ALLIED PILOTS ASSOCIATION EQUITY DISPUTE ARBITRATION

In the Matter of	)	
	)	
DISTRIBUTION OF EQUITY BY THE ALLED PILOTS ASSOCIATION	)	ARBITRATOR STEPHEN GOLDBERG
	)	
	)	

ALLIED PILOTS ASSOCIATION'S STATEMENT OF POSITION

Date: July 8, 2013

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The Arbitrator's task is to assess a distribution scheme by which the Allied Pilots Association ("APA" or "Association") intends to distribute equity received from American Airlines ("American" or the "Company"). The equity distribution scheme was developed through months of hard work by the five pilots serving on the Equity Distribution Committee ("Committee"), acting with the help of union staff, legal counsel, and financial experts. Thousands of hours of effort went into the development of the system. Without animus to any group of pilots, the Committee endeavored to create a fair and reasonable solution to an incredibly complex problem. They did so. The Arbitrator should uphold the equity distribution scheme in all respects, because it is not arbitrary, does not constitute discrimination against any pilot or group of pilots, and was not developed in bad faith.

Drawing from duty of fair representation principles, litigation over previous union distributions, and settlement allocation cases in the class action context, this brief demonstrates that the equity distribution scheme withstands scrutiny.

I. Facts

This Section summarizes the key facts regarding the equity distribution, as relevant to challenges. Additional detail is provided in the APA's six declarations.

A. The AMR Bankruptcy and Section 1113

On November 29, 2011, the parent company of American Airlines, AMR Corp., filed for bankruptcy under Chapter 11. The Company announced that a key goal of the reorganization would be to reduce labor costs. The Company therefore proposed a series of

drastic modifications to its collective bargaining agreements with the APA and other unions pursuant to Section 1113 of the Bankruptcy Code, 11 U.S.C. § 1113.[1] *See In re AMR Corp.*, Case No. 11-15463, Docs. 2034, 2041 (Bankr. S.D.N.Y. March 27, 2012). When the unions did not agree to these modifications, the Company requested court authority to abrogate the collective bargaining agreements on March 27, 2012. *Id.* After an initial denial, the court eventually granted authority to abrogate the 2003 collective bargaining agreement between American and the APA ("2003 CBA") on September 5, 2012. *In re AMR Corp.*, Doc. 4293.

While litigation was pending, the Association negotiated with American for a new collective bargaining agreement that would inevitably contain substantial concessions by the union, including the freeze of the defined benefit pension plan and elimination of the lump sum option, changes to schedule rules, and easing of restrictions on outsourcing of flying. In June 2012, the parties agreed that APA would receive a substantial equity stake in the Company (the "Equity Stake") in the event they could reach a new collective bargaining agreement. Declaration of Andrew Yearley ("Yearley Decl."), at ¶ 22.

The APA's top financial advisor, Andrew Yearley, met with Company representatives, principally its investment bankers, to negotiate the size of the Equity Stake. *Id.* at ¶ 8. Although Mr. Yearley presented a variety of figures that attempted to quantify the financial impact of the proposed concessions, these figures were highly speculative and were not the controlling factor in the negotiation. *Id.* at ¶¶ 10, 16–22. Instead, the parties used prior airline bankruptcy settlements to determine what equity stake would be acceptable to the various stakeholders. *Id.* at ¶ 18-20. Ultimately, the Company agreed to grant the

[1] A related provision, 11 U.S.C. § 1114, pertains to the benefits of retired employees.

Association 13.5% of the equity distributed to the universe of unsecured creditors in the bankruptcy. *Id.* at ¶ 10(a). In exchange, the APA released many of its legal claims arising from the bankruptcy, including its right to appeal the bankruptcy court's decision on the contract rejection motion. *See* LOA 12-01 at APA Exh. 5.

The new agreement, including significant concessions along with the Equity Stake, was ratified by the pilots on December 7, 2012, and approved by the bankruptcy court, as required by law, on December 19, 2012. Declaration of Mark Stephens ("Stephens Decl."), at ¶ 7. The agreement took effect on January 1, 2013. It is referred to in this statement as the "2013 CBA."[2]

Weeks after approval of the 2013 CBA, the Association entered a Memorandum of Understanding with American, US Airways, and the pilots' union of US Airways. *See* APA Exh. 1. Commonly referred to as "the MOU," this agreement governed pilots' terms and conditions of employment in the event of a merger between American and US Airways. *Id.* The MOU provided for certain modifications to the 2013 CBA, including an increase of two percentage points in Company contributions to the defined contribution plan. Declaration of Michael Mellerski ("Mellerski Decl."), at ¶ 88. Because the Boards of Directors of American and US Airways have now approved the merger, the MOU is almost certain to take effect when the Company emerges from bankruptcy. Stephens Decl. at ¶ 20.

[2] Some APA documents refer to the agreement as the "2012 CBA," because it was ratified in 2012, but this declaration uses the term "2013 CBA" based on the effective date of the agreement.

B. The Equity Distribution Committee

The APA's equity distribution scheme was developed by the Equity Distribution Committee and approved by the APA Board of Directors ("Board") virtually unchanged. Stephens Decl. at ¶ 11. The Committee was appointed on October 5, 2012, by APA President Keith Wilson. The members of the Committee are Michael MacMurdy, Michael Mellerski, Doug Pinion, David Quinlan, and Mark Stephens. *Id.* at ¶ 6. Each member had previously served in other capacities for the union and brought unique perspective and skills to the Committee. *Id.* The Committee members range in seniority from the 311th most senior pilot at American to the 6476th most junior, and range in age from 49 to 59. *Id.*

Over more than six months, the Committee spent thousands of hours developing the equity distribution scheme and dealing with related issues. *Id.* at ¶ 9. In doing so, they relied on extensive assistance from the APA's legal counsel, including specialists in bankruptcy, securities, ERISA benefits and taxation; financial advisors at Lazard; and internal union experts on the valuation of collective bargaining agreements, pilot data, and pensions. *Id.* at ¶¶ 14–18. Two of the Committee's advisors, Andrew Yearley of Lazard Frères & Co., LLC ("Lazard"), and Gregory Kidder of Steptoe & Johnson, LLP ("Steptoe"), have submitted Declarations in this proceeding.

