STATEMENT OF

CAPTAIN JOHN PRATER, PRESIDENT

AIR LINE PILOTS ASSOCIATION, INTERNATIONAL

BEFORE

THE COMMERCIAL AND ADMINISTRATIVE LAW

SUBCOMMITTEE

OF

THE COMMITTEE ON THE JUDICIARY

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WASHINGTON, D.C.

SEPTEMBER 6, 2007

AMERICAN WORKERS IN CRISIS: DOES THE CHAPTER 11 BUSINESS BANKRUPTCY LAWS TREAT WORKERS AND RETIREES FAIRLY?

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Good morning Madame Chairwoman and members of the Subcommittee. I am Captain John Prater, President of the Air Line Pilots Association, International. ALPA represents 60,000 professional pilots who fly for 41 airlines in the United States and Canada. On behalf of our members, I want to thank you for the opportunity to testify today about the urgent need for legislation to restore balance and basic fairness to the Section 1113 process under Chapter 11 of the Bankruptcy Code.

In the aftermath of the events of Sept. 11, 2001, ALPA and other labor unions faced continuous efforts by airlines to use the bankruptcy process as a razor-sharp tool to strip away working conditions and living standards that were built over decades of collective bargaining.

Airline workers have borne far more than their fair share of the pain to save their airlines, as massive pay cuts, lost pensions and other deep concessions clearly attest. Section 1113 of the code has been applied by the bankruptcy courts, at management's instigation, in a manner far removed from the original intent of these provisions. Instead of protecting employees, the 1113 process has been used by employers to unfairly gut the wages and working conditions of airline and other employees. These same employers also used the bankruptcy law to rubber stamp multimillion dollar rewards for the corporate executives who perpetrate these abuses on workers.

After 9/11, many airline managements used the 1113 procedures to not only gut employee wages and working conditions, they also exploited the bankruptcy process to cut staff to the bone. Both of these factors have combined to make piloting a far less desirable job than it used to be, contributing to increased pilot frustration, attrition and turnover at a number of airlines. Added to the understandable employee frustration and anger, these additional, related problems make the implications of failing to restore balance to the bankruptcy process more serious than just ending the immorality of this unfairness. The current imbalance has created a poisoned environment that has greatly undermined labor relations and employee good will in the airline industry, which are critical to the efficient operation of our essential national air transportation system.

Indeed, ALPA has seen that airline managements' successful efforts through Section 1113 to turn back the clock decades on workers' pay, rights and benefits have far exceeded any legitimate shared economic sacrifices that might have been necessary for the economic survival of the airlines. For example, a typical pilot at United Airlines endured two rounds of concessions that included a 30 percent pay cut, a second pay cut of 12 percent, harsher work rules, less job

security, and a terminated pension plan. In 2007, that pilot has so far received only a 1.5 percent pay raise and forms of profit-sharing worth only about 0.5 percent of his W-2 earnings. As harsh a reality as that is, imagine that pilot's disbelief and anger upon learning that the airline's CEO received a compensation package last year worth over $40 million dollars. The contrast of many unionized airline employees losing more than a third of their pay, work rules, and decades-old pension benefits, while outrageous executive compensation and benefits programs are approved for top airline managers, is enough to show that the current Section 1113 process is unbalanced and grossly abused.

Similar horror stories exist among the thousands of pilots flying in the US Airways family of airlines, as managers there departed the scene with golden parachutes, leaving behind employees who now struggle mightily to take care of their families while delivering millions of their passengers safely day after day. Distressing tales of employee suffering wrought by the 1113 process are also told by pilots and other workers at Northwest, Delta, Comair and Mesaba.

As the Subcommittee knows, the Section 1113 procedures are the mechanism by which employers can seek judicial permission to reject and thereby breach collectively-bargained obligations to their employees, and impose in their place dictated pay and working conditions. This Section 1113 process was originally intended to prevent employers from using the Chapter 11 process as an "escape hatch" to simply wipe away with a bankruptcy filing the binding, long and hard-fought pay and working condition achievements of workers secured by their collective bargaining agreements.

Prior to its enactment, in 1984 the Supreme Court ruled in the Bildisco case that an employer could walk away from binding collective bargaining agreements after a bankruptcy

filing without first making any showing of necessity as to the need to reject the terms of the agreement. In response, the Congress, at the urging of ALPA and other unions, acted swiftly to establish procedures that sought to protect the rights of employees in bankruptcy to prevent such results. The so-called 1113 process was inserted into the bankruptcy code to require a showing of justification and good-faith bargaining between labor and management in order to obtain needed concessions. Failing such a consensual agreement, a company could impose dictated terms and conditions on its employees after court process only if those concessions were determined by the court to be truly necessary to its survival.

