

Spring 3-1-1960

## Status In Bankruptcy Of Contributions Owed To Union Welfare Funds

Follow this and additional works at: <https://scholarlycommons.law.wlu.edu/wlulr>



Part of the [Bankruptcy Law Commons](#)

---

### Recommended Citation

*Status In Bankruptcy Of Contributions Owed To Union Welfare Funds*, 17 Wash. & Lee L. Rev. 117 (1960), <https://scholarlycommons.law.wlu.edu/wlulr/vol17/iss1/11>

This Comment is brought to you for free and open access by the Washington and Lee Law Review at Washington & Lee University School of Law Scholarly Commons. It has been accepted for inclusion in Washington and Lee Law Review by an authorized editor of Washington & Lee University School of Law Scholarly Commons. For more information, please contact [lawref@wlu.edu](mailto:lawref@wlu.edu).

between joint tortfeasors has more recently been recognized in some jurisdiction,<sup>36</sup> but contribution between sureties of a different nature<sup>37</sup> has not yet been recognized by the courts.<sup>38</sup>

In conclusion, when the equities of the quasi-surety are superior, it should prevail; when the equities of the true surety are superior, it should prevail; but when the equities are truly equal, contributive subrogation should be allowed. Only in this manner will both the *equitable* doctrine of subrogation and the *equitable* doctrine of contribution be made truly *equitable*.

ROBERT J. BERGHEL

### STATUS IN BANKRUPTCY OF CONTRIBUTIONS OWED TO UNION WELFARE FUNDS

A current problem under the Bankruptcy Act<sup>1</sup> is the status of employer contributions owed to union welfare funds when the employer becomes bankrupt.<sup>2</sup> While wages due to workmen have long been afforded priority of payment in federal bankruptcy proceedings,<sup>3</sup> difficulty has arisen in determining what constitutes wages within the meaning of the priority section.<sup>4</sup> After the passage of the Act of 1898, a distinction was drawn between wages and salary,<sup>5</sup> and when

---

contract or express agreement, but this has probably been replaced by the theory of enforcement based on equitable obligation. *Deering v. Winchelsea*, 2 Bos. & Pul. 270, 126 Eng. Rep. 1276 (Ex. 1787).

<sup>36</sup>*Wait v. Pierce*, 191 Wis. 202, 210 N.W. 822 (1926). There are two theories under which recovery was sought: (1) quasi-contract to help bear the common burden, *Builders Supply Co. v. McCabe*, 266 Pa. 322, 77 A.2d 368 (1951); *Proff v. Maley*, 14 Wash. 2d 287, 128 P.2d 330 (1942); and (2) prevention of unjust enrichment, *Pennsylvania Greyhound Lines, Inc. v. Rosenthal*, 14 N.J. 372, 102 A.2d 587 (1954).

<sup>37</sup>See note 29 *supra*.

<sup>38</sup>*King*, *Subrogation under Contracts Insuring Property*, 30 Texas L. Rev. 62, 65 (1951); *Langmaid*, *op. cit. supra* note 29, at 991 (both with regard to insurer).

<sup>1</sup>Bankruptcy Act § 64(b)(4), 30 Stat. 563 (1898), 11 U.S.C. § 104(a)(2) (1958).

<sup>2</sup>In the following cases contributions were held not to be preferred: *Local 140 Security Fund v. Hack*, 242 F.2d 375 (2d Cir. 1957), cert. denied, 355 U.S. 833 (1957); *In the Matter of Victory Apparel Mfg. Corp.*, 154 F. Supp. 819 (D.N.J. 1957); *In the Matter of Sleep Products, Inc.*, 141 F. Supp. 463 (S.D.N.Y. 1956), cert. denied, 355 U.S. 833 (1957); *In the Matter of Brassel*, 135 F. Supp. 827 (N.D.N.Y. 1955); *contra*, *Matter of Otto*, 146 F. Supp. 786 (S.D. Cal. 1956).

<sup>3</sup>The Act of Aug. 19, 1841, ch. 9 § 5, 5 Stat. 445, established the priority.

<sup>4</sup>*Nathanson v. NLRB*, 344 U.S. 25 (1952) (NLRB order within three months of bankruptcy proceeding to pay wages accrued more than three months prior to proceeding given priority).