C. The Committee's Guiding Principles

The distribution scheme is based in large part on a series of "guiding principles" developed by the Committee. Stephens Decl. at ¶ 22. As explained in the Declaration of Mark Stephens and in this Statement, many of the challenged decisions flow directly from these principles:

(1) The distribution should be based on a forward-looking analysis of contractual concessions in the 2013 CBA, starting on the effective date of that agreement.

The first two guiding principles can be summarized as follows: the distribution will be used to mitigate the impact of concessions in the 2013 CBA, measured beginning on the effective date of that agreement, January 1, 2013. *Id.* at ¶ 23. The APA only received the Equity Stake as a result of the 2013 CBA, and the parties understood the Equity Stake to be intended largely as compensation for the concessions in that agreement. *Id.* at ¶ 26. Those concessions came into effect on January 1, 2013, and would be in effect at least during the stated duration of the agreement, January 1, 2019. *Id.* at ¶ 23. The Committee analyzed the impact of these concessions by comparing the 2013 CBA to the 2003 CBA.

In accordance with this principle, the Committee decided *not* to use the equity distribution as a way of mitigating harms incurred prior to January 1, 2013, such as the concessions in that 2003 CBA. *Id.* at ¶ 26. The Equity Stake was certainly not meant to compensate for prior decades of harm. *Id.* Instead, it was connected specifically to the 2013 CBA. *Id.*

The Committee also did not focus on harm to the pilots during the approximately four-month period after American secured court authority to abrogate the 2003 CBA. *Id.* at ¶ 27. During that period, American phased in certain modifications to pilots' terms and conditions of employment, though many of the Company's bankruptcy proposals were never implemented during that period or only implemented for a short period of time. *Id.* In any case, abrogation itself was not the source of the APA's Equity Stake. *Id.* The Equity Stake came solely from the ratification and approval of the 2013 CBA. *Id.* The APA's attorneys informed the Committee that, while the APA could have argued in court that it

was entitled to some unsecured claim arising from abrogation, the outcome of that litigation likely would have been negative based on the legal precedent in the Second Circuit. *Id.*[3]

(2) Specific harm to pilots is highly uncertain and could not be fully remedied by the equity distribution even if it could be quantified.

Another critical principle was that the APA would not be able to use the distribution to mitigate all pilot harms. *Id.* at ¶ 29. For one thing, the Equity Stake was far too small to do so. *Id.* For another, it was simply impossible to project the harms to be incurred by individual pilots. *Id.* Indeed, in collective bargaining, American and the APA do not try to predict harm to individual pilots but rather look at aggregate harms to the entire pilot group. *Id.* But even these projections are uncertain, particularly in the realm of Scope, where the impact is highly dependent on Company business decisions, and with respect to work rules, where the impact is highly dependent on pilot behavior. *Id.* at ¶ 30.

Recognizing this, the Committee decided to concentrate on rough and general calculations of harm that accounted for relative effects on various pilot demographics. *Id.* at ¶ 31.

(3) Neither the Company nor APA could hold back any significant portion of the Equity Stake for later distribution.

The equity distribution scheme is also the product of the Association's recognition that it cannot reserve any significant portion of the Equity Stake for any significant period

[3] "Abrogation" is an important term of art established by the Second Circuit in a case holding that an order pursuant to Section 1113 does not reject a contract, giving rise to contract damages, but instead abrogates the contract. *In re Northwest Airlines Corporation,* 483 F.3d 160, 170-172 (2007). This is a critically important distinction for unions faced with a motion pursuant to Section 1113. *See In re Northwest Airlines Corporation,* 366 BR 270 (Bankr. S.D.N.Y. April 13, 2007) (holding that union did not have a legal right to damages following abrogation).

following its receipt. The reasons for this flow from tax law and from other logistical considerations. First, American refused to hold the equity, citing the risk that the Company would lose the ability to carry forward a very substantial net operating loss to offset future tax liability. *See* Declaration of Gregory Kidder ("Kidder Decl."), at ¶ 14. Meanwhile, the Association's tax counsel advised that the APA should not hold the equity. *Id.* at ¶ 33. The equity would be deemed to have been "constructively received" by pilots on the date that it was received by the APA, regardless of when the Association transfers it to pilots. *Id.* at ¶ 30. But it would be incredibly complex to determine the appropriate amount of tax, and withholding would be due immediately. *Id.* at ¶ 32. The Association would become the withholding agent, creating both a risk of liability for tax violations and a guarantee of significant administrative costs. *Id.* at ¶¶ 30–32. Moreover, if the Association were the withholding agent, the funds could not be contributed to a tax-protected retirement plan. *Id.* at ¶ 29.

Aside from these concerns, the Committee determined that a holdback would simply delay difficult eligibility issues, while exposing the money to inflation and investment risk. Stephens Decl. at ¶ 45. Furthermore, it would be difficult to predict how much of the money to reserve. *Id.*

D. Silos and methodology

The APA distribution scheme is based on a "silo system," meaning that the Equity Stake will first be separated into several smaller sums, or "silos," and a separate methodology will be applied to distribute the equity from each Silo. Mellerski Decl. at ¶ 7. The APA adopted a silo system because it allowed the union to account for a variety of harms associated with the concessions in the 2013 CBA, without necessitating an impossible

inquiry into the specific financial impact of each and every concession. *Id.* at ¶ 9. Indeed the term "silo" was adopted from the Delta ALPA MEC and the Northwest ALPA MEC, both of which constructed what they called silo systems for distribution of the money they received as a result of their carriers' bankruptcies. *See Gilliland v. Air Line Pilots Ass'n Int'l*, 741 F. Supp. 2d 1334 (N.D. Ga. 2009); *Bondurant v. Air Line Pilots Ass'n*, 679 F.3d 386 (6th Cir. 2012).

The APA adopted four Silos: (1) the Inverse Seniority Silo, (2) the Per Capita Silo, (3) the Years of Service Silo, and (4) the Pension Silo. The first two of these Silos are prorated for pilots who will be forced by federal law to retire at age 65 during the term of the 2013 CBA. The remainder of this section describes those Silos, while the following section explains the APA's decisions regarding allocation among the Silos.

