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In re:	Chapter 11
AMR CORPORATION, *et al.*,	Case No. 11-15463 (SHL)
Debtors.	(Jointly Administered)

OBJECTION OF THE TRANSPORT WORKERS UNION OF AMERICA, AFL-CIO TO THE MOTION OF DEBTORS FOR ENTRY OF ORDER PURSUANT TO 11 U.S.C. § 1113 AUTHORIZING DEBTORS TO REJECT COLLECTIVE BARGAINING AGREEMENTS

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The Transport Workers Union of America, AFL-CIO (the "**TWU**") submits this brief in opposition to the Motion (the "**Motion**") of American Airlines, Inc. ("**American**" or the "**Company**"), one of the above-captioned debtors (collectively, the "**Debtors**"), to reject its collective bargaining agreements pursuant to 11 U.S.C. § 1113(c).

PRELIMINARY STATEMENT

American's Motion to reject its seven collective bargaining agreements with the TWU ("**TWU CBAs**") should be denied because the Company failed to satisfy the strict procedural and substantive requirements of section 1113(c) of title 11 of the United States Code (the "**Bankruptcy Code**").

The imposition of draconian modifications to the TWU CBAs that will result in the loss of nearly 9,000 TWU jobs and a sub-standard collective bargaining agreement is so excessive as to be unconscionable. The modifications clearly are not "necessary modifications. . . that are necessary to permit the reorganization" of American as required by section 1113(b)(1) (A).

American seeks $1.25 billion in average annual cost savings over a six year period from all labor groups. Of the purported cost savings, $390 million will be imposed on the TWU workforce through a combination of measures that would decimate the workforce and, for those fortunate enough to remain employed, significantly reduce healthcare and other benefits and drive overall compensation levels to the lowest in the industry. American seeks these excessive concessions without need as it failed to first fully explore all of its restructuring options, including consolidation or merger. The Debtors' proposed financial targets are premised on a faulty stand-alone business plan model that ignores the consolidation that has taken place in the industry over the past decade. Indeed, the Debtors and their financial advisors acknowledge that they must consider consolidation, yet they premise their excessive labor modifications on a dead

on arrival stand-alone business model.[1] It is inconceivable that American would seek to impose destructive, draconian "cost-savings" on its employee groups without first exploring all of its available options. Instead, American seeks to reduce labor costs below the level needed to merge or consolidate, which has the result of giving the benefit of any synergies or upside created by any consolidation or merger to its non-labor stakeholders. Thus, beyond being unnecessary, the proposals do not treat the TWU and other labor groups fairly or equitably.

Furthermore, the Debtors' contention that it is necessary to obtain $1.25 billion in labor cost savings to establish a profitable, competitive, and sustainable business is not supported by the evidence. In fact, the Debtors' own investment banker acknowledges that it did not analyze alternative targets before opining that the Debtors' labor cost savings targets supplied by the Debtors were necessary to achieve the earning targets selected by American's management. Instead, the investment banker simply relied on the Debtors' business model revenue, earnings and other targets and concluded that massive labor costs savings were necessary to achieve them.

The Company's assertions that the proposed modifications to the TWU CBAs are necessary to achieve a competitive cost structure are also not supported by the record and are, in fact, objectively false. Although the Debtors' labor cost expert from F&H Solutions cherry-picks a few provisions from certain of the TWU CBAs and argues that they are not industry norm, neither he nor any other witness offered by American has presented evidence establishing that, on a whole, the existing TWU CBAs are above industry averages. The Debtors' expert conveniently ignores the fact that pay rates of the largest TWU-represented workgroup (consisting of approximately 11,500 mechanics and related employees) are the lowest among

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[1]The Committee has stated that it supports the Motion but it has not endorsed the business plan upon which the section 1113 proposals were made and made clear in the section 1113 scheduling order and on the record during the section 1113 hearing that nothing in the section 1113 hearing record will have a preclusive effect on other aspects of this case.

American's competitors. Since pay rates drive 75% of total compensation, this is a serious omission. Moreover, the Debtors failed to present any evidence that the proposed modifications leave those TWU workers who remain employed with industry competitive wages, benefits and work rules when viewed in their entirety. To the contrary, the proposed changes would leave TWU-represented workers at American, not with competitive contracts, but with contracts at the lowest end among its peers. Therefore, the proposed modifications are not necessary, as suggested by the Debtors, to achieve a competitive cost structure.

Assuming, *arguendo*, that $390 million in cost savings from the TWU are somehow necessary, the modifications proposed by American are not necessary to achieve that goal. Viable alternatives exist that could achieve sustainable cost savings in the range sought by the Company without terminating nearly 9,000 members of the TWU workforce. The Company, however, rejected these proposals. In addition, the Company has significantly understated the value of certain of its alleged cost savings measures. This effectively means that the Company is seeking concessions with a value far greater than $390 million. Therefore, assuming the Company's target of $390 million is somehow necessary, the modifications it proposes exceed that amount and, therefore, are not necessary.

Rejection of the TWU CBAs is also prohibited because the concessions sought from the TWU are not fair and equitable as required by section 1113(b)(1) of the Bankruptcy Code.

In addition, (i) the TWU has good cause to reject American's proposals and (ii) the balance of the equities clearly does not favor rejection of the TWU CBAs. Accordingly, the Debtors have failed to meet their burden of satisfying section 1113(c)(2) and (3) of the Bankruptcy Code and, therefore, the Motion must be denied.

STATEMENT OF THE FACTS[2]

The TWU and the Employees It Represents

The TWU represents approximately 23,500 employees at American, or nearly 40% of the workforce. The TWU is the largest bargaining unit at American. TWU-represented employees work in seven crafts or classes: (i) Maintenance & Related Employees ("**M&R**"); (ii) Fleet Service Employees and Ground Service Employees ("**Fleet**"); (iii) Stock Clerk and Crew Chief Stock Clerk Employees ("**Stock Clerks**"); (iv) Maintenance Control Technicians ("**MCT**"); (v) Ground School Flight Engineer Simulator and Pilot Simulator Instructors ("**Instructors**"); (v) (vi) Flight Dispatchers and Dispatcher's Assistants ("**Dispatch**"); and (vii) Flight Simulator Technicians, Associate Simulator Technicians and Technical Coordinators ("**Sim Techs**"). There are approximately 11,500 M&R employees, 10,200 Fleet employees, 1305 Stock Clerks, 175 Dispatchers, 170 Instructors, 87 MCTs, and 76 Sim Techs. The terms and conditions of employment for each employee craft or class are governed by separate collective bargaining agreements between American and the TWU. *See* AA Exhibits 1103-1111.

The TWU has a long history of representing workers at American going back as far as the 1940's. Over the past 60 plus years of representing members at American, the TWU made great strides in balancing the goal of good quality jobs while understanding the Company's need to be profitable. The TWU is well aware that a labor agreement must be a living document that evolves over time and that during negotiations the constantly changing business environment

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[2] Unless otherwise stated, the facts contained in this Statement of the Facts are drawn from the *Declaration of Donald M. Videtich In Opposition to the Motion of the Debtors for Entry of an Order Pursuant to 11 U.S.C. § 1113 Authorizing the Debtors to Reject the Collective Bargaining Agreements with the Transport Workers Union of America, AFL-CIO* (hereinafter the "**Videtich Decl. at** ¶___"); the *Declaration of Timothy J. Gillespie in Opposition to the Motion of the Debtors for Entry of an Order Pursuant to 11 U.S.C. § 1113 Authorizing the Debtors to Reject the Collective Bargaining Agreements with the Transport Workers Union of America, AFL-CIO* (hereinafter the "**Gillespie Decl. at** ¶___"); and the *Declaration of Thomas R. Roth In Opposition to the Motion of to Reject Collective Bargaining Agreements Covering Employees Represented by the Transport Workers Union of America, AFL-CIO Pursuant to 11 U.S.C. Section 1113(c)* (hereinafter the "**Roth Decl. at** ¶___").

should be taken into consideration. While no agreement is perfect, the TWU membership reached agreements that helped build American into the largest airline in the world.

The men and women represented by the TWU are and will continue to be on the front lines for American every day. In the past, the TWU has been mindful of American's financial situation and made decisions and created opportunities based on the belief that a healthy, financially viable company is the best solution for everyone, including its members and their families in the long run. However, after decades of hard work attempting to build an environment of mutual respect and understanding, the Debtors' bankruptcy filing seeks to undo all that has been built by honest, hard working employees.

In contrast to the financial creditors in these chapter 11 cases, for whom American is just another investment in their portfolio, American is the life-blood of the TWU-represented employees. The hardships that the Company is seeking to impose on TWU-represented employees through the section 1113 process will cause severe and irreparable harm to the well-being of the employees and their families and dependents, who depend on American not just for their wages, but also for health insurance, retirement, community and security. The vast majority of the TWU-represented employees dedicated twenty years of service (or more) to American. In recognition of their long and dedicated service, American proposes to terminate 9,000 of these employees in pursuit of an absurd business plan that is not viable on its face. Labor unrest is the only thing assured by American's business plan.

The TWU members are not wealthy. They are not the highest paid in the industry in their respective crafts. The average take home pay for a TWU-represented employee, adjusted for inflation, is below what it was over ten years ago. While the TWU membership is dedicated and loyal, nothing in the Bankruptcy Code or any other federal statute mandates the use of a debtor's

workforce as a bargaining chip. If, as it appears, it is inevitable that the Debtors will eventually merge with another airline, the TWU should not be required to make vast concessions now for the benefit of other stakeholders who will benefit in the future from the concessions.

The TWU-represented employees understand the concept of sacrifice and proved that by accepting $620 million in concessions in 2003. But the men and women represented by the TWU know the difference between fairly sharing sacrifices and being "filleted" to provide a better opportunity for other constituents. They do not deserve to be the proverbial ox that is gored.

The TWU continues to focus on making the right business decisions that support a healthier airline *and* its members' interests. However, the TWU will not let its members and their families unduly bear an unfair burden or sit on the curb while American marches in pursuit of a business plan that is neither viable on its face nor equitable in the disproportionate sacrifice it seeks from labor.

History of Pre-Bankruptcy Events and Negotiations

In 2001, the TWU was in negotiations and sent out certain tentative agreements for ratification by its members when the tragic events of 9/11 occurred. TWU members ratified the agreements but knew that difficult economic times were ahead. American, along with every other airline, experienced a sharp decline in passengers. The industry was in uncharted territory and the TWU worked hard to find solutions to cut costs. In October 2001, as the demand for flying decreased, aircraft were parked, and lower utilization of aircraft drove less need for maintenance, American began the lay off of maintenance and engineering staff in record numbers. To mitigate job loss and better position American for quick resumption of higher service levels, the TWU increased its efforts to work more productively.

During this time, distrust of management grew among both organized and unorganized labor groups because, while labor and support staff were being laid off in record numbers, direct and indirect management did not share in similar headcount reductions.

By mid-2002, passenger traffic started to improve. Some TWU-represented employee recalls were initiated in certain locations and aircraft were reactivated. Revenue, however, did not return to pre-9/11 levels and airlines trying to recover losses and win traffic back lowered airfares to unprofitable levels. By the end of 2002 it was clear that, after burning through cash reserves, mortgaging assets to unprecedented levels, and failing to adapt their business models fast enough, drastic structural changes were on the horizon for the airline industry.

In early 2003, at the request of American's management, and in response to the deteriorating financial condition of the Company, each of the seven TWU workgroups entered into new collective bargaining agreements (collectively, the "**2003 CBAs**") as part of the Company's out-of-court restructuring. The 2003 CBAs resulted in approximately $620 million in aggregate annual labor concessions from TWU-represented employees and an immediate layoff of approximately 1,300 M&R employees alone. Since 2003, the M&R work force alone has been reduced dramatically from approximately 16,000 to 11,500 employees.

The M&R group contributed approximately $315 million in concessions as part of the 2003 restructuring, including a staggering 17.5% reduction in base wage rates and another approximately 10% in various vacation, sick leave and other benefit concessions. Similarly, the Fleet service employees, who combined with M&R employees, represent nearly 95% percent of TWU-represented employees at American, contributed approximately $300 million in concessions, including a 16% reduction in base wage rates and similar cuts in benefits. These drastic changes, contrary to the assertions of the Company, have placed M&R and other TWU-

represented employees at the bottom end of the overall compensation scale compared to similar employees at American's competitors.

After the TWU ratified the 2003 CBAs and made extraordinary sacrifices to save the Company, it was revealed that at the same time that the Company was asking TWU for drastic concessions to avoid bankruptcy, senior management established a Supplemental Executive Retirement Plan for then chief executive officer, Donald Carty, and forty-four other executives to protect their retirement funds in the event of a bankruptcy filing.

