briggs Transp. Co. v. International Bhd. of Teamsters*, 116 L.R.R.M. (BNA) 2241 (D. Minn. 1984).

91. See *In re Gray Truck Line Co.*, 34 B.R. 174, 179 (Bankr. M.D. Fla. 1983)(dicta).

92. "The argument that [the debtor-employer] may go out of business absent the requested injunction is no more than a recognition that one of the unfortunate side effects of labor-management strife is economic loss to the employers and employees." *Briggs Transp. Co.*, 116 L.R.R.M. (BNA) at 2244. See also *Crowe & Assocs.*, 713 F.2d at 216; *Truck Drivers Local 807 v. Bohack Corp.*, 541 F.2d 312, 318 (2d Cir. 1976); *Petrusch v. Teamsters Local 317*, 14 B.R. 825, 830 (Bankr. N.D.N.Y. 1981).

93. 26 B.R. 919 (Bankr. S.D.N.Y. 1983).

be honest, loyal, trustworthy, and without conflicting interests, and with undivided loyalty and allegiance to their constituents. . . . Conflicts of interest on the part of representative persons or committees are thus not [to] be tolerated. . . . Thus, where a committee representative or agent seeks to represent or advance the interest of an individual member of a competing class of creditors or various interests or groups whose purposes and desires are dissimilar, this fiduciary is in breach of his duty of loyal and disinterested service.⁹⁴

The court then found that in at least three ways the attorney's functions on the committee and his larger fiduciary duty to the estate were in conflict with his actions and duties on behalf of a single claimant. First, the court noted that in the state court proceeding the attorney was contesting the very jurisdiction of the bankruptcy court, while as a committee member he was sanctioning the bankruptcy court's jurisdiction by working within its framework to foster his constituents' interests in the context of a reorganization plan.⁹⁵ A union which strikes over the proposed rejection of a collective bargaining agreement and then contests the bankruptcy court's jurisdiction to enjoin that strike would be in a similar position.⁹⁶

Second, the court in *Manville* noted that the attorney's actions in independently prosecuting a law suit in state court were "designed to benefit his client . . . and/or his own private interests in particular as opposed to benefitting [sic] all members of the asbestos claimants class which he represents as a committee member and fiduciary."⁹⁷ The court pointed out that because the interests of a single asbestos litigant may differ substantially from the interests of all asbestos claimants, one of these interests is bound to suffer as a result of the attorney's dual represen-

94. *Id.* at 925.

95. *Id.* at 926.

96. Although several lower courts have held that the Norris-LaGuardia Act deprives the bankruptcy court of jurisdiction to enjoin such a strike, see cases cited *supra* at notes 90-91; the Supreme Court has never addressed the question. Thus, the correctness of those decisions may certainly be questioned. See generally Note, *The Automatic Stay of the 1978 Bankruptcy Code Versus the Norris-LaGuardia Act: A Bankruptcy Court's Dilemma*, 61 Tex. L. Rev. 321 (1982). Because the issue is still unsettled, it is quite probable that a union might pursue the dual strategy of striking over a collective bargaining agreement and contesting the jurisdiction of the bankruptcy court to enjoin the strike.

97. 26 B.R. at 926.

tation.⁹⁸ A union's action in making interim wage and benefit demands, in going on strike to enforce them, or even in filing unfair labor practice charges would similarly be expected to benefit the special interests of the union and of the employees it represents, rather than the creditors as a class, who may indeed be positively harmed by such conduct.

Third, the court noted that as a member of the committee the attorney had access to confidential information regarding Manville's reorganization plans and operations, "which information is not intended to be used in fostering the rights of private litigants outside the context of protecting these creditors as a group in these bankruptcy proceedings."⁹⁹ In *Schatz*, a similar objection was made to the appointment of the union to the creditors' committee, but the court discounted it. There, the court reasoned that because of the employer's status as a Chapter 11 debtor, much of the information revealed to the creditors' committee could be obtained by the union through alternative channels.¹⁰⁰ It is not clear exactly what the court had in mind. The new labor provisions of the Bankruptcy Code would, of course, have entitled the union to whatever information it needed in order to evaluate the debtor-employer's proposed modifications.¹⁰¹ Also, to the extent that it applies to bargaining at that stage,¹⁰² the LMRA would impose a similar duty.¹⁰³ However, the quantum and nature of information that the union may obtain as a member of the creditors' committee is considerably broader. Apparently recognizing the inherent danger of granting a union free access to the debtor-employer's business files and records,

98. *Id.*

99. *Id.* See also *In re Wilson Foods Corp.*, 31 B.R. 272 (Bankr. W.D. Okla. 1983) (disqualification of a creditor who also happened to be a substantial competitor).

100. 5 B.R. at 548.

101. 11 U.S.C. § 1113(b)(1)(B)(1984). The court may also enter a protective order where further disclosure by the union "would compromise the position of the debtor with respect to its competitors in the industry in which it is engaged." 11 U.S.C. § 1113(d)(3)(1984).

102. See *supra* note 13.

103. Under the Labor Management Relations (Taft-Hartley) Act, 29 U.S.C. § 158(a)(5)(1982), a union has a right to obtain from the employer information that is directly relevant to the union's collective bargaining duties. See generally C. MORRIS, *THE DEVELOPING LABOR LAW* 606-29 (2d ed. 1983). In particular, when an employer claims an "inability to pay," as would the debtor in the context of bankruptcy, then it must be possible to substantiate that claim with relevant financial data. *NLRB v. Truitt Mfg. Co.*, 351 U.S. 149 (1956).

the court in *Schatz* also noted that it had the power to issue protective orders.¹⁰⁴

III. CONCLUSION

Certainly, the employees of a Chapter 11 debtor-employer, and the union representing them, have a legitimate interest in an attempted reorganization. It is not an interest, however, that warrants membership on the official unsecured creditors' committee. A union qualifies as a major "creditor" only in a loose and figurative sense of the word. Even if the prevailing definition of that term is correct, the union's real or primary interest will often lie not in the collection of the funds owed it or its members, already afforded some degree of priority, but in insuring the continuation of the business. Thus, a union would obtain membership on the creditors' committee by reference to one interest, but then use that membership to promote quite a different interest.

Moreover, a union's duties as the employees' exclusive bargaining agent under the federal labor laws potentially conflict with the duties that a union would have as a member of the committee. Indeed, to the extent that the union through the negotiation of high wages and restrictive work rules, may have contributed significantly to the very financial condition that the Chapter 11 debtor and its committee of creditors attempt to resolve, the union could be deemed to be in an "adversarial" position with respect to the other creditors.

The exclusion of union representatives from the official creditors' committee does not leave union and employee interests unprotected. The new Code provisions give a union rights concerning the rejection of existing collective bargaining agreements enjoyed by no other party to an executory contract with the debtor. Moreover, under the LMRA, the debtor-employer remains obliged to continue to recognize the union as the exclusive representative of its employees and to bargain with it in good faith over the terms of any new agreements that are reached. It would seem that these rights, coupled with the union's status as a "party in interest" with standing to be heard

104. 5 B.R. at 548.

on the reorganization plan, give more than adequate protection to the interests of the employees. The presence of a union representative on the creditors' committee adds nothing to these rights and only creates unnecessary conflict and confusion in the statutory scheme.