1. Inverse Seniority Silo

The Inverse Seniority Silo aims to mitigate the impact of contract changes that, while affecting all pilots, cause disproportionate harm to junior pilots. Many of the concessions in the 2013 CBA will lead to reduced opportunities for advancement to more lucrative flying positions. Mellerski Decl. at ¶ 40. For example, due to changes to work rules, pilots will be forced to work more days and hours, meaning that fewer pilots are needed for each aircraft type and seat. *Id.* at ¶¶ 40(a) and (b). Similarly, changes to the Scope clause of the CBA will allow the Company to outsource more flying, thereby limiting career advancement opportunities. *Id.* at ¶ 41.

However, the impact of these changes will not fall exclusively on junior pilots. *Id.* at ¶ 43. For example, work rule changes will likely eliminate some current routes and trips on all equipment types, thereby limiting the pool of trip options for even captains on the largest

planes. *Id.* at ¶ 43(a). Moreover, the impact of these changes depends in part on relative seniority within a bid status, meaning that the impact may be significant for a pilot who is very senior globally but junior within his bid status. *Id.* at ¶ 43(b).

To distribute the equity from the Inverse Seniority Silo, the distribution scheme provides that the most junior eligible pilot will receive twice the payout of the most senior eligible pilot. *Id.* at ¶¶ 45-46. Other pilots' payouts will be determined on a linear scale between those two endpoints. For example, a pilot who is junior to 75% of pilots would receive a payout 1.75 times larger than the most senior pilot.

The APA chose the 2-to-1 linear scale for several reasons. First, a linear scale—a straight line—was much simpler and more transparent than any more complicated curve that the APA might have devised. The 2-to-1 scale was appropriate because the most junior pilots (*i.e.,* narrowbody first officers) have pay rates that are approximately half of those for the most senior pilots (*i.e.,* widebody captains). In addition, other pilot unions that distributed money related to their carriers' bankruptcies used a 2-to-1 linear scale for seniority-based Silo distributions, albeit with senior pilots at the higher end of the scale. *Id.* at ¶ 46.

Finally, the Silo was prorated for pilots who will be legally required to retire during the term of the 2013 CBA. *Id.* at ¶ 49. The Inverse Seniority Silo was prorated because it corresponded to harm occurring only while a pilot is active. *Id.* To prorate the distribution from the Silo, the APA calculated the fractional number of years between January 1, 2013 and each pilot's sixty-fifth birthday, then divided by six, representing the six-year term of the contract. *Id.* at ¶ 50. Pilots will receive a percentage of the payout equal to the resulting value. *Id.* at ¶¶ 50-51.

2. Per Capita Silo

The Per Capita Silo aims to mitigate the impact of contract changes that affect all pilots to a roughly equal degree, or for which it was impossible to predict which pilots will be most significantly harmed. *Id.* at ¶ 52. This Silo is associated with concessions including changes to the medical insurance plan for active pilots and the lesser quality of work life associated with scheduling changes. *Id.* at ¶¶ 52(a) and (b).

The methodology in this Silo was simple: each pilot received an equal payout, except for pilots who will be legally required to retire during the term of the 2013 CBA. *Id.* at ¶ 54. This Silo was prorated for those pilots because, like the Inverse Seniority Silo, the harms associated with the Silo occur only while a pilot is active. *Id.* The proration methodology in this Silo is identical to the proration methodology in the Inverse Seniority Silo. *Id.*

3. Years of Service Silo

The Years of Service Silo aims to mitigate harm correlated with seniority, pay rate, or proximity to retirement. *Id.* at ¶ 22. All of these characteristics, in turn, are highly correlated with "years of service," as defined for the purposes of the Silo. *Id.* In particular, a pilot's payout from the Years of Service Silo is based on the number of years between the pilot's Occupational Date and January 1, 2013. *Id.* at ¶ 23. Occupational Date generally corresponds to the date that a pilot began flying for American, with certain exceptions.[4] *See* McDaniels Decl. at ¶ 8.

[4] An idiosyncrasy of the Railway Labor Act, 45 U.S.C. § 201, is that a person does not become an employee of an air carrier until they actually perform work for the carrier. *See Eastern Airlines v. Air Line Pilots Ass'n,* 920 F.2d 722, 727 (11th Cir. 1990). American assigns this "Occupational Date" 47 days after a person is hired by the Company. McDaniels Decl. at ¶ 8.

The following types of harms are associated with the Years of Service Silo: post-retirement harms, such as the elimination of subsidized retiree medical insurance and the elimination of the lump sum option in the pension plan; harms with impact correlated to a pilot's pay, such as profit-sharing; changes to the international premium, which have a greater affect on pilots with higher hourly rates and the ability to choose favorable trips; and changes to vacation, which are directly related to a pilot's length of service. Mellerski Decl. at ¶ 24.

The APA chose to create a single Silo based on years of service, rather than several Silos based on seniority, pay rate, and proximity to retirement, in order to avoid unnecessary complexity. *Id.* at ¶ 26. Years of service is directly linked to seniority and is correlated to age (and therefore proximity to retirement), pay rate, and accredited service for vacation purposes. *Id.* The APA chose to use pilots' Occupational Date as a measure of years of service because, as the determinant of bidding seniority, it was most closely related to many of the harms associated with the Silo. *Id.* at ¶ 28.

The methodology in this Silo provided every pilot a payout proportional to his or her years of service. *Id.* at ¶ 36. This Silo was not prorated because some of the harms associated with the Silo occur post-retirement. *Id.* at ¶ 38.

4. Pension Silo

The Pension Silo aims to mitigate harm associated with the freeze of the Defined Benefit Pension Plan (known as the "A Plan"). *Id.* at ¶ 56. The A Plan was frozen effective November 1, 2012, meaning that pilots will receive, at retirement, only the benefit they would have received if they had retired on that date. *Id.* at ¶ 57. To partially mitigate this loss, the parties agreed that pension contributions to the defined contribution plan would

increase from the current 11% to 14% initially, and then to 16% on January 1, 2014. *Id.* at ¶ 88.

Although the calculations in the Pension Silo are somewhat complicated, the basic idea is simple: project the benefit that each pilot would have received at retirement under the A Plan if the plan had not been frozen, then subtract from this figure a projection of the benefit the pilot will receive from the frozen A Plan, together with a projection of the increased pension contributions the pilot will receive. *Id.* at ¶ 58.