Moreover, contrary to representations made during the negotiations leading up to the 2003 CBAs, the TWU learned that senior management did not reduce their wages and other benefits to the same degree as the TWU and other unions. For example, while the TWU agreed to wage reductions of up to 17.5%, management compensation was reduced only 6-8%, and while TWU-represented employees agreed to reduce holidays from 10 days to 5 days, management's holidays remained at 10 days. Thus, while the TWU recognized - as it does now and always has - the need for fair, equitable and shared sacrifice and honest negotiations, the Company's senior management did not.

Notwithstanding the distrust and tension created by the actions of the Company's management, the TWU understood the need to improve efficiency and productivity. By way of example, the TWU participated in collaborative labor/management efforts as part of the Company's Performance Leadership Initiative ("**PLI**") that was established in 2005. As part of the PLI, a Maintenance Task Team ("**MTT**") of approximately 25 frontline TWU and management employees was formed. Working with the Boston Consulting Group, the MTT determined, among other things, that approximately $170 million in annual maintenance related cost savings could be achieved if the Company improved training and implemented other

improved business procedures. No layoffs were needed to achieve these savings. The Company, however, chose not to implement the key drivers of these cost savings.

Notwithstanding management's decision to reject significant cost savings proposals (while at the same time accepting hundreds of millions of dollars in bonuses as described below), M&R employees recognized the need to improve efficiencies and implemented numerous cost savings initiatives that have resulted in more than $1 billion in added value since 2004. Among these initiatives is the implementation of a new method for performing "C" checks (a type of overhaul maintenance function) on MD80 aircraft at the Company's Tulsa Maintenance Base. This improvement reduced the number of aircraft maintenance technicians ("**AMTs**") necessary to perform the overhaul from approximately 770 to approximately 350. This and other efforts at the Tulsa Maintenance Base resulted in added value totaling $500 million.

In addition, starting in 2007, the M&R group at Alliance Fort Worth Overhaul Base ("**AFW**") set and reached a goal of $300 million in added value through procedures designed to improve the deployment of workers and parts. These groundbreaking procedures at AFW allowed the Company to add an entire line of new aircraft modification work without adding any new maintenance or other staff. At the Kansas City Maintenance Base ("**MCIE**"), employees contributed another $150 million in value creation. These are just a few of the many initiatives that TWU-represented employees have taken to dramatically improve the efficiency of American's maintenance operations since 2003.

In or about August 2007, the TWU exercised early open provisions of the 2003 CBAs (each of which was amendable as of April 15, 2008) and the parties engaged in bargaining sessions pursuant to section 6 of the Railway Labor Act on various dates between November 2007 and 2009. These negotiations were conducted in a difficult negotiating environment,

especially after American paid approximately $200 million in Performance Share Unit Plan payouts to hundreds of executives in 2006 and subsequent years, while TWU employees were still living under the terms of the deeply concessionary 2003 CBAs. During the Section 6 negotiations American offered proposals to the TWU that would increase the non-competitive wage rates and related improvements in exchange for certain modifications to work rules and retirement benefits.

When negotiations did not lead to agreements, the TWU sought mediation with respect to the M&R, Stock Clerks and MCT groups and the TWU and American jointly sought mediation through the National Mediation Board pursuant to section 5 of the Railway Labor Act, 45 U.S.C. §§ 151 *et seq*. ("**RLA**"), with respect to the Fleet, Dispatch, Instructors and Sim Techs groups. Various mediation sessions took place with respect to each group between October 2008 and July 2011. Those negotiations resulted in a new collective bargaining agreement with (i) the MCT group which became effective May 5, 2010 and (ii) the Instructors which became effective October 1, 2011.

In 2010 and 2011, the TWU also reached tentative agreements ("**TAs**"), which were subject to ratification by the membership of each TWU group, with respect to M&R, Stock Clerks, Fleet (on two occasions), Dispatchers and Sim Techs. None of those TAs became effective.

The negotiations leading up to the TAs concerned mainly pay increases, improvements to vacation, holiday and sick leave and concessions related to retirement benefits (moving from a defined benefit pension plan to a 401(k) plan for new hires), retiree medical benefits, and certain work rules).

Post-Petition Negotiations

On November 29, 2011 (the "**Petition Date**"), the Company filed for bankruptcy and the TWU was told that the Company was going to make proposals for modifications to the CBAs in the future.

The nature and extent of the Company's proposals were not disclosed until February 1, 2012, when American presented its new business plan (which it labels Plan For Success) and term sheets containing proposed modifications to the TWU CBAs (the "**February Term Sheets**"). Copies of the February Term Sheets are marked as AA Exhibits 1126-1129 and 1202 -1204.

During the initial informational session at which the February Terms Sheets were provided, American informed TWU representatives that it was seeking average annual savings over the six year life of its business plan of $1.25 billion from all labor groups combined. The Company explained that its proposals to all labor groups sought 20% reductions of each group's respective labor costs.

Using this allocation methodology, the Company seeks average annual cost savings of $390 million from the TWU work groups over the next six years. In particular, the Company seeks cost savings of approximately $212 million from M&R, $150 million from Fleet, $20 million from Stock Clerks, $3.4 million from MCT, $3.2 million form Dispatch, $2.1 million from Instructors and $750,000 from Sim Techs. *See* AA Exhibits 1140-1143, 1205 -1207 and 1212-1214. The Company informed the TWU that it would not move off the $390 million "ask" - and it has not done so to date.

The labor cost savings that the Debtors seek are premised on its existing stand-alone "Cornerstone" business strategy, which has long proven unworkable. In particular, to arrive at the aggregate target cost savings number for labor, the Debtors' management first identified

anticipated revenue improvements and non-labor cost savings and then targeted a projected level of profitability and a projected EBITDAR margin of ███. In order to achieve these metrics, American simply plugged in a labor cost savings that would yield the desired result. It then allocated the cost savings measures by asking each labor group to reduce its percentage of the Company's overall labor costs by 20%, which in the case of the TWU groups as a whole, approximates $390 million.

American seeks these excessive concessions based on a stand-alone business strategy model that ignores the consolidation that has taken place in the industry over the past decade. Indeed, the Debtors and their own investment banker acknowledge that the Debtors have a fiduciary duty to consider consolidation, yet they premise their excessive labor modification proposals on an outdated stand-alone business model without first exploring all its available options, including a merger or consolidation that would require far less labor concessions.

In response to cross examination by the TWU, the Debtors' investment banker testified as follows:

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10 In addition to reviewing the debtor's stand-alone plan
11 is it your expectation that the debtor will be reviewing
12 consolidation, merger, M&A or other options prior to a plan
13 of reorganization?
14 A I think that would be likely because the debtor's
15 obligation is to maximize value for stakeholders, and my
16 sense is, is that the stakeholders would want to insure that
17 they are getting the highest possible value, so they would
18 want the debtor to look at all alternatives to a stand-alone
19 plan before supporting a plan of reorganization based around
20 the stand-alone plan.
21 Q So that would be yes?
22 A That would be yes.
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Transcript of hearing April 25 174:10 to 174:22.[3]

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[3] Citations to the transcript of the hearing on the Motion commencing on April 23, 2102 will hereinafter adhere to the following format: Tr. Apr. ___ Page:Line to Page: Line.

And then again at page 176:

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3 Q I believe you testified that a -- as a debtor you have
4 a fiduciary duty to all of the company's stakeholders,
5 correct?
6 A Yes.
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Tr. Apr. 25 176:3 to 176:6.

In response to cross examination by the TWU of the Debtors' industry expert, he testified as follows:

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5 Q Now, Your Honor -- I'm sorry. Mr. Kasper, Exhibit 30,
6 that shows that both United and Delta have larger networks
7 than American; is that right?
8 A Correct.
9 Q And it compares the size of the networks presently to
10 the size of the networks in 2002, correct?
11 A That's correct.
12 Q And if you look at 2002, American was the biggest one
13 with 263 shares, correct?
14 A Yes.
15 Q And you see that -- that Delta, Northwest, United and
16 -- and Continental, on a stand-alone basis, were all behind
17 American, right?
18 A That's correct.
19 Q But due to mergers, you have United, Continental and
20 Delta now ahead of American, right?
21 A That is correct.
22 Q And I -- I believe that -- that you would agree, would
23 you not, that the Delta and United mergers created bigger
24 networks than exist presently at American, correct?
25 A I would -- I would agree with that.

1 Q And you would agree that those mergers were beneficial
2 to their -- those airlines?
3 A I think so far they've worked out reasonably well for
4 the carriers.

****
14 Q And it's your understanding, is it not, that American
15 will be competing with United and Delta in the future,
16 correct?
17 A With any luck in a successful reorganization.
18 Q And in the -- in the context of that competition, will
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19 -- will it be important for American to increase its
20 network?
21 A I believe it will. Yes.
22 Q And I think you've said on -- on direct that a network
23 carrier likes a larger footprint because it enables the
24 carrier to attract highly valued business customers?
25 A That is correct.
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Tr. Apr. 23 235:5 to 236:25.

The TWU membership should not be compelled to bear the cost of American's experiments or to accept life altering proposals based on a faulty business plan strategy that in all likelihood will not exist in the very near future and was designed for purposes of extracting unnecessary labor concessions that will benefit all other stakeholders at the expense of the TWU and other organized labor groups.

In contrast to the proposals discussed prior to the Debtors' bankruptcy, the proposals contained in the February Term Sheets would have a devastating impact on TWU-represented employees and their families. In fact, the proposals the Company made would eliminate (i) approximately 4,370 jobs, or nearly 40% of the entire M&R workforce; and (ii) approximately 4,200 Fleet jobs, or nearly 40%, of the Fleet workforce. The proposals made to the Stock Clerks would result in the termination of 270, or approximately 20%, of its 1,305 members.

The Company's proposal to allow it to outsource up to 40% of aircraft related maintenance man-hours of work currently performed "in-house," in addition to what is already outsourced, is the most radical proposal that would trigger most of the layoffs of M&R employees. Significantly, while the Company assumes that outsourcing maintenance will result in significant cost savings, it has not provided any data or analysis to support this assumption.

American's own experience with outsourcing aircraft maintenance functions illustrates that outsourcing is not necessarily more efficient or less costly. American previously outsourced

maintenance on 757 aircraft to TIMCO, a large maintenance and repair organization ("**MRO**"). The time it took to perform the maintenance functions (or "turn times") proved to be longer than when performed in-house by TWU M&R personnel. This is extremely significant because the longer the "turn time" the longer the aircraft is out of service and not generating revenue. It does not appear that the Company took these factors into consideration when formulating its proposal.

MROs also do not have effective troubleshooting capability which, like slower "turn times," results in longer downtime for the aircraft. The TWU has sent TWU Technical Crew Chiefs with test pilots who observed American on-site managers themselves attempting to troubleshoot American's airplanes that were sent out for maintenance. Data has shown that the reliability of the aircraft leaving TIMCO is poor.

Other airlines are also learning that lower labor costs at MROs do not necessarily translate to overall lower maintenance costs. For example, Continental is working collaboratively with its mechanics and has one of the lowest maintenance costs in the industry while performing all 737 and most 757 heavy airframe work in-house.

Terminating approximately 9,000 jobs and causing major upheaval in the lives of the employees and their families in the hope of achieving uncertain cost savings is an untenable proposal, especially when credible alternatives exist. The Company could not, and cannot, in good faith expect that the TWU would ever accept such a draconian and unfair proposal.

Another example of the Company's harsh proposals is the modification of the TWU health insurance coverage and the implementation of a plan common to all employees. The TWU already contributes 19% towards member healthcare coverage. The Company's proposal contemplates a diminished medical plan design as well as an increased employee contribution level of 21% of the cost of coverage. Under the proposal set forth in its term sheets, the

Company will offer a 3-option program with family annual deductibles ranging from $900 to $4000 and co-insurance of either 20/80 or 20/70 for in-network services. For the plan with the best coverage, the monthly employee contribution for family subscribers is $460; the lesser plan is $232. For part-time workers, monthly employee contribution for family subscribers would nearly double at $805 per month for the best plan, $406 for the lower plan and $473 for the standard plan. This one-size fits-all approach creates a disproportionate burden on lower paid workers, such as many of those represented by the TWU. The unaffordable cost of healthcare coverage may prevent many employees from participating in the correct health plan for their family's needs or force them to pay an unduly burdensome price in order to maintain coverage. Given the high cost of healthcare, this proposal is intolerable.