<sup>5</sup>*First Nat'l Bank v. Barnum*, 160 Fed. 245 (M.D. Pa. 1908).

courts had difficulty giving meaning to the terms "workmen, clerks and servants"<sup>6</sup> in the 1898 Act,<sup>7</sup> Congress amended the Act.<sup>8</sup>

In *United States v. Embassy Restaurant, Inc.*<sup>9</sup> the Supreme Court solved a current problem in this area by holding that contributions owed to a union welfare fund are not "wages . . . due to workmen" within the priority section of the Bankruptcy Act.<sup>10</sup> Embassy was required by collective bargaining agreements with local unions to contribute to the union welfare fund a specified amount each month for each full-time employee.<sup>11</sup> Embassy failed to contribute for the three months prior to the filing of a petition in bankruptcy. In the bankruptcy proceeding the trustees of the welfare fund claimed the full amount of the unpaid contributions on the ground that the claim was entitled to priority as wages under the Bankruptcy Act.<sup>12</sup> The referee disallowed the claim, but the United States District Court vacated the order and granted the requested priority.<sup>13</sup> The Court of Appeals for the Third Circuit affirmed,<sup>14</sup> but the Supreme Court reversed the lower courts' decisions and reinstated the order of the referee.<sup>15</sup> Mr. Justice Clark in delivering the opinion for the majority said, "The broad purpose of the Bankruptcy Act is to bring about an equitable distribution of the bankrupt's estate. . . ."<sup>16</sup> Consequently, "if one claimant is to be preferred over others, the purpose should be clear from the statute."<sup>17</sup> The court also pointed out that "if the contributions are placed in the wage priority class, they will likewise be rendered non-dischargeable."<sup>18</sup> Therefore, they will remain outstanding debts of the bankrupt if the assets of the estate are insufficient

<sup>6</sup>In re Greenwald, 99 Fed. 705 (E.D. Pa. 1900) (traveling salesman denied priority); In re Scanlan, 97 Fed. 26 (D. Ky. 1899); In re Grubbs-Wiley Grocery Co., 96 Fed. 183 (W.D. Mo. 1899) (manager denied priority).

<sup>7</sup>See note 1 supra.

<sup>8</sup>Bankruptcy Act, § 64(b)(4), 30 Stat. 563 (1898), 11 U.S.C. § 104 (a)(2) (1958) (traveling and city salesmen included in priority section).

<sup>9</sup>359 U.S. 29 (1959).

<sup>10</sup>Id. at 35.

<sup>11</sup>Labor Management Relations Act (Taft-Hartley Act) § 302(c), 61 Stat. 157 (1947), 29 U.S.C. § 186(c) (1958) (payments held in trust as required; no question of validity of welfare fund).

<sup>12</sup>See note 8 supra.

<sup>13</sup>Matter of Embassy Restaurant, 254 F. Supp. 141 (E.D. Pa. 1957).

<sup>14</sup>Matter of Embassy Restaurant, 254 F.2d 475 (3d Cir. 1958).

<sup>15</sup>359 U.S. at 29.

<sup>16</sup>Id. at 31, quoting from *Kothe v. R. C. Taylor Trust*, 280 U.S. 224, 227 (1930).

<sup>17</sup>359 U.S. at 31, quoting from *Nathanson v. NLRB*, 344 U.S. 25, 29 (1952); accord, *Kuehner v. Irving Trust Co.*, 299 U.S. 445, 452 (1937).

<sup>18</sup>359 U.S. at 31. See Bankruptcy Act § 17, 30 Stat. 550 (1898), as amended 11 U.S.C. § 35(a)(5) (1958).

to discharge them.<sup>19</sup> The Court recognized the liberal tendencies of Congress in expanding the wage priority provision of the Act,<sup>20</sup> but pointed out that such expansion was in respect to classes of persons and not classes of claims.<sup>21</sup> The Court met the argument that the contributions were in the nature of an assignment of the employee's wages by stating that the agreement establishing the fund required that the contributions should be paid directly to the trustees of the fund. Therefore, the payments were never due to the workmen and could not be assigned by them to the trustees of the fund.<sup>22</sup>