The most difficult aspect of the Pension Silo calculation is a projection of pilots' future pay, but here again the idea is simple. The Committee developed a pay model that uses actual pay over the last five years to project a salary for each seniority number. *Id.* at ¶¶ 64-68. The model then traces pilots' progression through the seniority list over time, assuming that each pilot retires at age 65, and matching pay at each seniority number to the historical data. *Id.* at ¶¶ 72-74. The model also accounts for pay raises by assuming that pay at each seniority number will increase annually by the percentages specified in the 2013 CBA and by 1.7% each year thereafter. *Id.* at ¶ 72.

E. Allocation between Silos

After determining the methodology for each Silo, the Committee had to make a recommendation as to how the Silos would be weighted. Ultimately, the Committee decided to allocate 30% of the Equity Stake to the Inverse Seniority Silo; 30% to the Pension Silo; 20% to the Per Capita Silo; and 20% to the Years of Service Silo. Stephens Decl. at ¶ 76. The Board accepted the recommendation without alteration. *Id.* at ¶ 77.

This allocation decision was based on a number of factors, including estimates of the financial impact on pilots resulting from the 2013 CBA. *Id.* at ¶ 73. However, the

Committee did not rely solely on such projections. *Id.* Instead, the allocation process was one based largely on "art, judgment, and policy rather than a definitive damage or cost calculation." *Id.* at ¶ 71. For example, the APA had an institutional interest in "limit[ing] the absolute differentials between pilots while still acknowledging that some pilots were likely to be affected more than others." *Id.* at ¶ 73. And the importance of many contract changes cannot be fully assessed on a purely quantitative basis. *Id.* at ¶ 72.

There were several additional reasons why valuation estimates could not be determinative. The available estimates were mostly projections of cost-savings to the Company, first used in the context of collective bargaining. *Id.* at ¶ 73. These estimates were an imperfect proxy for harm to pilots and were highly speculative even when used as originally intended. *Id.* at ¶¶ 72-73. For these reasons and others, the APA and American had not relied on valuation analyses when they negotiated the size of the Equity Stake, focusing instead on the sums granted to pilots unions in other airlines' bankruptcies. Yearley Decl. at ¶¶ 16-22.

Unsurprisingly, the Committee discovered that there were many different ways of quantifying and categorizing the damages associated with the contractual concessions, each of which led to different, but reasonable, allocation recommendations. Stephens Decl. at ¶ 75. The Committee settled on the following figures as one rational way of measuring the financial impact of the concessions, using a six-year duration for most contractual changes but a twelve-year duration, the average remaining career of an American pilot, for pension: $1080 million impact from freeze of the defined benefit pension plan (Pension Silo), $1127 million impact for concessions associated with reduced flying opportunities (Inverse Seniority Silo), $551 million impact for concessions assumed to have an equal effect across

the pilot group (Per Capita Silo), and $555 million impact for concessions correlated to pay or service (Years of Service Silo). *Id.* at ¶ 75. When taken as a percentage of the overall impact and then rounded to the nearest ten, these figures corresponded to the ultimate allocation: 30% Pension Silo, 30% Inverse Seniority Silo, 20% Per Capita Silo, and 20% Years of Service Silo. *Id.* at ¶ 76.

F. Eligibility for the Equity Distribution

Aside from the silo methodology and allocation of funds among the silos, the equity distribution scheme includes eligibility criteria to determine who is eligible to receive payouts from each silo.

1. Eligibility for Pilots who are active on January 1, 2013, or become active during the Supplementary Qualification Period

The starting principle for eligibility is simply that all pilots who were active on January 1, 2013, are eligible to receive a share of the equity from all four silos. Stephens Decl. at ¶ 44. To the extent possible, the Committee also wanted to include pilots who would become active later and would therefore be affected by concessions in the 2013 CBA. *Id.* at ¶ 46. However, the Committee faced serious time constraints and could not extend the eligibility period indefinitely, due to a range of legal and logistical concerns. *See supra* at 7. In order to include as many pilots who would become active after January 1, 2013, as possible, within these constraints, the Committee created a Supplemental Qualification Period ("SQP"), which extends from January 1 to August 1, 2013. Stephens Decl. at ¶ 47. Any pilot who becomes active during the SQP is eligible for a share of the equity, just as if he had been active on January 1, 2013, provided that he signs an enforcement letter and accompanying promissory note agreeing to remain an active pilot at American for at least

twelve months. *See* Stephens Decl. at ¶ 69. This requirement is designed to deter pilots from briefly returning to the company or changing status solely in order to claim a share of the equity distribution. *Id.*

The Committee also established eligibility rules for certain special categories of pilots, most of which are described here.

2. Furloughees

The eligibility criteria provided that any pilot could become fully eligible if the pilot (1) was offered and accepted recall during the SQP (*i.e.,* before August 1, 2013), (2) was scheduled during the SQP for a training class to begin on or before October 30, 2013, and (3) signed the enforcement letter and promissory note described above. Stephens Decl. at ¶ 54. As of May 6, 2013, every furloughed pilot had been offered recall to American and therefore has had the opportunity to satisfy these requirements. *See* McDaniels Decl. at ¶ 16.

Furloughed pilots who have chosen not to return to American are ineligible for a share in the equity distribution. Stephens Decl. at ¶ 58. There is no way to predict whether these pilots will ever return to American and, if so, when. *Id.* at ¶ 57; McDaniels Decl. at ¶ 19. Pilots currently on furlough have deferred for as long as six years and there is a significant likelihood they will never return to active status at American. Stephens Decl. at ¶¶ 56-59; McDaniels Decl. at ¶¶ 18-19. In light of these facts and in light of the impracticability of reserving a portion of the equity for later distribution, the Committee decided to make pilots choosing to defer recall ineligible for a share of the equity.