Subsequent to the delivery of the February Term Sheets and through March 22, 2012, the date on which American delivered its second round of term sheets to the TWU, each of the seven TWU work groups delivered a series of proposals to American. As reflected in the TWU Proposals, TWU made counterproposals to the February Term Sheets that included acquiescence to several of American's proposals, including certain provisions that would result in some employee reductions and cost savings in the range requested by American. For example, the first counterproposal made on behalf of the M&R group dated February 24, 2012, accepted the Company's proposal to (i) outsource some maintenance work, (ii) outsource Title II High Voltage work at the Tulsa maintenance base, and (iii) outsource other maintenance functions. *See* Videvitch Decl, Exhibit A (M&R Proposal dated February 24, 2012).

In addition to delivering its written proposals, the TWU informed the Company's negotiators that, among other things, the TWU recognized, as it had in the past, the need to make concessions but that proposals designed to eliminate the enormous amount of jobs envisioned by

the Company was not and would not be acceptable in light of the fact that other viable options were available to achieve cost savings without causing upheaval to thousands of families. Moreover, the Company's proposals to reduce vacation, sick leave and other benefits as described in the February Term Sheets are additional examples of excessive and overreaching cost cutting measures. M&R employees are already at the bottom of the industry in pay rates, holidays and sick leave. The Company's attempt to reduce these benefits to even lower levels, while keeping its wages at the bottom of the industry, is outrageous and unfair and the TWU made that clear to the Company during negotiations conducted after receipt of the February Term Sheets.

On March 22, 2012, the Company delivered new term sheets to the TWU (the "**March Term Sheets**"). The March Term Sheets contain the proposals that are attached to and described in the Motion. *See* AA Exhibits 1136-1139 and 1209 -1211.

Notwithstanding the meaningful TWU counterproposals and the serious concerns and objections raised by the TWU, the March Term Sheets did not alter American's fundamental proposals that would lead to mass layoffs and reduce compensation levels to the lowest level among its competitors. Moreover, the Company stuck to its take-it or leave-it approach and did not make any concessions whatsoever with respect to the $390 million aggregate cost savings that it was seeking to extract from the TWU.

In essence, on March 22, 2012, only days before filing its Motion, and after nearly two months of discussions and negotiations, the Company presented the TWU with essentially the same proposals it made on February 1, 2012. This is not a fairly shared sacrifice but a disproportionate labor sacrifice for the benefit of other constituents. The proposals contained in the March Term Sheets and described in the Motion are (i) not reflective of good faith

negotiations, (ii) not necessary, (iii) not fair and equitable and (iv) the TWU has good reasons not to accept them.

ARGUMENT

I. THE DEBTORS FAIL TO SATISFY THE REQUIREMENTS FOR REJECTION UNDER 11 U.S.C. § 1113

The Debtors have not met their burden of proving compliance with the statutory requirements of section 1113 of the Bankruptcy Code. Section 1113 of the Bankruptcy Code provides, in pertinent part, as follows:

> (b)(1) Subsequent to filing a petition and prior to filing an application seeking rejection of a collective bargaining agreement, the debtor in possession or trustee (hereinafter in this section "trustee" shall include a debtor in possession), shall --
>
> (A) make a proposal to the authorized representative of the employees covered by such agreement, based on the most complete and reliable information available at the time of such proposal, which provides for those necessary modifications in the employees benefits and protections that are necessary to permit the reorganization of the debtor and assured that all creditors, the debtor and all of the affected parties are treated fairly and equitably; and
>
> (B) provide, subject to subsection (d)(3), the representative of the employees with such relevant information as is necessary to evaluate the proposal.
>
> (2) During the period beginning on the ate of the making of a proposal provided for in paragraph (1) and ending on the date of the hearing provided for in subsection (d)(1), the trustee shall meet, at reasonable times, with the authorized representative to confer in good faith in attempting to reach mutually satisfactory modifications of such agreement.
>
> (c) The court shall approve an application for rejection of a collective bargaining agreement only if the court finds that --
>
> (1) the trustee has, prior to the hearing, made a proposal that fulfills the requirements of subsection (b)(1);

> (2) the authorized representative of the employees has refused to accept such proposal without good cause; and
>
> (3) the balance of the equities clearly favors rejection of such agreement.

Section 1113 "encourages the collective bargaining process as a means of solving a debtor's financial problems insofar as they affect its union employees." *In re Century Brass Prods., Inc.*, 795 F.2d 265, 272 (2d Cir. 1986). "Knowing that it cannot turn down an employer's proposal without good cause gives the union an incentive to compromise on modifications of the collective bargaining agreement, so as to prevent its complete rejection. Because the employer has the burden of proving its proposals are necessary, the union is protected from an employer whose proposals may be offered in bad faith." *In re Maxwell Newspapers, Inc.*, 981 F.2d 85, 90 (2d Cir. 1992) (citations omitted).

Courts in this Circuit have parsed the statutory language into seven elements. *See In re Carey Transp., Inc.*, 50 B.R. 203, 207-213 (Bankr. S.D.N.Y. 1985), *aff'd*, *Truck Driver's Local 807 v. Carey Transp.*, 816 F.2d 82, 90-91 (2d Cir. 1987). These seven elements are:

> (1) The debtor must make a proposal to modify the collective bargaining agreement or obtain concessions from the union, which is based on the most complete and reliable information available at the time the proposal is made. The debtor's failure to supply complete and reliable information is fatal to a motion to modify or terminate a collective bargaining agreement. *See In re Liberty Cab & Limousine Co.*, 194 B.R. 770 (Bankr. E.D. Pa. 1996).
>
> (2) The proposal must be necessary to the debtor's reorganization;
>
> (3) The proposal must treat all creditors, the debtors and all other affected parties fairly and equitably;
>
> (4) The debtor must meet at reasonable times with the union;
>
> (5) The debtor must negotiate in good faith with the union in an attempt to reach mutually satisfactory modifications of the collective bargaining agreement. This factor requires actual

negotiating; a "take it or leave it" bargaining session is not sufficient. *See In re S.A. Mech., Inc.*, 51 B.R. 130, 132 (Bankr. D. Ariz. 1985);

(6) The union has refused to accept the debtor's proposal without good cause. "Where the union makes compromise proposals during the negotiating process that meet its needs while preserving the debtor's savings, its rejection of the debtor's proposal would be with good cause." *In re Maxwell Newspapers*, 981 F.2d 85, 90-91 (2d Cir. 1992);

(7) The balance of the equities clearly favors rejection of the collective bargaining agreement.

The Debtors bear the burden of persuasion by a preponderance of the evidence on the first six elements and must prove the seventh element, that balancing the equities *clearly* favors the requested relief, by a standard greater than a preponderance of the evidence. *See In re Walway*, 69 B.R. 972, 974 n.18 (Bankr. E.D. Mich. 1987) (holding that the word "clearly" in the final factor indicates a higher standard of proof is required). The Debtors bear the burden of proof and must satisfy all seven of these elements for relief pursuant to Bankruptcy Code section 1113. *See United Food and Commercial Workers Union, Local 211 v. Family Snacks, Inc. (In re Family Snacks, Inc.)*, 257 B.R. 884, 892 (8th Cir. BAP 2001). If the Debtors fail to meet the burden on even one element, the Motion must be denied.

The nature and extent of the modifications proposed by the Debtors exceed those that are necessary to permit the Debtors to successfully reorganize. Furthermore, the Debtors have failed to negotiate in good faith. In addition, the TWU has good cause to refuse to accept the Debtors' proposals, and the balance of the equities clearly does not support the proposed modifications. Simply put, the Debtors fail to meet their burden of proof under section 1113. Therefore, the Motion must be denied.

A. The 1113 Proposals Are Not Necessary Modifications That Are Necessary To Permit A Successful Reorganization

Section 1113 requires that a debtor propose only those modifications that are "necessary" to permit its reorganization. The necessity inquiry is fact-sensitive and "the impetus of small or subtle changes in the circumstances may alter [the Court's] perspective and conclusions. Every fact and circumstance is relative to some unspecified and undefinable benchmark in the context of what is necessary . . ." *In re Delta Air Lines*, 342 B.R. 685, 691 (Bankr. S.D.N.Y. 2006). As recognized for over twenty-five years,

> "There can be no pat formula. Any analysis must be undertaken on a case by case basis with due consideration given to the nature of the business and industry patterns. In this way provisions dealing with wages and benefits that have a disproportionate impact on the debtor's business can be selectively addressed without the need for wholesale revision of every provision developed in prior bargaining. In other words, the § 1113 process is designed to encourage selective, *necessary* contract modification rather than a total elimination of all provisions in the collective bargaining agreement. Complete *de novo* negotiations would be wasteful and counterproductive."

Carey, 50 B.R. 203, 209 (Bankr. S.D.N.Y.), *aff'd*, 816 F.2d 82 (1985) (emphasis in original).

Necessity is a relative concept that is denominated in degrees and must be determined in reference to a particular outcome. A provision may be necessary in the sense that it is absolutely required for a company to survive and successfully restructure. The Second Circuit has found that definition to be too restrictive. On the other hand, a debtor may not use a claim of necessity "as a medicine to rid themselves of corporate indigestion." *In re Century Brass Prods., Inc.*, 795 F.2d 265, 272 (2d Cir. 1986). The less actually necessary a proposal is, the more a debtors' insistence on it calls the debtor's good faith into question. *In re Maxwell*, 981 F.2d at 90-91 ("Because the employer has the burden of proving its proposals are necessary, the union is protected from an employer whose proposals may be offered in bad faith." (citation omitted)). If

it is more likely than not that a debtor can successfully reorganize without the requested modifications to the collective bargaining agreements, then the debtor has not met its burden for rejection of those agreements.

Moreover, it is not sufficient for the Debtors to show that, as a general matter, some changes are necessary. The Debtors must show by a preponderance of the evidence that the entire proposal, taken as a whole, is necessary. *In re Royal Composing Room, Inc*., 848 F.2d 345, 348 (2d Cir.1988). Where, as here, a proposal, taken as a whole, exceeds the Debtors' stated needs by millions and the Debtors' stated needs are themselves overstated by millions, the Court should find that the proposal, as a whole, is unnecessary.

1. The Debtors' Business Plan Is Flawed On Its Face.

The Debtors' business plan is a follow-on plan to the failed Cornerstone Strategy. There is little new in the current Plan for Success that was not contemplated, directly or indirectly, in the previous plan. In other words, the gravamen of the Plan for Success is reducing expenses and enhancing revenue to present credit metrics that may attract new capital so the Debtors can invest in their fleet. *See* Goulet Decl. at ¶ 46. The two features present in the Plan for Success that were not present in the Cornerstone Strategy are the unprecedented level of new aircraft ordered by the Debtors, but not justified by the Debtors' route structure or financial capability, and the unprecedented labor cost reductions made available under section 1113. Neither of these features is justifiable, and the labor cost savings are so enormous in relation to the Debtors' need, as to be unnecessary for the Debtors' reorganization. These facts alone could lead the Court to conclude that the Plan for Success is a flawed plan for American's future. But there is an even more fundamental defect, which gives rise to the inescapable conclusion that the Plan for Success is incurably flawed: it is predicated upon a stand-alone American emerging from these chapter 11 cases.

It is axiomatic that the Debtors have missed out on the multiple waves of consolidation that have swept through the airline industry over the last decade. The fact that American must merge with another airline with a complementary route structure and fleet to compete effectively with its peer group is equally axiomatic. As a result of the consolidations, American lost its place as the world's largest airline, falling to third. At the same time, during 2006 and 2007, two years of minimal profitability, American failed to invest in its fleet, choosing instead to pay hundreds of millions of dollars in bonuses to its executives. American, however, chooses to ignore the competitive advantages of consolidation and, concomitantly, the competitive challenges that American's merged peers pose for American's ability to compete in the future. The Debtors' investment banking expert, agrees that American has a fiduciary duty to consider alternatives to the so-called stand-alone plan and that has not happened. *See* Tr. Apr. 25 111:11 to 113:9.

The importance of American's fulfilling its fiduciary duties and considering all available alternatives cannot be overstated. The Plan for Success, inconceivably the only plan considered by American's management in the context of section 1113 negotiations, calls for draconian modifications to the TWU CBAs, which likely would not be required under a different plan. As it is, the modifications proposed by American are unnecessary. The level of labor cost savings required in a consolidation scenario would emanate from a multitude of factors, including revenue enhancements and operating synergies the merged carrier could be expected to achieve. Yet this Court will never be told the extent of those modifications because the Debtors have utterly failed to consider any alternatives to the stand-alone plan. That is not a Plan for Success; it is a recipe for financial ruin. The fact is that American cannot survive as a stand alone airline.