Since that time, the employee protective purpose of Section 1113 has been turned on its head by the bankruptcy courts and subverted by employers to achieve precisely the contract-destroying, worker-bashing results that Congress originally sought to prevent. ALPA has seen the requirements of Section 1113 repeatedly ignored or misapplied, without due regard for the financial security interests of airline employees and their families. The most extreme examples of the one-sided nature of the current process are in recent court decisions which allow management to reject binding collective bargaining agreements and impose working conditions, while prohibiting employees from withdrawing their services under those agreements, as other parties facing such rejection are routinely allowed to do under bankruptcy law. Corrective legislation is urgently needed to restore the original intent and purpose of these Section 1113 provisions, and to restore balance and basic fairness to the bankruptcy process as it impacts honest workers called upon to sacrifice to help save their employers.

ALPA believes that Congress must act to overhaul the Section 1113 process by: (1) tightening the standards governing when management can reject their contractual obligations to

workers, so that a breach of a collective bargaining agreement can be permitted only when truly necessary, and only to provide the employer with no more than is truly necessary to ensure the competitive survival of the business; (2) ensuring fair treatment and equitable sacrifices from ***both*** executives and workers in the bankruptcy process so as to prevent further outrageous abuse by corporate officers lining their own pockets while their employees disproportionally sacrifice to help save the company; and (3) making it clear that employees have the right to strike in response to a breach of their collective bargaining agreements if a consensual agreement between the parties cannot be reached. This clarification is desperately needed to restore balance to the 1113 process and to help foster superior, mutually acceptable labor-management solutions to bankruptcy crises through collective bargaining.

All of these changes are urgently needed to restore some semblance of a level playing field in collective bargaining between workers and management, and to deter employers from ever again using the bankruptcy process as the vehicle for widespread and unjustified abuse of workers. I will now describe a number of additional examples which show what has gone wrong with the current administration of the 1113 process, both in the corporate boardrooms and in the courts, and illustrate why such legislation is so urgently needed to correct the employer abuse which has flourished unchecked in the current environment.

I. The Bankruptcy Courts Have Allowed Employers To Use The Section 1113 Process As Leverage To Gut Labor Contracts Without Requiring Employers To Show That The Concessions Are Necessary Or Fair.

The courts, egged on by opportunistic employers, have progressively undermined the "necessity" standard for granting employer relief in Section 1113. As I have alluded to, this standard is supposed to allow only those changes in working conditions that are truly "necessary to permit the reorganization" of the employer. In practice, these limits have all but been ignored by both employers and the bankruptcy courts, which in many cases have used the bankruptcy process as leverage to simply jam draconian wage and benefit cuts down employees' throats. These scorched-earth tactics of using the 1113 procedures to force extraction of concessions that are not truly necessary or otherwise achievable in consensual bargaining have led to widespread tension and resentment among employees, creating lasting damage to labor relations.

ALPA's experience has shown that circumstances where consensual solutions have been reached by the parties have led to far superior outcomes for airlines, their pilots and the flying public. Congress needs to take steps to restore support for consensual negotiations in such circumstances. Both employers and the bankruptcy courts need to be reined in to ensure that the numerous recent abuses of the 1113 process are never repeated.

It gets worse: we have seen profitable airlines use Section 1113 as a bargaining lever to wrest employee concessions to either facilitate a sale or other transaction or just to improve the competitive position or profitability of the carrier. In the case of the bankruptcy of Hawaiian Airlines, pilots faced a Section 1113 motion by a *profitable* company after having made pre-petition concessions demanded to avoid a Chapter 11 filing. All this after management approved a self-tender of the airline's stock at a substantial premium to market value *following* September

11 and *before* the bankruptcy filing. This scheme by Hawaiian was an outrageous abuse of the process.

In the case of Delta Airlines, even after many months of litigation before the bankruptcy court, management continued to demand extreme concessions. Only after the establishment of a special neutral arbitration tribunal, which took the matter out of the hands of the bankruptcy court, did management finally reduce its demands and, in response to ALPA's demands, offer the pilots a bankruptcy claim in exchange for substantial concessions. After a consensual agreement was reached on this basis, the Company completed its successful reorganization and returned to profitability. I would note legislative reforms should build off this success and allow consensual use of such expert arbitration panels versed in the industry as an alternative to court proceedings in 1113.

In the Comair bankruptcy, pilots were forced into Section 1113 litigation because the operation was simply deemed *not profitable enough* to its corporate parent, Delta, while at the same time Delta proclaimed that it had plenty of money on hand as a justification to creditors for fighting a hostile takeover attempt by America West/US Airways.