3. Pilots flowing up from American Eagle

In 1997, APA, American, American Eagle Airlines ("Eagle") and the Air Line Pilots Association (representing Eagle pilots) entered into an agreement that permitted certain

Eagle pilots to "flow up" to American in the event of hiring by American and permitted junior American pilots to "flow down" to Eagle in the event of furloughs. McDaniels Decl. at ¶¶ 21-22. This agreement became Supplement W to the 1997 and 2003 CBAs between APA and American and expired by its terms in May 2008. *Id.*

Although Supplement W has expired, certain Eagle pilots still have American seniority numbers and may become active American pilots during the SQP. Stephens Decl. at ¶ 67. These pilots do not qualify for the Pension Silo because they had no frozen defined benefit and were not American employees with an expectation of a benefit under the A Plan. *Id.* However, they can become eligible for payouts from the other three silos in much the same way that furloughed pilots can become eligible. By the SQP, they must (1) be offered and accept a spot in an American training class scheduled to begin on or before October 30, 2013, and (2) sign an enforcement letter and promissory note. *Id.*

4. Pilots on Long-Term Disability, Sick Leave of Absence or Unpaid Sick Leave of Absence

Pilots qualify for a full share of the equity distribution if they have been receiving Long Term Disability ("LTD") benefits for fewer than five years, or if they are on Sick Leave of Absence ("SLOA") or Unpaid Sick Leave of Absence ("USLOA"). Stephens Decl. at ¶¶ 61-62. These pilots have a relatively strong likelihood of returning to active status. *Id.*

In contrast, pilots who have been on LTD longer than five years are removed from the seniority list and can only return to active status by agreement of both the Company and APA. Stephens Decl. at ¶ 63. These former pilots are much less likely to return to active status than the pilots who have been on LTD less than five years. *Id.* Nevertheless, the APA decided that these pilots should be eligible to receive a partial share of the equity

distribution. All former pilots who have been on LTD longer than five years are eligible for a payout from the Pension Silo because, under the A Plan, pilots receiving disability benefits continued to accrue credited service up to age 60. *Id.* at ¶ 64. Additionally, those who have been on LTD longer than five years but began receiving disability benefits on February 1, 2004, or later are eligible to receive a payout from the Per Capita Silo. *Id.* These pilots participate in the active-pilot medical plan and therefore are affected by the changes to that plan which the Per Capita Silo was designed, in part, to mitigate. *Id.*[5]

5. Other leaves of absence

Pilots on Military Leave of Absence ("MLOA") as of January 1, 2013, will receive their full share of the equity distribution. This is consistent with APA's continued support of military service and also reflects the fact that, historically, nearly all pilots on MLOA return to active status. Stephens Decl. at ¶ 53. Pilots on Personal Leave of Absence ("PLOA"), who also almost always return to active status, will receive their full share of the equity distribution provided that they sign an enforcement letter and promissory note agreeing that they will return to active status for at least twelve months. See Stephens Decl. at ¶¶ 65, 69.

6. Pilots Terminated Awaiting Grievance

Terminated Awaiting Grievance, or "TAG," is a status created by APA and used only internally within APA. McDaniels Decl. at ¶ 14. In order to be on TAG status, a pilot must (1) have been terminated for cause as a result of the disciplinary process in Section 21

[5] Former pilots who went onto LTD before February 1, 2004, qualify for the retiree medical plan, rather than the active-pilot medical plan. *See* section IV.C below; Stephens Decl. at ¶¶ 61, 64. The particular cases of First Officers Emery, Meadows and Preitz will be addressed below in section VII.

of the CBA and (2) be pursuing reinstatement. *Id.*; Stephens Decl. at ¶ 68.[6] The Committee decided to make TAG pilots fully eligible for a share of the equity distribution in the same way as active pilots. *Id.* This is consistent with APA's advocacy for these pilots' reinstatement to active status and with the fact that historically a substantial portion of pilots on TAG have been reinstated. *Id.*

G. The Treatment of Former TWA Pilots and Pilots Formerly Covered by Supplement B

Among others, two groups of pilots have claimed that the equity distribution scheme is unfair to them: former TWA pilots and pilots formerly covered by Supplement B.

1. Former TWA pilots

AMR acquired the assets of Trans World Airlines, Inc. ("TWA"), in April 2001 following its bankruptcy filing, and AMR transferred the assets to a newly established corporate entity called TWA LLC pending integration with American. To govern the integration of former TWA LLC pilots into the American workforce, the APA and the Company negotiated Supplement CC to the then-existing collective bargaining agreement, the 1997 CBA. Supplement CC modified Section 13 of the Green Book, which would have required that each TWA Pilot be placed on the Pilots' System Seniority List as of the date on which he or she actually commenced service at American.[7] Instead, Supplement CC

[6] To have TAG status, a pilot must either have a pending grievance that would result in his or her reinstatement if the pilot were to prevail or be participating in a program, such as a substance abuse program, that, if successful, would result in the pilot's reinstatement. McDaniels Decl. at ¶ 14 & n.3.

[7] Section 13 provides that "Seniority as a pilot shall be based upon the length of service as a flight deck operating crew member with the Company . . ," which corresponds to a pilot's Occupational Date and thus his or her seniority.

attempted to preserve TWA pilots' pre-merger career expectations by integrating 1,095 TWA pilots above the junior pre-transaction American pilot and granting preferential flying opportunities to former TWA pilots in the St. Louis domicile. *See* Mellerski Decl. at n.9.

After American filed for bankruptcy, it sought authority under Section 1113 of the Bankruptcy Code to abrogate the 2003 CBA, including Supplement CC, and announced its intention to close the St. Louis domicile. The bankruptcy court granted American authority to abrogate, and the Association and the Company agreed to Letter 12-05 as part of the new CBA. Letter 12-05 addressed the loss of protected flying in St. Louis under Supplement CC. *See* Mellerski Decl. at n.12. The letter provided that a panel of three neutral arbitrators would "establish certain terms of the CBA as a substitute for the loss of Supplement CC preferential flying opportunities in order *to resolve all issues* related to the impact on TWA Pilots of termination of Supplement CC." *See* LOA 12-05, APA Exh. 5 (emphasis added). In addition, because the seniority system was never the subject of the negotiations or litigation under Section 1113, the parties agreed that "TWA Pilots' existing seniority placements on the Pilots' System Seniority List are final and shall continue pursuant to Section 13 of the CBA." *Id.* In the meantime, American agreed not to close St. Louis until the arbitrators issued their award. *Id.* That award is not expected to be in final contractual language until August 29, 2013.

When the Equity Distribution Committee finalized its recommendations to the Board of Directors, the arbitration regarding Supplement CC had not yet begun. In the face of significant uncertainty regarding the future situation of former TWA pilots, the Committee endeavored to develop a system that treated those pilots fairly. *See* Mellerski Decl. at ¶¶ 31-34, 69-71, 76, 98.