No one, other than Tom Horton, thinks that it can and no one, perhaps other than Tom Horton, believes that it will.

Despite its dead on arrival business plan, American asks this Court to authorize the rejection of the TWU CBAs- an act that will directly result in the loss of almost 9,000 jobs, significant reductions in pay for the few surviving employees, and the total loss of any security the TWU-represented employees have sacrificed for in the past. American should be required to present a viable business plan before being allowed to take such drastic measures.

2. The Debtors Do Not Need $1.25 Billion In Labor Savings

The Debtors' contention that it requires $390 million of cost savings from the TWU is based on the Debtors' underlying premise that it is necessary to obtain $1.5 billion in annual employee cost savings (which includes $1.25 billion from American and the balance from American Eagle) to establish a profitable and sustainable business. This underlying premise, however, is not supported by the evidence.

To arrive at the aggregate target cost savings from labor, the Company did not focus on whether their proposals to each labor group was market-based. Rather, the Debtors' management simply backed into the number by first making assumptions regarding the profitability metrics it wanted to reach. *See* Goulet Decl. ¶ 54 and fn. 21 *Id.*

There is no evidence, however, that the Debtors considered modestly lower financial metrics to ascertain whether achieving lower metrics would result in a sustainable business while at the same time reducing the cost savings ask from labor. Moreover, while the Debtors' financial advisor and investment banker opines in conclusory fashion that the metrics selected by the Company's management would result in a sustainable business enterprise and that the cost savings requested by the Company are necessary to reach them, he acknowledges that he was not involved in selecting the amount of the labor cost reductions and was not asked to consider, and did not consider, whether any lower cost savings number would result in a sustainable business. *See* Tr. Apr. 25 89:21 – 90:16, 94:1- 95:3.

Given the failure of the Debtors and their financial advisor and investment banker to consider whether more modest labor cost savings could result in a profitable and sustainable business, the Court should not find that the Debtors' proposed modifications which seek $390 million in cost savings, are necessary modifications that are necessary to permit the reorganization of the Debtors. The Debtors should not be permitted to assert that such drastic concessions are necessary unless less oppressive alternatives have been fully reviewed and analyzed.

3. The Debtors Undervalue Their Proposals To Extract Even More Concessions From The TWU-Represented Employees

The Debtors' proposal is not necessary because the Debtors either undervalue or *ascribe no value* to substantial portions of their proposals. As discussed more fully below, applying the Debtors' own outsourcing valuation methodology, the Debtors vastly underestimate the value that they will obtain from outsourcing. Second, and equally as egregious, the Company demands contract changes which, if implemented, would fundamentally alter employee protections, but attribute *no dollar value* to these changes. In other words, the Debtors insist on sweeping

contractual changes, such as increasing the amount of part-time employees, that they assert have no value. As an initial matter it is difficult to see how changes with a zero value could be necessary to the Debtors' reorganization. But, even if arguably necessary, the Debtors must properly value the modifications insisted upon.

As a result of the Debtors' improper valuations, the 1113 Proposal which is alleged to achieve the $390 million ask, would, if implemented, extract substantially more value from the TWU. This result is unnecessary by any measure.

The Debtors Undervalue The Savings From Outsourcing

More than 50 percent of the labor cost savings demanded of the TWU come directly from proposed modifications that will result in the outsourcing of thousands of jobs. AA Exs. 1212, 1213, 1140. The Debtors' valuation of the cost savings from outsourcing is generated pursuant to flawed metrics being applied to an arithmetic formula. The Debtors measure cost savings from outsourcing by subtracting the labor rates of outside vendors from the cost of the work performed in-house. The Debtors, however, acknowledge that they have not obtained actual bids from vendors for much of the work they seek to outsource. Instead, the Debtors use estimates to calculate the amount of their supposed savings. As discussed more fully below, the assumed rates the Debtors' utilize are not accurate and reliable. By applying improper vendor rates, the Debtors significantly undervalue the cost savings they contend will result from outsourcing, thereby overstating the amount of concessions that are purportedly "necessary."

Value of Cost Savings From Outsourcing

The Debtors measure the value derived from outsourcing pursuant to a simple arithmetic formula:

The cost of the TWU-represented employee ("**C-TWU**")

MINUS The cost of the replacement vendor ("**C-RV**")

= Debtor Saving (per employee) ("**Debtor Savings**")

Thus, for example, if the C-TWU rate is $7/hr and the C-RV rate is $5/hr, the Debtor Savings is $2/hr. If, by contrast, the C-TWU rate is $9/hr and the C-RV rate is $5/hr, the Debtor Savings is $4/hr. Similarly, if the C-TWU rate is $9/hr and the C-RV rate is $3/hr, the Debtor savings is $6/hr. In other words, Debtor Savings, which is the difference between the TWU rate and the vendor rate, will be greatest when the TWU number is high and the vendor rate is low (indeed, this is the argument that the Debtors use to justify outsourcing). In determining the value of outsourcing, however, the Debtors artificially manufacture a Debtor Savings rate that is too low, *i.e.*, the C-TWU number is artificially low and/or the C-RV rate is artificially high. The result is that the Debtors, based on their own valuation methodology, derive more benefit from outsourcing then they give the TWU credit for.

The Debtors Underestimate The C-TWU

The Company prices the difference between the cost of performing a function in-house and outsourcing by comparing the vendor's hourly rate with the rate of compensation for an American employee. For example, in calculating the price savings for outsourcing Fleet service employees, the Debtors compare the assumed vendor rate against the cost of a *junior* level American employee who earns less that an average employee. The proper approach is to use the cost of an *average* American employee.

Under the TWU agreements, employees are subject to a wage progression. A new hire starts at the bottom wage rate and progresses over several years to the top of the scale. Under the existing Fleet agreement for example, an employee starts at $8.64 hourly wage rate and progresses to $21.16 per hour after nine years of service. The average rate for the 2,000 most junior employees is $18.67. Adding benefit and other costs to the base rate brings the American in-house rate to approximately $33.58 per hour. The Debtors compare this base rate total cost to the assumed vendor rate of ██████ per hour. ██. Under the Company's approach, this ██████ difference is the hourly saving from outsourcing for the Fleet employee.

Yet, it is beyond doubt that a junior employee, if retained, would over the 6 year period of the contract term gradually move up the progression ladder and become the average employee. In fact, based on the current demographics of Fleet employees, the average hourly rate for an eliminated employee is significantly higher than the rate the Debtors' assume for a terminated employee. Thus, a major structural change which enables the Company to avoid the cost of performing the work in-house, avoids the cost of the average employee, not the near-term new hire. The hourly cost differential resulting from the Debtors' use of the cost of the junior employee, as opposed to the average employee, is more than $16 million per year for which the TWU is not being given credit against the Company's $150 million demand from Fleet employees.

The Debtors Overestimate The Cost Of The Replacement Vendor (C-RV)

In addition to under-estimating the cost of the existing TWU-represented employee, the Debtors' over-estimate the cost of vendor rates and thereby fail to give the TWU significant credit against the $390 million target. For instance, with respect to Fleet work that American

wants to outsource, the Debtors use an estimated hourly vendor cost of approximately [redacted]. However, the Company's own analysis of outsourcing experience indicates that vendor rates are actually much lower, closer to [redacted] per hour. The difference is significant. The appropriate estimate reduces the cost savings required under the Company's request by $16.4 million per year for the TWU's Fleet group alone.

The Debtors also over-estimate the vendor cost for M&R outsourcing. For valuation purposes the all-in hourly rate used by American for aircraft maintenance performed by a vendor is estimated at [redacted].[4] [redacted]. This might be a reasonable basis for estimating the "heavy maintenance" ("C" and "D" checks) involving the B757 fleet. However, under the Company's proposal, at least 250 mechanic jobs are directly eliminated by outsourcing the B777 and B767 fleets. These are wide-body aircraft deployed in international service. The comparator airlines with similar aircraft, to the extent they outsource, outsource to vendors in China or Singapore at substantially lower costs. Although management recognizes this possibility, the higher assumption – which results in undervaluing TWU concessions – was used. Again, by using too high a cost estimate for outsourced maintenance labor, the Company devalues the cost savings resulting in the demand for additional concessions that are not necessary to meet its $390 million cost savings target from the TWU. Put another way, assuming *arguendo* that the $390 million is an appropriate cost savings target (which it is not), the modifications requested by the Debtors are not necessary because, based on their own valuation methodology, the Debtors will obtain more than $390 in cost savings.

[4] [redacted]

The Debtors Undervalue the Savings From Other Proposals

There are many forms of contract concessions, such as wage and benefit reductions, which can be implemented immediately, and once implemented produce a level stream of savings throughout the 6-year duration of the plan. Other changes, notably outsourcing, are assumed to be implemented gradually, presumably because the Company requires time to negotiate vendor contracts. Under the Debtors' model, the so-called "phase-in" of savings creates a discount to the steady-state savings which inevitably will be realized by the Company. And, under the Company's approach, these saving are not credited to the TWU target of $390 million.

There are several types of "terminal value" for which the Debtors have neglected to give the TWU credit. For example, the Debtors discount the value of outsourcing by over $21 million per year presumably due to delays in implementing the outsourcing program, but do not account for the fact that the Debtors will continue to benefit from outsourcing Fleet work past the proposed six year CBA period. The delay in credit for the "phase-in" of outsourcing, over the 6-year business plan, represents a discount of over $21 million per year. In short, a major structural change resulting in the elimination of more than 1,000 jobs is underpriced by over 19 percent because the Debtors have refused to recognize the terminal value which will be realized in all years following the 6-year business plan.

Similarly, the Debtors' demand to extend the wage progression period for Plant Maintenance Mechanics (a subset of M&R) (the "**PMMs**") from 5 years to 9 years for new hires. *See* AA Exhibit 1209. The effect of this change is that it would take a new hire almost 10 years to achieve the maximum pay rate. The Debtors ascribe *zero* value to this change. The Debtors reason that during the 6-year term of the CBA, there are unlikely to be any "new hire" PMMs. Under the business plan, headcounts for the TWU M&R group are assumed to decline over the

6-year period (due to terminations and outsourcing, etc). Additionally, with all the outsourcing, hundreds of incumbent PMMs will have recall rights. If the Company needs a new PMM it will be required under the CBA to rehire a laid-off PMM, who is likely to have already achieved the maximum rate. Thus, the Company assumes that there will be no new PMMs hired during this 6-year period that will be subject to its progression demand over the contract term and thus no value is assigned. The Debtors have acknowledged in negotiations that this change in the wage structure will reduce average pay in the classification and drive significant savings in the future. On the one hand, the Debtors insist on the change; but on the other hand, insist the change has no value. If the change has no value, how can it possibly be necessary to the reorganization? The position is untenable and out of line with market norms.

The Debtors Ascribe Zero Value to Wide Scale Changes

Numerous Company proposals are designed to expand management prerogatives but, according to American, have no economic value that is appropriately credited to the TWU concession target. These items represent a grab-bag of contractual provisions which the Company argues are necessary, but it fails to attribute any economic value towards the cost savings target. As with the items described above, the Debtors take the untenable position that a change has no value but is necessary within the meaning of section 1113.

i. The "40 Percent Rule – Principal among the examples is the Company's position on the level of outsourcing under the M&R CBA. American proposes to expand its right to outsource additional jobs "*up to* 40 percent of aircraft maintenance work currently done in house."[5] (emphasis added). In valuing the cost savings, the Debtors have valued the level of outsourcing that they believe they will actually need now (a number less than 40%). They have

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[5] AA Ex. 1209

not valued the potential cost savings that would be achieved if they reached the 40% target in the future. In essence, the Debtors demand that they retain the option to terminate up to 40% of all M&R employees but they have not given the TWU any credit for that option.

ii. **Part-Time Caps** – The Company proposes to eliminate all restrictions on the right to employ and utilize part-time employees. The Company's optimal staffing models for the relevant classifications, suggest a fixed number of additional part-time workers. The Debtors, however, demand the option to employ and utilize part-time workers at will in the future, to preserve their flexibility. Yet, the Debtors propose to preserve the option of increasing the use of part-time employees over time while at the same time ascribe it a zero value toward the aggregate savings target.

iii. **Control over the Qualifications Administrative Manual –** Another example of Company overkill is the proposal to eliminate any restrictions on its right to change the Qualifications Administrative Manual. Wage negotiations involve an equation between the pay level and the associated duties, responsibilities and qualifications of the classification. Under the current collective-bargaining agreements, the Debtors and TWU negotiate these terms together. The Debtors insist that they control one side of this equation (*i.e.* the duties required for a specific pay level) but that the employees are locked into compensation levels. In plain terms, American seeks the right to increase an employee's duties without permitting a corresponding increase in the rate of pay. This change dissolves the wage-effort bargain that is fundamental to wage negotiations. The Debtors' assertion that this proposal has minimal economic value is unsound. If such a change has no economic value, the Company's insistence on its inclusion is unwarranted.