Additionally, testimony at the hearings on Comair's Section 1113 motion established that the Company's demands for a 22% pay cut would qualify some full-time pilots for federal welfare assistance. In response to testimony from a pilot whose family would qualify for federal food stamps were he to work full-time under the Company's demands, the bankruptcy judge indicated that he would not be persuaded by these facts of employee hardship and suffering, because he viewed the issue purely in economic terms. In fact, in his decision granting Comair's Section 1113 motion, the judge failed to take into consideration the impact the Company's 1113

proposal would have on the pilot group and its families. A concessionary agreement was only reached after the airline effectively moderated its demands by offering the pilots meaningful "upside" benefits. This case alone cries out for legislative remedy.

In the case of Mesaba Aviation, the bankruptcy court approved as "necessary" a wage cut of almost 20% that would have lasted for 6 years, within a structure that did not envision any reversal or mitigation of the cuts during that lengthy period. After the district court agreed with ALPA that such overreaching amounted to bad-faith conduct and an abuse of the bargaining process, and subsequent consensual negotiations, the Company finally agreed to a contract that, while definitely concessionary, provided a significantly smaller pay cut but did not prevent the Company from successfully reorganizing under a plan that is expected to provide close to a 100% recovery for all creditors.

All of these circumstances, taken together, show beyond doubt that the current 1113 process, which does not impose effective limits on the "necessity" of employer concession demands, is open to employer abuse and grants inappropriate leverage for employers to wrest unwarranted concessions from employees. These examples also show that consensual solutions to financial crises are always superior to the imposed alternatives. The current 1113 process undermines consensual, legitimate solutions to financial crises. Necessary modifications to that process must correct these imbalances and support superior consensual solutions.

Reforms are also needed to ensure that an employer would not be permitted to commence the 1113 process seeking court permission to reject a collective bargaining agreement unless there has been good-faith bargaining over proposed modifications to the agreement for a reasonable period of time and the parties reach impasse. Reforms should also include setting

specific limits on the scope of labor cost relief that can be sought by an employer, including requiring clearly expressed financial contributions that would be asked of employees to help the carrier exit bankruptcy, which would not be permitted to extend more than a short time period following successful exit of the employer from bankruptcy. Such a provision would help prevent the abuse of employers "locking in" long-term drastic concessions which continue long after the exit of bankruptcy, as has been the case at United, Northwest, US Airways, Delta, Comair and Mesaba. Reforms should also require the court to consider whether alternative proposals for relief from the union would be sufficient to permit successful reorganization. Additionally, the bankruptcy court should be required to consider the effect of the proposed cuts on the workforce, the employer's ability to retain a qualified workforce and the effect of a strike in the event the collective bargaining agreement is allowed to be rejected. All of these changes are necessary to ensure that the sacrifices that are extracted from employees are truly fair, reasonable and necessary, and to stem employer abuse of the current administration of the 1113 process.

II. The Current Double Standard Under Chapter 11: Deep Sacrifice For Workers, Huge Payouts For Those At The Top.

Modifications should require that the economic relief sought from employees not be disproportionate to the treatment of executives and other groups. These changes are urgently needed to restore basic fairness and credibility to the 1113 process. The current system has led to outrageous unfairness, with workers absorbing huge, long-term cuts in pay, work rules, and retirement benefits while management executives have enjoyed huge payouts which appear to be nothing more than rewards that are directly tied to the level of pain they have inflicted on the employees. For example:

- Pilots at United Airlines, who took concessions of 40% or more in pay, lost numerous important work rules, had their defined benefit pension plan terminated in multiple rounds of Section 1113 litigation, and were locked into a nearly seven-year deeply concessionary agreement, saw the injustice of the United Board raising the pay of Chief Executive Glenn Tilton 40% just months later. This staggering increase is on top of stock grants to Mr. Tilton and other United executives worth in excess of $20 million, as well as stock options worth millions more, made as part of United's plan of reorganization.

- Northwest Airlines' pilots were also forced to accept huge wage cuts of nearly 40%, as well as accept numerous rollbacks to their quality of life by losing key protective working conditions. By contrast, the CEO was rewarded with $1.6 million in salary and bonus payments last year. The revelation that he will also be rewarded with more than $26 million in stock-related compensation over the next few years under a court-approved management equity plan further demonstrates the basic unfairness and abuse of the 1113 process.

We urge reforms that would include a requirement that compensation to be paid to officers and directors be subject to oversight for reasonableness by the court as part of the employer's emergence from bankruptcy. Under current law, executive compensation is only required to be disclosed in the reorganization plan but is not subject to court review. The courts should be required to ensure that executive compensation is reasonable and not disproportionate in light of the other concessions made by other groups during bankruptcy.

Reforms are also needed to require the court to impose an adverse presumption against granting employee relief if the employer has implemented an executive compensation program either during bankruptcy or within six months prior to bankruptcy. If such a program has been implemented, a presumption should be created that the employer has not met the requirement that the proposed cuts not overly burden the affected employee group. These changes are urgently needed to stop any future court-assisted looting of employees by greedy executives of the type that has already occurred.