First, in the Inverse Seniority Silo, the Committee used all pilots' system seniority, which is directly linked to their Occupational Date. *Id.* at ¶ 48. For former TWA pilots, Occupational Date was assigned through Supplement CC. McDaniels Decl. at ¶ 10. These pilots are therefore more junior, and have fewer years of service, than they would if their TWA date of hire was the relevant starting point.

On the whole, the use of Occupational Date in this Silo benefited former TWA pilots by providing them a larger payout than they would have received if the Committee had used their date of hire at TWA. *See* Mellerski Decl. at ¶ 33. The Inverse Seniority Silo, weighted 30%, assigns more money to junior pilots in order to compensate them, in part, for the loss of career advancement opportunities. *Id.* at ¶¶ 40-44. If the Committee had used former TWA pilots' date of hire at TWA, those pilots would appear more senior and therefore would have received a lesser payout from the Inverse Seniority Silo. *Id.*

On the other hand, many former TWA pilots received less from the Years of Service Silo than they would have received if years of service were measured from their TWA date of hire. But the Years of Service Silo is allocated 20 % of the distribution, or only two thirds the weight of the Inverse Seniority Silo. *Id.* at ¶ 20.

Meanwhile, the Pension Silo, based on the A Plan freeze, relies on credited years of service at American and salary projections. APA used the past pay of former TWA pilots to project future pay for that group. This approach benefited former TWA pilots by producing a larger payout than those pilots would have received if the Committee had not created a separate model for them. *Id.* at ¶ 69. By using past pay of former TWA pilots, the model gives these pilots the benefit of their history under Supplement CC—*i.e.,* higher pay based

on the fenced flying in St. Louis—thereby increasing the calculations of their future lost pension benefit and, consequently, their payout from the Pension Silo. *Id.* at ¶ 70.

Starting on January 1, 2023, the model assigns former TWA pilots the higher of the salary output for them under the separate former TWA model and under the general model. *See id.* at ¶¶ 69-71. This, again, benefits former TWA pilots by assigning them a higher salary projection. The date January 1, 2023 was meant to be a reasonable assumption about when the fences in Supplement CC might be eliminated based solely on retirements at age 65 and assuming no changes in the number or types of aircraft, that is a static fleet. *See id.* at ¶¶ 73, 76.

2. The A-Scale Pilots Under Supplement B

In November 1983, the APA and the Company entered into Supplement B that created what was intended to be a permanent "B Scale" in which newly hired pilots would receive lesser pay and benefits than pilots hired prior to Supplement B. (Pilots working prior to Supplement B are known as "A Scale" pilots; pilots hired after Supplement B became effective are known as "B Scale" pilots.) Stephens Decl. at ¶ 83. Supplement B had no duration clause and provided that "neither party will attempt to totally eliminate the existing differentials" in pay and benefits. *Id.* at ¶ 84. In particular, B Scale pilots received 50% of the A Scale hourly rates, greatly reduced minimum benefit under the A Plan, or defined benefit plan, and a 3% contribution to the B Plan or defined contribution plan, as opposed to the 11% earned by A Scale pilots. *Id.* at ¶ 85. (The terms "A Plan" and "B Plan" are entirely unrelated to the terminology arising from Supplement B.) *Id.* at ¶ 83.

Over time, APA was able to narrow the differentials, and, as a result of a Presidential Emergency Board in 1997, get the Company to agree to phase out the B Scale entirely by

August 2001. *See Id.* at ¶ 86. Supplement B remained in effect, as it provided that the Company promised that it would "take no action, by way of notice, negotiations or otherwise, to diminish the pay or retirement benefit programs in effect on" November 1, 1983. *Id.* at ¶ 84. In practice, however, all pilots have been on the same uniform benefit plans since 1991 and on the same pay scales since August 2001. *Id.* at ¶ 86.

After AMR declared bankruptcy in late 2011, a principal element of the Company's proposals to the APA was to terminate the A Plan. *See Id*. at ¶ 87. Obviously, outside of bankruptcy, this change would have been prohibited by the 2003 CBA for all pilots and, in addition for the A Scale pilots, by Supplement B to the 2003 CBA.

The APA was able to assemble support from other creditors in the bankruptcy to oppose the Company's attempt to terminate the A Plan.[8] *Id*. at ¶ 89. These creditors supported the APA's effort to preserve the A Plan, but only on the condition that pilots' ability to take their A Plan benefit as a lump sum would be permanently eliminated. *Id*. The lump sum option was already barred during bankruptcy by Section 436(d)(2) of the Pension Protection Act. *Id*. at ¶ 88. There was a widely held perception among the creditors and the Company that, if the A Plan were not terminated, keeping the lump sum distribution option

[8] A termination of the A Plan would also have taken away any claim for damages that the APA could have made based on changed to the pension plan and given that claim instead to the Pension Benefit Guaranty Corporation ("PBGC"). And, for reasons APA need not elaborate here, the actuarial calculation used by the PBGC would have greatly inflated the amount of that claim, massively diluting the claims of other unsecured creditors. It was largely for this reason that APA was able to assemble support opposing the Company's proposal to eliminate the A Plan.

would cause profound staffing problems when the Company emerged from bankruptcy.[9] *Id.* Indeed, the existence of a lump sum option at Delta was part of the reason for termination of the pilots' defined benefit plan during its bankruptcy. *Id.*

Because the lump sum distribution option is protected under Section 411(d)(6) of the Internal Revenue Code Section and Section 204(g) of the Employee Retirement Income Security Act ("ERISA"), a change in federal regulations was needed in order to allow the lump sum to be eliminated. *Id.* at ¶ 89. Working with the U.S. Treasury Department, the PBGC, and eventually the Company, APA obtained the ability to preserve the A Plan benefits accrued through November 1, 2012, by obtaining the bankruptcy court's permission to freeze the A Plan and eliminate the lump sum distribution option from the A Plan. *Id.* A freeze, versus termination of the A Plan, greatly benefitted the more senior pilots. *Id.*

H. Results

The Committee's work was not premised on producing any predetermined result and should be judged largely on the diligence and reasonableness of the Committee's process. However, payout calculations may be helpful in assessing the fairness of the equity distribution scheme. Several aspects of these calculations are notable.