4. The Debtors' Claim That The TWU CBAs Are Above-Market Is Not Supported By The Facts Of These Cases

The Debtors' pleadings are rife with *innuendo* that the TWU CBAs are not competitive. *See e.g.*, MOL Part IV pg. 9, Part V pg. 5. But, as the Debtors acknowledge, "labor costs are a function of wages, work rules and benefits." MOL Part 1 pg. 69. On average, wages comprise three quarters of total compensation and the substantial majority of TWU-represented employees earn either the lowest or the near lowest wage rates (as compared to the comparator group). The TWU measures the relative compensation of its members using a model that is designed to measure total compensation per hour worked. The analysis is comprehensive and captures differences in cash compensation (base wages, license and skill premiums, longevity), supplemental benefits (pension, active health insurance, retiree health insurance, life insurance, short term disability benefits, long term disability insurance benefits, uniform/clothing allowances), and pay for time not worked (paid breaks, vacations, holidays, sick leave and on-the -job-injury benefits).

That measure is compared against the results of comparator airlines, Southwest, Continental, United, Delta and US Airways. Measured by capacity (domestic and international), these airlines, together with American, are the 6 largest carriers representing 77 percent of the entire industry. Traditionally, American, Continental, United, Delta and US Airways are considered the "legacy" or "network" carriers. Southwest is included because it is the 3rd largest airline (largest in the domestic market) measured by available seat miles ("**ASMs**"), and the largest airline measured by passengers enplaned. Additionally, Southwest is the major competitor of American measured by revenue share on city pairs served.

Wage Rates

Contrary to the Debtors' suggestion, the TWU CBAs, when considered in their entirety, are eminently competitive - in the Debtors' favor. As described below, wage rates for the three largest TWU craft classifications have been at or near the bottom of the market for years. Wage rates, which is the key driver of total compensation, have remained at the bottom of the scale even though United, Delta and US Airways have all gone through the chapter 11 process since 2003.

For the AMT at American, 73 percent of total compensation is driven by the base hourly wage rate. The fact that American pays its top-of-scale mechanic more than $4.85 per hour **less** than the industry average ($27.20 versus $32.05) explains the TWU's already unenviable position. Beyond the base rate – adding license, longevity, shift differentials and line premium – the wage gap persists. The all-in AMT/Line rate at top-of-scale at American is $32.75; compared to $37.06 for the other airlines – a $4.31 per hour difference.

Table[6] **11–** Comparative Wage Rates – 2012
TOS Hourly Rate Including License, Line, and Longevity

Airline	Aviation Maintenance Tech		Fleet Service Clerk	Stock Clerk
	Base	Line		
American	$32.20	$32.75	$21.46	$21.46
United	36.42	36.92	21.22	21.17
Continental	36.42	36.92	22.29	21.17
Delta	33.98	34.73	21.16	21.46
Southwest	43.89	43.89	25.97	27.30
US Airways	32.83	32.83	20.57	21.26
Average	$36.71	$37.06	$22.24	$22.47
AA Rank	Last	Last	3	3
AA as % of Avg.	87.7%	88.4%	96.5%	95.5%

[6] All tables referenced can be found in the Roth Declaration.

Pensions

To support its proposed reduction in TWU pensions, the Company has repeatedly declared that the competitive airlines have frozen or terminated their traditional defined benefit pension plans ("**DBP**") and replaced them with defined contribution plans ("**DCP**"), principally through the 1113(c) process. *See* Wright Decl. at ¶ 11, *citing* Glass Decl. at ¶¶ 271-275. However, with respect to ground service employees, this at best, is only partially true. The demise of the DBP for fleet service and M&R employees of the competitive airlines is greatly exaggerated. Today Continental and US Airways continue to have DBP for their M&R employees; Continental, United, and US Airways continue to maintain DBP for Fleet. More importantly, all of the comparator airlines offer pension programs that provide retirement plans superior to that proposed by American. The Company's demands with respect to pensions are unnecessary and leave TWU members with pension benefits far below its competitors.

Table 12 – Summary of Retirement Plans — Comparative Airlines 2012

		AA Prop.	COA	UAL	SWA	USA	DAL
Mech.& Related	DBP:	None	1.19% x FAE x YOS	None	None	Yes; IAM - NPP	None
	DCP:	100% match up to 5.5%	matching plan based on YOS: to 50% match up to 6%	5%; no match required	100% match up to 7.3%	None	2% plus 100% match up to 5%
	Cost:	4.4% of straight time	8.8% of Gross	5.0% of gross	5.8% of gross	6.4% of gross	6.0% of gross
Fleet Service	DBP:	None	1.19% x FAE x YOS	Yes: IAM-NPP	None	Yes; IAM - NPP	None
	DCP:	100% match up to 5.5%	matching plan based on YOS: to 50% match up to 6%	None	100% match up to 7.3%	None	2% plus 100% match up to 5%
	Cost:	4.4% of straight time	8.8% of Gross	6.5% of gross	5.8% of gross	5.0% of gross	6.0% of gross

Note: Cost to employer estimated assuming 80% participation to DCP.

Medical Care

A third major element of compensation is healthcare benefits. The Company's analysis of other airlines (conducted in mid-2011) revealed that contributions for active employees represented by the TWU were already on par with industry standards. The reported composite employee contribution, as a percent of the total cost, was 19 percent — the same as Continental, and higher than United, Southwest, US Airways. Only Delta was higher at 21 percent. Here, again, the Company's demand for an "equivalent" employee contribution of 21 to 27 percent is unnecessary and goes beyond the competitive norm. At US Airways for instance, the Fleet, M&R, and Stock Clerk groups agreed to a three-tiered Preferred Provider Organization ("**PPO**") Plan. Suffice to say that the plan option calling for the lowest contribution (7 percent) is far

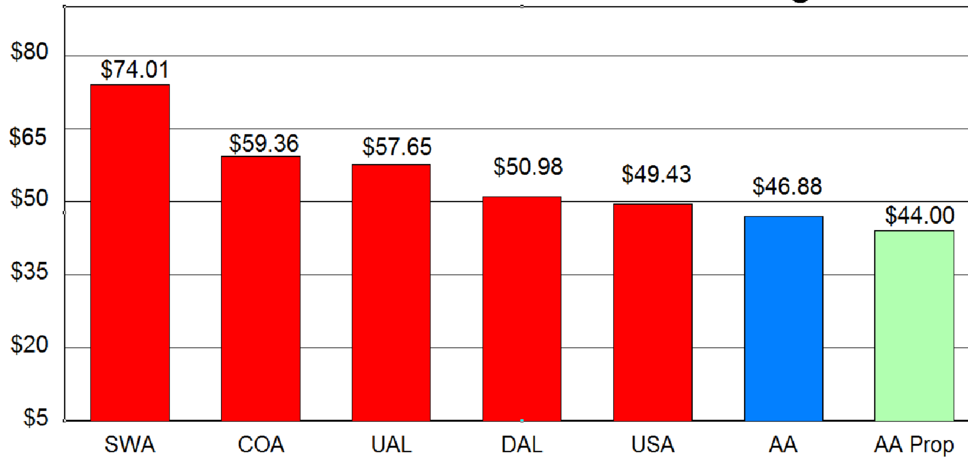
superior in coverage than either of American's proposed plans requiring 21 percent. Similarly, at United, the ground service employees agreed to a PPO that initially requires a 20 percent employee contribution for single or family coverage. Significantly, the employee contribution increase is subject to a 7 percent annual cap. Accordingly, the contribution today is significantly less than 20 percent. As with US Airways, the United plan design, with a fixed annual deductible of $250 and out-of-pocket maximum of $1,500, is superior to the best option (22% single/29% family) offered by American.

When Northwest sought consensual agreements from its ground service employees in its 2006 bankruptcy, it proposed that employees pay 15 percent of required contributions to a quality PPO. The employee contribution was subject to a maximum annual increase of 8 percent. The plan called for an annual deductible for single/family of $350/$700 for both in-network and out-of-network. The out-of-pocket employee maximums were $2000 and $4000 for single and family subscribers respectively. The cap on contributions caused the employee share to fall over the term. Apart from much lower contributions, the design features of the Northwest plan provided coverage far superior to that offered by American now.

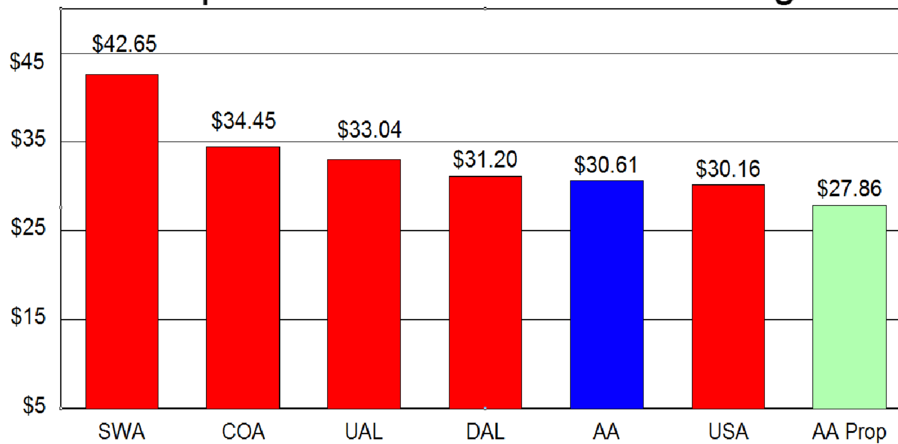
Table 13 - Summary of Active Employee Health Insurance Plans - Comparative Airlines 2012 Active Employees in Ground Service						
	AA Prop.	COA	UAL	SWA	USA	DAL
Annual Deductible: Ind/Family	$300/ $900	None	$250/ $500	$200/ $300	$225/ $450	$500/ $1,500
Co-Insurance:	80/20	100%	80/20	80/20	90/10	80/20
Out-of-Pocket Max: Ind./Family	$2,750/ $8,250	NA	$1,500/ $3,000	$2,500/ $2,500	$1,500/ $3,000	$2,500/ $5,000
Drug Co-Pay: Generic (min/max) Formulary (min/max) Non-Form (min/max)	 $10 ($20/$75) 30% ($40/$150) 50% ($70/$180)	 $5 $25 $50	 20% credited to Deductible	 $0 20% credited to deductible	 $15 $30 $50	 $10 25% ($30/$75) 25% ($50/$125)
Employee Cont. Share:	22% Ind. 29% Fam.	20%	13%	0%	14%	
Notes: AA proposal for "Value" Plan which is most popular plan with TWU members (90%); features are for in-network where applicable for plans most comparable to AA "Value" Plan.						

Total Compensation

AMT is the largest classification in TWU's M&R group. This class represents 36 percent (approximately 8,400 employees) of all TWU members at American. Prior to any proposed concessions in compensation, AMTs at American were the lowest paid in the comparison group at $46.88 per hour. After reducing shift differentials, pensions, health care, vacations and sick leave the AMT's compensation falls to $44.00 per hour – 12 percent below US Airways, the next lowest in the group.

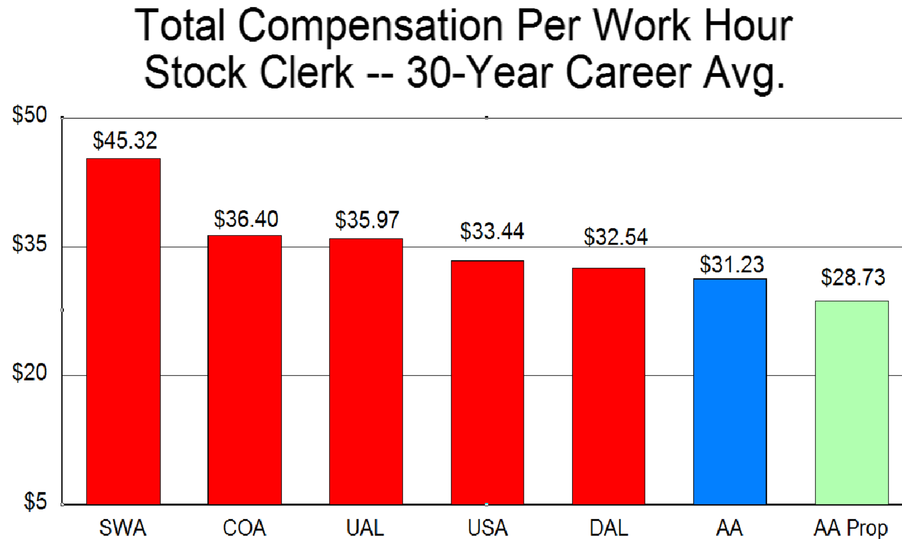


Fleet makes up 43 percent of the TWU membership and is the sole classification under the TWU Fleet Service contract. Today, Fleet is paid $30.61 per hour, slightly above US Airways. For Fleet the base rate is 82 percent of total compensation. At $21.16, the Fleet is already $1.00 below the average. But after the additional cuts in compensation demanded by the Company, the Fleet rate will be $27.86 – 8.5 percent below the next lowest rate.