Mr. Justice Black, in a dissenting opinion in which Chief Justice Warren and Justice Douglas concurred, said that there were two grounds upon which this claim should be given priority: (1) the policy of Congress in subsequently expanding the priority section<sup>23</sup> when courts have limited its application;<sup>24</sup> (2) the operation of the collective bargaining agreement as an assignment of the workers' interest in the fund to the trustees.<sup>25</sup>

It would seem that the majority opinion has lost sight of congressional intent concerning contributions to welfare funds. Although Congress has manifested no rule to be followed in the field of Bankruptcy law concerning these contributions, other statutes dealing with welfare funds afford an appropriate basis for gleaning congressional intent concerning the funds. Under the Taft-Hartley Act<sup>26</sup> the workman's interest is deemed sufficient to require protective measures in the form of administration of the welfare and pension plans by trustees,<sup>27</sup> and the courts also consider contributions to the plans to be one of the terms and conditions of employment<sup>28</sup> for which the employer must bargain collectively as required by the Act.<sup>29</sup> The most recent con-

<sup>19</sup>359 U.S. at 31.

<sup>20</sup>See note 8 *supra*.

<sup>21</sup>359 U.S. at 33.

<sup>22</sup>*Id.* at 33-34.

<sup>23</sup>Act of June 15, 1906, ch. 3333, 34 Stat. 267; Act of May 27, 1926, 44 Stat. 667; Act of June 22, 1938, § 1, 52 Stat. 874; Bankruptcy Act § 64, 70 Stat. 725 (1956); 11 U.S.C. § 104(a)(2) (1958).

<sup>24</sup>*In re Greenwald*, 99 Fed. 705 (E.D. Pa. 1900); *In re Scanlan*, 97 Fed. 26, 27 (D. Ky. 1899). For additional cases, see 72 Fed. Dig., Workman, 696 (1941).

<sup>25</sup>359 U.S. at 39.

<sup>26</sup>61 Stat. 136 (1947), 29 U.S.C. §§ 141-97 (1958).

<sup>27</sup>Labor Management Relations Act (Taft-Hartley Act) § 302(c), 61 Stat. 157 (1947), 29 U.S.C. § 186(c) (1958) (payments to union representatives for welfare and pension plans are unlawful unless such payments are held in trust).

<sup>28</sup>*Inland Steel v. NLRB*, 170 F.2d 247 (7th Cir. 1948), cert. denied, 336 U.S. 960 (1949).

<sup>29</sup>Labor Management Relations Act (Taft-Hartley Act) § 8(d), 61 Stat. 140 (1947), 29 U.S.C. § 158(d) (1958).

gressional expression concerning such plans shows that Congress considers the contributions to be both compensation and inducement to workers<sup>30</sup>—both of which have long been held to be synonymous with wages.<sup>31</sup>

The majority opinion bases the holding in part on the broad purpose of the Bankruptcy Act—equitable distribution of the bankrupt's estate and discharge of the bankrupt.<sup>32</sup> In so doing, the Court seems to lose sight of the purpose of the priority section, which is "to furnish distressed workers with a cushion of purchasing power against the impact of their employer's bankruptcy."<sup>33</sup> This purpose is rather summarily brushed aside by saying that if the workmen and the welfare fund participate equally their recovery will be reduced. While appearing self evident, closer examination discloses a flaw in this reasoning. The purpose of the welfare fund is to provide "life insurance, weekly sick benefits, hospital and surgical benefits" and similar advantages for union members.<sup>34</sup> Therefore, if the contributions to the welfare fund are given priority, the workmen's purchasing power will actually be increased since their entire wage recovery can be used to purchase necessities and other items needed immediately.

The majority's rejection of the contention that the contributions are actually an assignment of wages due to the workmen is based on a technicality and ignores the substance of the matter. At least this seems to follow from Congress' own expressions<sup>35</sup> when determining the necessity for the enactment of the Welfare and Pension Plans Disclosure Act.<sup>36</sup> The Senate Committee Report says, "Regardless of the form they take, the employer's share of the cost of these plans or the benefits the employers provide are a form of compensation,"<sup>37</sup> and "the plans are in common use as a competitive inducement to attract and retain good employees."<sup>38</sup> These statements show that Congress considers the contributions to be actually due to workmen, and

<sup>30</sup>S. Rep. No. 1440, 85th Cong. 2d Sess. (1958); 3 U.S. Code Cong. & Ad. News 4137, 4139.