[9] The Unsecured Creditors Committee asserted that the Debtors "have adduced sufficient evidence to support a finding that but for the elimination of the [Lump Sum Option], a termination of the Pilot Plan prior to emergence [from chapter 11] would be necessary because American would otherwise face mass retirements by American's pilots upon emergence" the consequences of which would "devastate the Company." UCC Response to Motion to Eliminate the Lump Sum, Doc. 5674 at 4.

First, the vast majority of pilots are expected to receive payouts within a relatively narrow range. More than four fifths of pilots are projected to receive between $100,000 and $140,000. Mellerski Decl. at ¶ 96.

Second, as indicated by the graph in APA Exhibit 44, the payout shows no bias for or against junior or senior pilots. Variation within any given seniority range is greater than variation between that seniority range and any other.

Third, as indicated by the graph in APA Exhibit 45, the payout shows no bias against former TWA pilots. When excluding the Pension Silo (because the pension harm of former TWA pilots cannot be fairly compared to the pension harm of the general pilot population), the payouts to former TWA pilots look virtually identical to the payouts to the general pilot population. Mellerski Decl. at ¶ 99.

II. Legal Standard

The Arbitrator must judge the APA's decisions concerning the equity distribution through the lens of the duty of fair representation. A union is deemed to violate that duty only when its conduct is "arbitrary, discriminatory or in bad faith." *Vaca v. Sipes*, 386 U.S. 171, 207 (1967). Given the fact that a union is deemed to represent a bargaining unit as a whole, and therefore a broad range of competing and conflicting interests, a review of its decisions is to be "highly deferential." *Air Line Pilots Ass'n, Int'l v. O'Neill*, 499 U.S. 65, 78 (1991). Indeed, it is to be presumed that union decisions "may have unfavorable effects on some members of the craft represented." *Steele v. Louisville & N.R. Co.*, 323 U.S. 192, 203 (1944); see also *Humphrey v. Moore*, 375 U.S. 335 (1964). In other words, "[t]he complete satisfaction of all who are represented is hardly to be expected." *Ford Motor Co. v. Huffman*, 345 U.S. 330, 338 (1953). In view of the wide range of interests a union is obligated to

represent, a reviewing tribunal is required to approach substantive examination of a union's performance in the same way that courts review the enactments of legislative bodies. *O'Neill*, 499 U.S. at 78. That "extremely deferential standard" precludes reviewing bodies from "substitut[ing] their judgment for that of the union, even if, with the benefit of hindsight, it appears that the union could have made a better call." *Neal v. Newspaper Holdings, Inc.*, 349 F.3d 363, 369 (7th Cir. 2003).[10]

In this regard, a union's conduct may be deemed "arbitrary only if, in light of the factual and legal landscape at the time of the union's actions, the union's behavior is so far outside a wide range of reasonableness . . . as to be irrational." *O'Neill*, 499 U.S. at 67 (quoting *Huffman*, 345 U.S. at 338). As the Supreme Court has further held, "This wide range of reasonableness gives the union room to make discretionary decisions and choices even if those judgments are ultimately wrong." *Marquez v. Screen Actors Guild, Inc.*, 525 U.S. 33, 45-46 (1998).

In order to constitute "discriminatory" conduct, a union must have done far more than differentiate among and between groups – a task a union is frequently forced to

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[10] While the duty of fair representation is a fiduciary duty, *Air Line Pilots Ass'n, Int'l v. O'Neill,* 499 U.S. 65, 74 (1991), it is well to remember Justice Frankfurter's observation that to "say that a man is a fiduciary only begins analysis" and begs the question about the nature of the duty in the particular legal context. *Securities and Exchange Comm'n v. Chenery,* 318 U.S. 80, 85-86 (1943). APA represents a collection of competing and divergent interests, *cf. United States v. Jicarilla Apache Nation,* __ U.S.__, 131 S.Ct. 2313, 2328 (2011) (recognizing that, although the government owed a fiduciary duty, it had conflicting obligations to different tribes and individuals), and it is precisely because of this intense conflict that the fiduciary duty in the fair representation context is significantly more forgiving than the monoptic duty of an ERISA fiduciary. *Compare Air Line Pilots Ass'n,* 499 U.S. at 78, *Humphrey v. Moore,* 375 U.S. 335, 349 (1964), and *Ford Motor Co. v. Huffman,* 345 U.S. 330, 338 (1953), *with NLRB v. Amax Coal Co.,* 453 U.S. 322 (1981).

undergo in any case – but to have done so in a manner and for reasons that are "intentional [and] severe" and "unrelated to legitimate union objectives." *Amalgamated Ass'n of St., Elec. Ry. & Motor Coach Employees*, 403 U.S. 274, 301 (1971). Consequently, in order to "discriminate" for the purposes of the duty of fair representation, a union must differentiate between and among groups of workers on the basis of such prohibited factors as race, gender, union membership or status as a union dissident. *Jeffreys v. Commc'ns Workers of America*, 354 F.3d 270, 275 (4th Cir. 2003); *Ramey v. District 141, IAM*, 378 F.3d 269, 277 (2d Cir. 2004).

Finally, in order for a union to be said to have engaged in bad faith conduct, there must be "substantial evidence of fraud, deceitful action or dishonest conduct." *Lockridge*, 403 U.S. at 299; see also *Vaughn v. Air Line Pilots Ass'n, Int'l*, 604 F.3d 703, 709-10 (2d Cir. 2010) (engaging in "fraud, dishonesty, [or] other intentionally misleading conduct" with "an improper intent, purpose, or motive") (quoting *Spellacy v. Airline Pilots Ass'n, Int'l*, 156 F.3d 120, 126 (2d Cir. 1998) (internal citations, quotations omitted)).

III. The Selection, Methodology, and Weighting of Silos was not Arbitrary, Discriminatory, or in Bad Faith

In developing the equity distribution, the APA adopted a "forward looking" perspective, considering harms expected to result from concessions in the 2013 CBA, starting on the effective date of that agreement, January 1, 2013. But the Association recognized that the exact impact of these concessions was impossible to predict, and so it created a silo system to roughly account for broad categories of damages. Many of the challenges to the silo system dispute this fundamental approach, explicitly or implicitly. Because that approach was wholly reasonable, these challenges must be denied.