Stock Clerks, representing 6 percent of the TWU population at American, is the only classification under the TWU Stock Clerk agreement. Stock Clerk's compensation level is

currently the lowest among the comparative airlines. With the additional concessions, they will be paid $28.73 per hour, 13.3 percent below the next lowest rate of $32.54 at Delta.



Conclusions On Compensation Comparisons

With respect to the TWU group, the Company's demands for changes in scope alone eliminate any competitive labor cost disadvantage. The additional demands for reduced compensation are completely unnecessary to achieve the competitive labor cost objective contemplated by the section 1113(c) process. The cuts in compensation – including pensions, health insurance, vacations, sick leave and shift differentials – drive the key TWU classifications to the absolute bottom of the competitive airline market. This is plainly overkill and goes well beyond necessity by any measure.

Pay Levels Upon Exit From Bankruptcy

As discussed above, it is clear that overall compensation levels for TWU-represented employees is not above market and that the proposals demanded by American would push the levels to the low end of American's competitors. The Company, through its airline labor expert, argues that this result is consistent with prior airline bankruptcy experience. As set forth in the declaration of Thomas R. Roth In Opposition To The Motion To Reject The Collective

Bargaining Agreements Covering Employees Represented By The Transport Workers Union of America, AFL-CIO (the "**Roth Decl**."), this assertion is not accurate. Moreover, even if it was, the test for whether modifications are necessary is not whether the proposals are necessary to drive compensation levels to the ground, but whether they are necessary to permit reorganization. Those proposed by American are clearly excessive and beyond what is necessary to permit reorganization.

5. The Debtors' 1113 Proposal Is Not Necessary Because The TWU Proposed An Alternative That Meets The Debtors' Cost-Savings Targets

The Debtors' 1113 Proposal is not necessary for their reorganization because there is a different, viable, less oppressive alternative available to the Debtors. From the time it was presented the February Term Sheets through the day American filed the Motion, the TWU made several proposals to the Company that would achieve substantially all of the Debtors' target labor cost-savings without the massive headcount reductions and certain other modifications included in the Debtors' February Term Sheets. A detailed discussion of the TWU's proposals and how they meet the Debtors' cost-savings targets is set forth in the Roth Decl.

Across all TWU bargaining units, TWU negotiators focused on contract changes that would produce hard-dollar savings while preserving headcount to the greatest extent possible. The TWU position, collectively, would generate approximately ninety percent of the $390 million target set by the Debtors even if the Debtors' flawed valuations were utilized. If the proposals were properly valued, the TWU proposals would reach one-hundred percent of the Debtors' objective. And, significantly, the TWU's proposals would have preserved many more jobs. Roth Decl. at ¶¶ 45, 81 and Tables 16 and 17 therein.

Thus, the Debtors could achieve their target savings from the TWU-represented employees without resorting to the drastic measures (including almost 9,000 job cuts) requested by the Debtors' proposals.

B. The Debtors Failed to Make Their Proposals Based on the Most Complete and Reliable Information

One of the requirements that a debtor must satisfy before a court can authorize the rejection of a collective bargaining agreement is that the debtor provide the union with the most complete and reliable information available at the time the debtor makes its proposal. 11 U.S.C. 1113(b)(1). American has failed to satisfy this element because it has provided little, if any, information regarding its analysis and strategy with respect to future merger/consolidation opportunities.

The Debtors' and their investment bankers acknowledge that a consolidation transaction is something that American has explored and should explore. Indeed, American has a fiduciary duty to maximize value during this chapter 11 proceeding by exploring all alternatives. Yet, in the context of section 1113 proposals and negotiations, American has ignored, and not provided information regarding, any analysis of how a merger transaction may impact the need for the labor concessions it is requesting. Instead, it focuses exclusively on the stand-alone strategy and contends that information regarding consolidation transactions has no relevance to the necessity of the proposals that is has made to the TWU. This contention is wrong because in order for the TWU to fully assess the necessity of concessions that are premised on a stand-alone plan, the Debtors should be required to provide information concerning the amount and form of concessions that might be necessary in the event American merged with another airline. This is especially the case where, as here, American's industry competitors have experienced a wave of consolidations that have resulted in improved financial performance.

C. The 1113 Proposal Does Not Treat the TWU-Members Fairly And Equitably

Section 1113(b)(1)(A) mandates that the Debtors' proposals treat all creditors, the debtors, and all affected parties fairly and equitably. The Debtors may not seek to place a disproportionate share of the financial burden of avoiding liquidation upon labor unions. *See In re Nat'l Forge Co.,* 279 B.R. 493, 501 (Bankr. W.D.Pa. 2002). The burden must be spread fairly and equitably among all affected parties. *See Wheeling-Pittsburgh Steel*, 791 F.2d at 1091. The focus of the inquiry is whether the proposed sacrifices will be borne disproportionately by members of the bargaining unit or will be spread among all affected parties. *See id*. Moreover, the concessions sought from various parties "must be examined from a realistic standpoint." *See id*. at 1093.

Despite the clear requirement of the statute and the admonitions of the courts, the Debtors' proposal foists substantially all of their cost savings on their labor unions. Preliminarily, there is a dearth of evidence in the record that financial creditors of the Debtors (*i.e*., bondholders) will share any part of the sacrifice of these chapter 11 cases. In fact, those creditors (unsecured all) will likely receive all of the stock of the reorganized company under a plan of reorganization. Other creditors (*i.e*., trade creditors and lessors) may be providing minimal concessions to aid the Debtors' reorganization, but may reap enormous dividends in the form of the appreciation of equity that they may receive under a plan and a going-forward business partner for those concessions. And, the Debtors' management and support staff savings may turn out to be illusory.

The Debtors allege that the 1113 Proposal is fair and equitable because, among other reasons, American's non-union employees will shoulder their fair share of the burden. While the precise nature of the cost-savings that these groups will contribute has not been determined, it is clear that "American simply cannot reduce significantly Management and Support Staff's

compensation below their already uncompetitive levels and hope to attract and retain the talent necessary to allow it to successfully emerge from restructuring." MOL, Part I p. 54. The Debtors state further that:

> On January 24, 2012, American's CEO, Tom Horton, announced a review and restructuring of American's management workforce that is intended to reduce the total direct cost attributable to management and support staff by at least 15% through reductions in headcount. The reductions began at the top—at the Senior Officer level. They included four Executive and Senior Vice Presidents and the consolidation of their responsibilities with those of other executives. These reductions will continue progressively down through the Management and Support Staff ranks and are anticipated to account for the remaining $107 million in Management and Support Staff labor cost reductions. To the extent, however, that these headcount reductions fall short of that number, additional labor cost reductions will be achieved through other means in order to ensure that Management and Support Staff contribute fairly and equitably to the overall direct labor cost reductions.

Id. They go on to say that ". . . the remaining $55 million in cost reductions [needed to achieve their targets] will be realized through a combination of other changes" that will be determined as American finalizes its internal evaluation process. *See* Wright Decl. at ¶ 67. In other words, the Debtors have not yet identified the cuts, but will get there eventually, and the Court, TWU and all other parties in interest are supposed to just trust them. TWU does not trust the Debtors on this score, having learned painful lessons in the past, and neither should the Court. In 2003, after obtaining staggering concessions from labor, including the TWU, including record numbers of layoffs, direct and indirect management staff suffered very few job losses. Management simply was protected, despite assurances by the Debtors that everyone would share the sacrifice.

Simply put, the Debtors are looking to TWU and the other unions to bear the brunt of the so-called "shared sacrifices." That is not fair and equitable to the TWU-represented workforce.

D. The TWU Has Good Cause to Refuse to Accept The Debtors' Proposal

Bankruptcy Code section 1113(c)(2) provides that the court may authorize the Debtors to reject a collective bargaining agreement *only if* the TWU has refused to accept the Debtors' proposal without good cause. The Debtors bear the burden of proving that the TWU rejected the proposed modifications without good cause. *See, e.g., In re Family Snacks*, 257 B.R. 884, 892 (8th Cir. B.A.P. 2001). The Debtors concede that they must prove this element by a preponderance of the evidence. When a labor union "seeks to negotiate compromises that meet its needs while preserving the debtor's required savings, it would be unlikely that its rejection of the proposal could be found to be lacking good cause." *Royal Composing Room*, 848 F.2d at 349; *see also In re Maxwell*, 981 F.2d at 90. In other words, if the TWU proposed an alternative to the Debtors' proposal that would achieve the same level of savings but in a form that was more palatable and less oppressive for the TWU-represented workforce, and the Debtors refused that proposal, that workforce would have good cause for rejecting the Debtors' proposal.

This is what happened here. As detailed in section I.A.5 supra, the TWU delivered several proposals to the Debtors and engaged in discussions with the Debtors in an effort to reach mutually acceptable collective bargaining agreements. The proposals put forward by the TWU would achieve substantially all of the Debtors' target labor cost-savings without the draconian headcount reductions and other modifications included in both the February Term Sheets and the March Term Sheets. A detailed discussion of the TWU's proposals and how they meet the Debtors' cost-savings targets is set forth in the Roth Declaration submitted herewith. The Debtors refused these proposals, insisting on their more egregious, drastic proposals. Thus, the TWU-represented work force faced a Hobson's choice: accept the oppressive proposals put forward by the Debtors or bear the brunt of the instant Motion to reject the TWU CBAs. In the face of such a choice, when a better, less

severe alternative was available to the Debtors, the TWU-represented workforce cannot be said to have refused the Debtors' 1113 Proposal without good cause.

Moreover, the TWU is justified in refusing to accept the Debtors' proposals because the Debtors engaged in bad faith negotiations with the TWU. For example, the Debtors have steadfastly refused to reduce their $390 million demand of the TWU (which is based on a fallacious business plan). As another example, the Debtors' proposal assumes outside vendor rates that it knows are significantly higher than rates the Debtors currently pay to outsource similar work and that are higher than rates generally obtained in the market. The import of this is that the Debtors failed to provide the TWU with sufficient credit toward its savings target.

In refusing to accept the TWU's proposals, which would provide the Debtors with their target cost savings; by refusing to budge off the $390 million target, and by failing to properly credit the TWU for the actual value of the Debtors' outsourcing proposals, it is clear that the Debtors' true objective was never to engage in good faith negotiations with the TWU, but to fabricate a record of compliance with section 1113 as a subterfuge to convince this Court to grant the Motion. *See In re Royal Composing Room, Inc.*, 848 F.2d 345, 348 (2d Cir. 1988) ("If the debtor proposes an element objectionable to the union, the union . . . can argue that the part of the proposal it cannot accept was included by the employer in bad faith, in an attempt to stalemate negotiations and allow it to obtain outright rejection rather than a negotiated compromise. If the union can make such a showing, the debtor would not be entitled to reject the labor contract under *Carey Transportation*, 816 F.2d at 90").

The Debtors behavior makes sense only as a tactic to ensure that negotiations fail. The rejection of the Debtors' proposals by the TWU-represented workforce was therefore in good

faith. Therefore, the Debtors have failed to carry this element of section 1113 and the Motion must therefore be denied.

E. The Balance Of The Equities Does Not Clearly Favor Rejection Of The TWU CBAs

The Debtors have not demonstrated that the balance of the equities favors rejection of the TWU CBAs -- let alone "clearly" favors rejection. The Debtors argue that the equities clearly favor rejection "because the specter of liquidation is much worse for all constituencies." MOL Part I pg. 95. American goes on to state that "if American disappears, all of its employees would receive less than if the airline emerged as a going concern." *Id.* These arguments assume, without any evidentiary support, that American will liquidate if the Motion is denied. That is simply not the case.

If the TWU CBAs are not rejected, American will not be forced to liquidate. Rather, it will be forced to make new reasonable proposals, unlike those embodied in the Company's February Term Sheets and March Term Sheets. Given that the Debtors entered chapter 11 with in excess of $4 billion in cash and their liquidity position remains stable, there is no reasonable likelihood of a liquidation pending negotiations that would occur after the Court denies the Motion.