III. More Unfairness: Deep Concessions Are Extracted From Employees, While Other Stakeholders Suffer Few Or No Adverse Consequences.

Legislative reforms are also needed because employees have also suffered extreme unfairness at the hands of the 1113 process compared to other stakeholders and participants in the bankruptcy process. For example:

- Pilots at Hawaiian Airlines faced demands for concessions despite a plan of reorganization that paid unsecured creditors in full.
- Professional advisors, banks, economic experts, financial managers and executives who participate in the Section 1113 process on behalf of airlines do not share in the sacrifices. Instead they earn lucrative fees and even "success" bonuses with the approval of the bankruptcy court, while the workers' pay, work rules and pensions are allowed to be gutted.

Reforms should require the bankruptcy court to conclude, before it can allow an employer to reject a collective bargaining agreement, that the economic relief sought from employees is not disproportionate to the treatment of other stakeholder groups. This is not the case today, and it is a basic flaw of the current system that needs urgent correction.

IV. Even More Unfairness: Airlines Use Section 1113 To Avoid Binding Obligations To Employees, But Have Convinced Some Courts That The Bankruptcy Laws Immunize Them From Facing Any Employee Self-Help In Response.

The last item that I wish to bring to the Subcommittee's attention is what I perceive to be the most egregious of the many aspects of unfairness that exists in the current administration of the Section 1113 system that I have highlighted today. As I have explained, airlines have used the Section 1113 process as leverage to obtain what they could never obtain in consensual bargaining – deep, lasting and unfair changes to avoid the binding commitments that they made to their employees in collective bargaining agreements, but that has not been enough for them. They have gone to the bankruptcy and federal courts and asked them to declare that airline

employees do not have the right to respond to these unilateral, fundamental breaches of their collective bargaining agreements by withholding services, as common sense, fairness and the basic tenets of labor law would seem to dictate. In fact, two bankruptcy courts, a federal district court, and the Second Circuit Court of Appeals have ruled that airline employees can be forced to accept the utter destruction of their fundamental rates of pay and working conditions in collective bargaining agreements, but may not strike in response. This approach, of course, leaves employees chained to the railroad tracks as the 1113 Express bears down on them. Airline employees are being singled out unfairly by being denied the right to withhold services under a labor contract after it is rejected, which is a right that every other party to a rejected contract has under the current bankruptcy code. In fact, a split panel of the Second Circuit could only justify this highly inequitable result with the fiction that management is not actually breaching a collective bargaining agreement when it obtains judicial permission to reject a labor contract through the Section 1113 process, a notion wholly at odds with settled bankruptcy doctrine.

The willingness of the courts to enjoin a strike in response to management imposition of unilateral terms under Section 1113 has taken away any incentive for airlines to negotiate rather than dictate terms in bankruptcy. Airline employees have a right under the Railway Labor Act to strike after a bankruptcy court grants a motion to reject a collective bargaining agreement under Section 1113 and management imposes new inferior rates of pay, benefits, job security and/or working conditions. We believe that under the Norris–LaGuardia Act (which was enacted in the 1930's to generally preclude injunctions against strikes) bankruptcy judges and U.S. District Court judges do not have jurisdiction to issue injunctions against such strike activity when

management has acted unilaterally to change the status quo and tear up a binding labor contract outside of the negotiations process.

It is essential that any reform legislation explicitly preserve the right of airline employees to strike after a Section 1113 contract rejection, and our proposal does that. If the rule were otherwise, as some courts have concluded, management would be allowed to impose conditions without having to face the prospect of a strike. Such blatant inequality allows management free reign to impose conditions without any check on the kind of overreach and abuse that has occurred to date. Legislation is needed to restore the economic balance contemplated in the anti-strike injunction mandates of Congress in the Norris-LaGuardia Act, which the Supreme Court found "was designed primarily to protect working men in the exercise of organized, economic power, which is vital to collective bargaining." Balance will be restored and management will be forced to act responsibly and fairly in bankruptcy towards its employees ***only if*** it is faced with the real possibility of a responsive strike.

In sum, while ALPA recognizes that substantial economic sacrifices may be necessary by employees during severe economic disturbances, and in fact has repeatedly acted in a leadership role to help many airlines survive the ravages of the post 9-11 environment, management and the courts have moved the 1113 process far from its original intent to protect workers. Today, it is an extreme and one-sided process that is used to destroy workers' lives. ALPA believes that corrective legislation is urgently needed to fix the misinterpretation and abuse of the 1113 process that has snowballed in the last five years. The Congress must act to restore the original intent of this legislation and protect employees from unfair, dictated sacrifices made while the corporate chieftans reap huge payoffs.

Madame Chairwoman, I appreciate the opportunity to testify here today, and I would be happy to answer any questions you have.