<sup>31</sup>Harris v. Lambros, 56 F.2d 488 (D.C. Cir. 1932); Rickett v. Union Terminal Co., 33 F. Supp. 245, 249 (N.D. Tex. 1940); In re Green, 34 F. Supp. 791, 793 (W.D. Va. 1940); First Nat'l Bank v. Barnum, 160 Fed. 245, 247 (M.D. Pa. 1908).

<sup>32</sup>See notes 16 and 17 *supra* and accompanying text.

<sup>33</sup>In the Matter of Victory Apparel Mfg. Corp., 154 F. Supp. 819, 822 (D.N.J. 1957); accord, Blessing v. Blanchard, 223 Fed. 35, 37 (9th Cir. 1915).

<sup>34</sup>359 U.S. at 30.

<sup>35</sup>See note 30 *supra*.

<sup>36</sup>Public Law 85-836, 72 Stat. 997 (1958).

<sup>37</sup>See note 30 *supra*.

<sup>38</sup>*Ibid.*

it is only for the protection of the parties that the statute requires the plans to be administered by trustees.<sup>39</sup> Since these contributions are due to the workmen, it would follow that they have an interest in them. The Taft-Hartley Act<sup>40</sup> protects this interest by requiring the union and the employer to bargain collectively concerning these plans;<sup>41</sup> therefore, it seems that the collective bargaining agreement itself should be treated as an assignment of the workmen's interest in the contributions to the trustees. In 1907, in the leading case of *Shropshire, Woodliff & Co. v. Bush*,<sup>42</sup> the United States Supreme Court held that an assignment of the wage earner's claim to a third party did not destroy the priority of the claim under the Bankruptcy Act. "The priority is attached to the debt and not to the person of the creditor; to the claim and not to the claimant. The act does not enumerate classes of creditors . . . but, on the other hand, enumerates classes of debts as 'the debts to have priority.'"<sup>43</sup> In his dissent in the *Embassy* case Mr. Justice Black relied on this case, reasoning that the mechanics by which the fund is established are not conclusive as to whether there has been an assignment or not.

It should be pointed out that most of the lower federal court decisions were in accord with the majority opinion.<sup>44</sup> Moreover, while the Internal Revenue Code allows deductions for contributions to union welfare funds as business expenses,<sup>45</sup> it expressly excludes them as wages for purposes of withholding taxes.<sup>46</sup> This Act shows unequivocally the intent of Congress to deny wage status to welfare fund contributions in matters concerning taxation, but the Court itself in the *Embassy* case points out that congressional intent in one context is not absolutely controlling in another context.

When a New York court was confronted with this very same problem and refused to give preferred status to a welfare fund claim, the

---

<sup>39</sup>See note 11 supra.

<sup>40</sup>Labor Management Relations Act (Taft-Hartley Act) § 8(d), 65 Stat. 601 (1951), 29 U.S.C. § 158(d) (1958).

<sup>41</sup>*Inland Steel v. NLRB*, 170 F.2d 247 (7th Cir. 1948), cert. denied, 336 U.S. 960 (1949).

<sup>42</sup>204 U.S. 186 (1907).

<sup>43</sup>Id. at 189.

<sup>44</sup>See note 2 supra.

<sup>45</sup>Int. Rev. Code of 1954 § 162(a)(1).

<sup>46</sup>Int. Rev. Code of 1954 § 3121(a)(2). Int. Rev. Code of 1954 § 162(a)(1), permits such contributions to be deducted as business expenses by the employers. But see, § 3121(a)(2), under which contributions are not wages for purposes of withholding tax. For similar statutory provisions see Fair Labor Standards Act § 7(b)(4), 63 Stat. 913-14 (1949), 29 U.S.C. § 207(d)(4), which provides that the "regular rate" at which an employee is employed shall not include contributions irrevocably paid to trustees as third persons pursuant to bona fide welfare or pension plans.