Moreover, as part of the balancing analysis, the Court should take the Debtors' negotiating conduct into account. Although the Debtors go to great lengths to document the fact that they were willing to met, discuss and respond to inquiries, it is the quality and content, not the quantity, of discussions that is most important. As outlines above, from the time it issues the February Term Sheets on February 1, 2012, until it delivered the March Term Sheets on March 22, 2012, American did not move off its take-it-or-leave-it approach and insisted on $390 million in cost savings from the TWU. In fact, American actually insisted on more than $390 million in concessions because it undervalue or offered no credit for many of its proposals.

Furthermore, American knew, and was told by TWU negotiations that proposals that would result in the loss of 9,000 jobs were extremely oppressive, and would never be accepted. Nevertheless, just like it refused to lower its overall ask, American did not alter its position on outsourcing issues. The TWU, on the other hand, many significant proposals designed to improve the financial condition of the Company while mitigating, to some degree, the hardships that the Debtors' proposals would impose on TWU members and their families.

In short, the balance of the equities does not clearly favor rejection of the TWU CBAs. Meaningful and viable alternatives are available that can both position American to become a profitable business without imposing unduly burdensome hardships on TWU represented employees and their families.

II. ASSUMING REJECTION OF THE TWU COLLECTIVE BARGAINING AGREEMENTS, THE COURT LACKS THE POWER TO IMPOSE TERMS AND CONDITIONS OF EMPLOYMENT ON TWU-REPRESENTED EMPLOYEES.

The proposed order filed with the Motion would grant the Debtors extraordinary relief that is not requested in the Motion itself, permitted under section 1113 of the Bankruptcy Code, or within the power of this Court to grant. In particular, the Motion requests only that the Court authorize the Debtors to reject their CBAs with the Unions:

> Pursuant to section 1113(c) of the Bankruptcy Code, the Debtors are seeking entry of an order authorizing them to reject the CBAs between the Debtors and the Allied Pilots Association, the Association of Professional Flight Attendants, and the Transport Workers Union of America, AFL-CIO (collectively, the "Unions").

Motion at ¶ 6.

Nevertheless, the proposed order submitted with the Motion would grant the Debtors the unfettered and unilateral right to impose on the TWU-represented employees the terms of the 1113 proposal:

> ORDERED that the Debtors are authorized to implement and perform under the terms of the proposals under section 1113 of the Bankruptcy Code, as more fully described in the Motion, and to take any and all actions that may be reasonably necessary or appropriate to effectuate the same and perform all obligations contemplated under such proposals; and it is further

Proposed Order at p. 2.

The relief granted in the proposed order therefore is significantly broader that that requested by the Motion. In fact, imposing terms of the 1113 Proposal on the TWU-represented employees is not discussed anywhere in the Motion. Accordingly, the Debtors are not entitled to this relief, should the Court grant the Motion at all (which it should not).

Assuming, *arguendo*, the Court determines that the Debtors have properly requested authority to impose the terms of the 1113 Proposal if the Motion is granted, such relief is outside the scope of section 1113 and cannot be granted by the Court. Section 1113(a) limits the relief the Debtors may request to assumption or rejection of a CBA. *See* 11 U.S.C. § 1113(a) ("The debtor in possession … may assume or reject a collective bargaining agreement only in accordance with the provisions of this section"). Moreover, section 1113(c) grants the Court the power only to "approve an application for rejection of a collective bargaining agreement" if the Court finds that the statutory requirements have been satisfied. *See* 11 U.S.C. § 1113(c); *but see*, 11 U.S.C. § 1113(d)(2) (authorizing debtors to "terminate or alter" any provision of a CBA pending the court's ruling only in cases where the court fails to rule within the statutory time period). The power of the Court under section 1113 is clear and unambiguous: it can authorize the Debtors only to assume or reject a collective bargaining agreement. The Court cannot impose the terms of employment following the rejection of a CBA.

Furthermore, the question of whether and which terms of employment the Court should impose is a non-core matter that the Court does not have the power to resolve on a final basis.

In *Stern v. Marshall*, 131 S.Ct. 2594 (2011), the Supreme Court ruled that Bankruptcy Courts, which derive their authority not from Article III of the U.S. Constitution but from Article I, lack the constitutional authority to adjudicate claims that properly can be decided only by an Article III court. *Stern v. Marshall*, 131 S.Ct. at 2597. Thus, while the Bankruptcy Court may have the statutory authority pursuant to 28 U.S.C. § 157 to determine "core" matters on a final basis, such authority may not be constitutional. *Id*. In *Stern*, the Supreme Court held that the Bankruptcy Court lacked the constitutional authority to enter a final judgment on a counterclaim that was asserted in connection with a claim filed against the bankruptcy estate, because the Bankruptcy Court's determining that question "[withdrew] from judicial cognizance [a] matter which, from its nature, is subject of a suit in the common law, or in equity, or admiralty." *Id*. (*citing Murray's Lessee v. Hoboken Land & Improvement Co.*, 59 U.S. 272 (1856)).

The *Stern* Court distinguished between matters involving "public rights" (matters involving a federal regulatory scheme) and "private rights" (matters arising out of state common law between two parties that do not depend on the will of Congress). *Id.* at 2611-2614. With respect to the latter, the Court held that "if a statutory right is not closely intertwined with a federal regulatory program Congress has power to enact, and if that right neither belongs to nor exists against the Federal Government, then it must be adjudicated by an Article III court." *Id.* at 2614. In order words, Article I courts may enter final judgments only in matters involving questions that are closely related to a statute constitutionally enacted and involving the federal government. Otherwise, a final judgment can be entered only by an Article III court.

The issue of what terms of employment prevail following the rejection of a collective bargaining agreement is neither "closely intertwined" with a federal statutory scheme, nor does it involve, directly or indirectly, the federal government. Rejection of a collective bargaining

agreement simply results in "terminating the parties' agreed-to working conditions… ." *In re Northwest Airlines Corp.*, 483 F.3d 160, 174 (2d Cir. 2007). Where, as here, the parties' relationship is governed by a federal statute, such as the RLA, rejection has no effect on the parties' duty "to make every reasonable effort to 'make' [an agreement]." *Id.* Importantly, rejection of a collective bargaining agreement "absolves [the parties] of their status quo duties under the RLA," *id.*, making the dispute resolution procedures of the RLA inapplicable once the collective bargaining agreement has been rejected. In any context, the RLA does not specify or impose terms and conditions of employment. Rather, the terms and conditions of employment under the RLA are subject to private negotiations among private parties leading to private agreements. In the context of a collective bargaining agreement that has been rejected pursuant to section 1113, the RLA both prevents the imposition of terms and conditions by proscribing an employer's authority to unilaterally alter any term in a collective bargaining agreement and relieves the parties of the statute's mediation procedures. The parties are thus left to their private remedies which are at the heart of Article III.

Accordingly, the sole remedy this Court may provide to the Debtors is authority to reject their collective bargaining agreements with the TWU. This point is moot, however, because, as discussed herein, the Debtors have not satisfied the requirements of section 1113 and are not entitled to reject those agreements.

III. POST STERN, THE RIGHT TO STRIKE CANNOT BE ENJOINED BY A BANKRUPTCY COURT

The TWU does not consent to the jurisdiction of the Court to enjoin or in any way limit its right to strike in the event of an adverse ruling on the Debtors' Motion. Specifically, the TWU submits that the Supreme Court's decision in *Stern* regarding the jurisdiction of a

bankruptcy court conflicts with the injunctive relief arguably permitted by the decision of the *In re Northwest Airlines Corp.,* 483 F.3d 160 (2d Cir. 2007) regarding the right to strike.

In *Stern*, the Supreme Court reviewed the jurisdiction of a bankruptcy court that calls into question whether a bankruptcy court has the jurisdiction to enjoin a strike. *Stern* observed that congress divided jurisdiction over bankruptcy cases into three categories: (i) those arising under title 11, (ii) those arising in a title 11 case, and (iii) those only related to a case under title 11. *Stern*, 131 S. Ct. at 2603-04. *Stern* further recognized that under 28 U.S.C. § 157(b)(1), the bankruptcy court's primary jurisdiction extends only to "all core proceedings arising under title 11 or arising in a case under title 11." *Stern*, 131 S. Ct. at 2603 (quoting 28 U.S.C. § 157(b)(1)). However, with regard to "noncore" proceedings only "related to" a case under title 11, the bankruptcy court may only submit proposed findings of fact and conclusions of law to a district court for final consideration after *de novo* review. *Stern*, 131 S. Ct. at 2604.

In *Stern*, the Supreme Court concludes by observing that: (1) Article III of the Constitution provides that the judicial power of the United States may be vested only in courts whose judges enjoy the protections set forth in that Article; (2) in enacting section 157, Congress exceeded the limitation contained in Article III in "one isolated respect"; and (3) the bankruptcy court in *Stern* lacked the constitutional authority to enter a final judgment on a state law counterclaim that was not resolved in the process of ruling on a creditor's proof of claim. *Stern*, 131 S. Ct. at 2620.

The Second Circuit held that where a debtor has been authorized by a bankruptcy court to abrogate its CBA, such abrogation absolves the debtor of its status quo duties under the RLA. *See In re Northwest Airlines Corp.,* 483 F.3d 160, 169-70 (2d Cir. 2007). The Second Circuit noted that Northwest did not breach the CBA when it rejected the agreement, but rather by

following the section 1113 process to its conclusion had "*abrogated*" the agreement, after which the CBA ceased to exist. In holding that rejection under section 1113 abrogates a CBA, the court noted that "[c]ontract rejection under § 1113, unlike contract rejection under § 365, permits more than non-performance; it allows one party, with the court's approval, to establish new terms that were not mutually agreed upon, the antithesis of a status quo." *Id.* at 171. The Court went on to state that "[i]f a rejected CBA were somehow to remain in force (to whatever extent), a carrier's adherence to a new, bankruptcy-court-approved contract would surely violate Section 2 (Seventh) of the RLA, which prohibits carriers from 'chang[ing] the rates of pay, rules, or working conditions of its employees, as a class as embodied in agreements except in the manner prescribed in such agreements or in section 156 of this title.'" *Id.* In accord with the Supreme Court holding in *Stern*, in *Northwest*, the Second Circuit affirmed the district court's strike injunction holding that the union there had not sufficiently pursued the RLA's dispute resolution processes and that a strike would violate the union's duty under §2 (First) of the RLA to make every reasonable effort to reach a new agreement. *Id.* at 175.

Section 1113 provides the exclusive mechanism by which a debtor may obtain authority to reject its CBAs with its unionized employees. *Chicago Dist. Council of Carpenters Pension Fund v. Cotter*, 914 F. Supp. 237, 242 (N.D. Ill. 1996) (quoting *In re Alabama Symphony Assoc.*, 155 B.R. 556, 571 (Bankr. N.D. Ala. 1993)) ("Section 1113 has been interpreted to mean that no other provision of the Code may be used to allow a debtor to bypass the requirements of Section 1113. In other words, a collective bargaining agreement cannot be rejected under Section 365."); *see also Tool & Die Makers Local Lodge Number 113 v. Buhrke Industs., Inc.*, 1996 WL 131698, *8 (N.D. Ill. 1996) ("Section 1113 modifies or alters the result obtained under § 365 to the extent of the provision in §1113"). Collective bargaining agreements remain in effect until

modified or rejected in accordance with the statute's requirements. *See* 11 U.S.C. § 1113(f) ("No provision of this title shall be construed to permit a trustee to unilaterally terminate or alter any provisions of a collective bargaining agreement prior to compliance with the provisions of this section."); *In re Ionosphere Clubs, Inc.*, 922 F.2d 984, 990 (2d Cir. 1990); *In re Arrow Transp. Co. of Delaware*, 224 B.R. 457, 460 (Bankr. D. Or. 1998). Among other things, section 1113 requires that the modifications sought by the Debtors be necessary for a successful reorganization and that the Debtors attempt to negotiate modifications to their CBAs with the union in good faith before they can be allowed to reject those agreements. 11 U.S.C. § 1113.

Under the Railway Labor Act, 45 U.S.C. §§ 151 *et seq*., a union is authorized to exercise self-help remedies -- including the right to strike – arguably even after rejection of a collective bargaining agreement under section 1113 of the Bankruptcy Code. The RLA, which applies to airlines by virtue of 45 U.S.C. § 181, establishes a comprehensive set of procedures for resolving disputes between carriers and their unionized work force to "avoid any interruption to commerce or to the operation of any carrier engaged therein" and "provide for the prompt and orderly settlement" of disputes over rates of pay, working conditions or the interpretation and application of collective bargaining agreements. 45 U.S.C. § 151(a). As interpreted by the Supreme Court, the RLA distinguishes between "minor" and "major" disputes, and requires different dispute resolution mechanisms for each category of dispute. *Consolidated Rail Corp. v. Ry. Labor Execs. Ass'n*, 491 U.S. 299, 302-04 (1989); *Elgin, J. & E.R. Co. v. Burley,* 325 U.S. 711, 722-26 (1945). Minor disputes -- which involve disagreements over whether employer or employee action is permitted under the terms of an existing collective bargaining agreement -- are subject to mandatory binding arbitration before the National Railroad Adjustment Board or an adjustment board established by the employer and union. 45 U.S.C. § 153; *Conrail*, 491 U.S. at

303-04. Unions are not permitted to strike over minor disputes, and courts are free to enjoin such illegal strike activity. *Conrail*, 491 U.S. at 304; *Bhd. of R.R. Trainmen v. Chicago R. & Ind. R.R. Co.*, 353 U.S. 30, 42 (1957) (holding that NLGA does not deprive federal courts of jurisdiction to enjoin strikes over minor disputes because of specific provisions of RLA compelling unions to submit such disputes to binding arbitration). In other words, Congress chose compulsory arbitration as "the statutory substitute for strikes and other work action by which unions in other industries have often tried to enforce their interpretation of a collective bargaining agreement (in the absence of a no-strike clause), but which are thought unduly disruptive in the transportation industry." *Chicago & North Western Transp. Co. v. Ry. Labor Execs. Ass'n*, 908 F.2d 144, 148 (7th Cir. 1990), *cert. denied*, 498 U.S. 1120 (1991).

The RLA treats "major" disputes very differently. A major dispute occurs where either the carrier or the union seeks to change the terms of an existing collective bargaining agreement. Rejecting compulsory arbitration for major disputes, Congress instead imposed upon carriers and their labor unions a lengthy series of mediation-type procedures set forth in section 6 of the RLA to facilitate consensual resolution of the dispute. 45 U.S.C. §§ 156, 157, 160; *Bhd. of Ry. and S.S. Clerks v. Florida E. Coast Ry. Co.*, 384 U.S. 238, 246-47 (1966) ("[T]he procedures of the Act are purposely long and drawn out, based on the hope that reason and practical considerations will provide in time an agreement that resolves the dispute."); *Detroit & Toledo Shore Line R.R. Co. v. United Transp. Union*, 396 U.S. 142, 149 (1969) (noting that exhaustion of the Act's remedies is an "almost interminable process"). These procedures include providing written notice of the proposed contractual changes, direct negotiations between the parties, and mediation under the auspices of the National Mediation Board. *Detroit & Toledo*, 396 U.S. at 149-51, n.14. If these efforts fail, the President has the power to create an Emergency Board to

investigate the dispute and submit a report. 45 U.S.C. § 160; *Detroit & Toledo*, 396 U.S. at 150-51. Throughout this process, and until 30 days have elapsed following closure of the National Mediation Board proceedings or, if one has been appointed, submission of the Emergency Board's report, neither the carrier nor the union may unilaterally change the terms of employment or resort to self-help remedies. 45 U.S.C. § 152, Seventh; *Detroit & Toledo*, 396 U.S. at 150-51. Instead, both sides must "exert every reasonable effort" to settle the dispute "in order to avoid any interruption to commerce or to the operation of" the carrier. 45 U.S.C. § 152, First. However, neither the President, the Emergency Board nor the National Mediation Board has the power to decide the dispute or impose a resolution on the parties.

Once the parties have exhausted the section 6 procedures and still failed to resolve a major dispute, both sides are allowed to resort to self-help without judicial interference. As put bluntly by Judge Posner, the "terminus of such a dispute, if the procedures set forth in section 6 fail to produce agreement between the parties, is a strike." *Chicago & North Western*, 908 F.2d at 148. Since Congress did not provide for compulsory arbitration, once the union "exhaust[s] all the procedures provided by Congress," it is permitted to invoke the "ultimate sanction" of a strike. *Florida E. Coast*, 384 U.S. at 244; *Conrail*, 491 U.S. at 303 ("Once [the RLA's] protracted process ends and no agreement has been reached, the parties may resort to the use of economic force."); *Bhd. of R.R. Trainmen v. Jacksonville Terminal Co.*, 394 U.S. 369, 378-79 (1969) (noting that Court had held in a "long line of decisions" that once the RLA's major disputes procedures were exhausted the "ultimate right of the disputants to resort to self-help" could be invoked); *Bhd. of Locomotive Eng's v. Baltimore & Ohio R.R. Co.*, 372 U.S. 284, 291 (1963) ("What is clear . . . is that both parties, having exhausted all of the statutory procedures, are relegated to self-help in adjusting this dispute. . . ."). A strike is "'the inevitable alternative

in a statutory scheme which deliberately denies the final power to compel arbitration.'" *Jacksonville Terminal*, 394 U.S. at 378 (quoting *Florida E .Coast Ry. Co. v. Bhd. of R.R. Trainmen*, 336 F.2d 172, 181 (5th Cir. 1964), *cert. denied*, 379 U.S. 990 (1965)).

The coequal restraint on the use of self-help by labor and management is the critical element of the RLA's mechanism for preventing strikes while still protecting employees from the superior bargaining power of management. During the protracted section 6 process, self-help is not available to either side. The carrier cannot modify the status quo by unilaterally changing the terms and conditions of employment, and the union cannot modify the status quo by striking. As explained by the Supreme Court, this "status quo" requirement encourages the parties to reach a consensual solution:

> Its immediate effect is to prevent the union from striking and management from doing anything that would justify a strike. In the long run, delaying the time when the parties can resort to self-help provides time for tempers to cool, helps create an atmosphere in which rational bargaining can occur, and permits the forces of public opinion to be mobilized in favor of a settlement without a strike or lockout. Moreover, since disputes usually arise when one party wants to change the status quo without undue delay, the power which the Act gives the other party [the right] to preserve the status quo for a prolonged period will frequently make it worthwhile for the moving party to compromise with the interests of the other side and thus reach agreement without interruption to commerce.

Detroit & Toledo, 396 U.S. at 150.

However, the coequal lifting of restraints on the use of self-help by both sides when the section 6 procedures fail to produce a consensual agreement is no less important in achieving the RLA's objectives. Once the parties have exhausted section 6 procedures, the carrier must make the decision whether to try to continue negotiations or make unilateral changes to working conditions with the knowledge that the union is free to strike if it wishes. Indeed, it "could hardly be expected that the union would sit idly by as the [carrier] rushed to accomplish the very

result the union was seeking to prohibit by agreement." *Id*. at 154. Knowledge that the other side can resort to self-help is a further deterrent to actually engaging self help by either management or labor, and an inducement to return to the bargaining table without a commerce-disrupting work stoppage. *See Burlington N. R.R. Co. v. Bhd. of Maint. of Way Employees*, 481 U.S. 429, 451-52 (1987) (reasoning that, because of both parties' interest in avoiding a strike, the availability of self-help "may increase the effectiveness of the RLA in settling major disputes by creating an incentive for the parties to settle prior to exhaustion of the statutory procedures").

Moreover, maintaining the mutual availability of self-help under the RLA prevents one side from ever being completely at the economic mercy of the other, and permits negotiations between the airline and the union to be conducted fairly and freely. As the Supreme Court has noted, if the airline is free to resort to self-help, "the union cannot be expected to hold back its own economic weapons, including the strike." *Detroit & Toledo*, 396 U.S. at 155; *Jacksonville Terminal*, 394 U.S. at 384 ("'[W]hen the machinery of industrial peace fails, the policy in all national labor legislation is to let loose the full economic power of each (party). On the side of labor, it is the cherished right to strike.'") (quoting *Florida E. Coast Ry.*, 336 F.2d at 181). Making self-help available to both sides ensures that whatever agreement is ultimately reached will be the product of arms-length negotiations, rather than a one-sided deal produced by economic coercion. "Only if both sides are equally restrained can the Act's remedies work effectively." *Detroit & Toledo*, 396 U.S. at 155; *see also Jacksonville Terminal*, 394 U.S. at 381, 392-93 (holding that state courts have no power to enjoin peaceful strike activity and picketing protected under the RLA and noting that the "Railway Labor Act's entire scheme for the resolution of major disputes would become meaningless if the States could prohibit the parties from engaging in any self-help.").

Thus, while Congress clearly wanted to prevent strikes, the RLA does not seek that objective at the expense of disarming organized labor. Rather, the RLA preserves the strike as a legitimate tool in industrial relations that unions are free to invoke when the RLA's other procedures fail to resolve a major dispute. *Jacksonville Terminal*, 394 U.S. at 384 ("[E]mployees subject to the Railway Labor Act enjoy the right to engage in primary strikes over major disputes."). As explained by the Ninth Circuit, while Congress intended the RLA to be a "response to the perceived dangers of disruption in the transportation industry," the

> policy of the statute is not that any act which disrupts the transportation industry may be enjoined. Instead, after major disputes procedures are completely exhausted, with reasonable efforts having been made to reach an agreement, the policies peculiar to the RLA are also exhausted, and the parties are governed by general labor law principles.
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> [*Trans Int'l Airlines, Inc. v. Int'l Bhd. of Teamsters*, 650 F.2d 949, 962-63 (9th Cir. 1980) (where union struck after exhausting the major dispute resolution mechanisms under the RLA, the federal courts had no power to enjoin strike), *cert. denied*, 449 U.S. 1110 (1981).]

Thus, so long as it is consistent with the RLA, a strike is perfectly lawful even if it causes economic disruption to the carrier. *Jacksonville Terminal*, 394 U.S. at 374-75, 393.

Indeed, courts must not violate the RLA's three key principles that (1) neither side can unilaterally alter the status quo while the section 6 procedures are ongoing, (2) self-help remedies must be available on equal terms to both sides, and (3) no outsider (whether a court, an arbitration panel or even the President) has the legal authority to impose a resolution of a major dispute on either the employer or the union.

In *Pan American World Airways, Inc. v. Int'l Bhd. of Teamsters*, 894 F.2d 36, 37-38 (2d Cir. 1990), the parties exhausted the RLA's major dispute resolution procedures without reaching agreement on a new contract following the expiration of the parties' collective

bargaining agreement. The airline then immediately (and lawfully) modified the employees' rates of pay, rules and working conditions, while the employees continued working without a contract. *Id*. at 38. Over a year later, after further negotiations failed to produce a new contract, the union began a series of intermittent work stoppages. *Id*. The airline unsuccessfully sought an injunction on the grounds that its lawful unilateral modification of the terms of employment created a new "status quo" that could not be disrupted by the union until section 6's dispute resolution procedures were exhausted a second time. *Id*. at 38-39. On appeal, the Second Circuit rejected this attempt by the airline to enforce working conditions "unilaterally imposed by Pan Am in the exercise of its right to self-help" and "deny that right to its adversary." *Id*. Instead, the court held that a new "status quo" following a carrier's unilateral imposition of new terms of employment only occurs when the carrier and the union reach a consensual resolution of the dispute.

Until that happens, the union retains the right to strike. *Id*. at 39. The TWU does not consent to the jurisdiction of this Court to consider this issue or in any way to abrogate these rights.

IV. STATEMENT PURSUANT TO RULE 7012 OF THE FEDERAL RULES OF BANKRUPTCY PROCEDURE

The TWU asserts that the question of whether the Bankruptcy Court can impose terms of employment on the TWU-membership and whether the TWU-membership retains the right to strike in the event of rejection are non-core under 28 U.S.C. § 157, and the TWU does not consent to the entry of a final order by this Court.

V. RESERVATION OF RIGHTS

Pursuant to the agreement between the Debtors and the TWU, because the TWU has sent the Debtors' last and best proposals out to a vote by its membership, the TWU has not cross-examined Debtors' witnesses Jeffrey Brundage, James Weel and Mark Burdette and the TWU has reserved the right to cross-examine these witnesses. The TWU preserves and reserves the right to raise any evidentiary objections to the testimony given by these three witnesses. In addition, the TWU reserves the right to rely on the testimony of all witnesses whether called by the TWU or other parties and to rely upon any arguments raised by other parties.

CONCLUSION

For the reasons stated above, the portion of the Motion seeking to reject the TWU CBAs should be denied because American has not satisfied the requirements necessary for the rejection of collective bargaining agreements under section 1113 of the Bankruptcy Code.

Dated: New York, New York
May 7, 2012

Respectfully submitted,

By: /s/ Sharon L. Levine

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