After establishing the reasonableness of two fundamental APA decisions—the use of a "forward looking" approach and the refusal to speculate as to the exact extent of damages—this Section rebuts challenges to the specific silo methodologies, the proration of two silos based on mandatory retirement, and the allocation of funds between the silos.

A. It was Reasonable for the APA to Construct the Silo System Using a "Forward Looking" Approach Considering Harm from CBA Concessions in the 2013 CBA

It is fundamental to the APA equity distribution scheme that the distribution focuses on harms incurred by pilots as a result of the 2013 CBA, the agreement in which the APA received the Equity Stake, beginning on the effective date of that agreement, January 1, 2013. Several challengers have asserted that the APA should use the equity distribution to compensate pilots for harms incurred prior to that date, looking back to concessions made ten years ago, in the 2003 CBA, or to the extensive furloughs beginning in 2001. Other pilots contend that the relevant period should date to the beginning of the AMR bankruptcy or to the abrogation of the APA's collective bargaining agreement in September 2012.

The APA's decision to focus on the term of the 2013 CBA was not arbitrary, discriminatory, or in bad faith. The APA received the Equity Stake as part of a comprehensive collective bargaining agreement in which the Association agreed to many concessions and received the equity in exchange. As in similar pilot union monetary distributions, it was reasonable for the union to use the equity as a way of mitigating the impact of those concessions. *See, e.g., Bondurant v. Air Line Pilots Ass'n*, 679 F. 3d 386, 392-93 (6th Cir. 2012) (rejecting a challenge to the eligibility cut-off date for distribution of a

bankruptcy claim because the union reasonably matched eligibility to a prospective estimate of time to be worked during the term of the concessionary contract).[11]

It would have been impossible for the APA to consider all past harms incurred by American Airlines pilots. Measuring ten years of harm, going back to the 2003 CBA, would have been an extraordinarily difficult task. Moreover, if the APA had decided to consider past harm, there would be no logical stopping point. For example, prior to the 2003 CBA, many pilots were furloughed after the terrorist attacks of September 11, 2001. And in 1983, the APA agreed to create the "B-scale," a group of pilots who received lesser pay and benefits. Was APA required to consider all of these harms in the equity distribution?

The APA also acted reasonably in rejecting the start of the AMR bankruptcy as a reference point. The bankruptcy had no immediate effect on pilots' terms and conditions of employment, with one exception: by law, the pension plan could no longer offer a lump sum. Aside from that change, the full 2003 CBA was still in effect until the court authorized abrogation. And the elimination of the lump sum in bankruptcy was not tied to CBA negotiations that ultimately led to the Equity Stake.

A slightly more logical suggestion is that the equity distribution should consider harms starting on September 5, 2013, when American received court authority to abrogate the 2003 CBA. But there are several reasons why it was not irrational or unfair for the APA to choose a different reference point. For one thing, most of the CBA changes did not take

[11] In assessing the reasonableness of the APA's equity distribution scheme, the Arbitrator may consider evidence of practice among other unions as an indication that the APA's adoption of the same practice was reasonable. *Cf. Bernard v. McLean Trucking Co.,* 429 F. Supp. 284, 287 (D. Kan. 1977) (finding a union's conduct reasonable where the union relied on prior industry practices).

immediate effect; indeed, many had still not taken effect as of January 1, 2013.[12] In any case, abrogation itself did not guarantee the APA any equity stake. To the contrary, while the APA could have requested an unsecured claim arising from the abrogation, the prospects for success in the resulting litigation would have been minimal given adverse precedent in the jurisdiction of the bankruptcy. *See In re Northwest Airlines Corp.*, 366 BR 270 (Bankr. S.D.N.Y. 2007) (holding that the Second Circuit's decision in an earlier appeal in the Northwest bankruptcy "expressly excludes the possibility of damages for the lawful rejection of a collective bargaining agreement pursuant to § 1113").

It was only the 2013 CBA that ensured that APA would receive the Equity Stake. Consequently, it was rational for the APA to use the start of the 2013 CBA as the reference point for determining eligibility and distribution methodology. For example, in prior cases, unions have defeated challenges to settlement distributions that included only pilots employed as of the date of the settlement, even if the damages claimed by the union started before that date. *See, e.g., Steelworkers Local Union No. 2869*, 239 NLRB 982 (1978) (holding that it was reasonable for a union to limit distribution of a settlement to pilots employed as of the date of the settlement, even though the harm occurred in part prior to that date); *Jordan v. Nat'l Postal Mail Handlers Union, Local 300*, 2007 WL 4947823 (E.D.N.Y. Dec. 28, 2007) report and recommendation adopted, 2008 WL 465503 (E.D.N.Y. Feb. 15, 2008) (reaching a similar conclusion on analogous facts).

[12] For example, many significant work rules changes were set to be phased in over a period of years, and American did not seek to take advantage of most of the changes to the Scope clause prior to January 1, 2013. Stephens Decl. at ¶ 27.

B. It was Reasonable for the APA to Spurn the Impossible Task of Precisely Measuring Speculative Future Harms

There is a second critical basis for the silo construction and allocation: The APA decided that, although it would consider the harm expected to result from the 2013 CBA, the equity distribution could not be based on an attempt to exactly predict the magnitude of that harm or its distribution across the pilot group. Instead, like pilot unions at Delta and Northwest, the APA adopted a silo system to loosely account for broad categories of expected damages.

Many challenges are premised on the notion that the APA should have been more precise in measuring the harms associated with the 2013 CBA and in designing the equity distribution scheme to mitigate those harms. But, for the most part, these harms have not yet occurred (and had not occurred at all when the Committee started its work on the equity distribution scheme). These harms are incredibly difficult to predict, with projections varying based on assumptions about future business decisions of American, trends in the airline industry, pilot behavior, and many other factors. While the Equity Distribution Committee carefully considered all available data, the APA was justified in declining to make the equity distribution scheme dependent solely on a series of guesses about the future effects of dozens of different concessions in the 2013 CBA. Instead, the APA's silo system roughly accounts for a variety of different harms without attempting to value particular changes or predict the impact on particular individuals.

Neither the APA nor any challenger has located precedent in which a union was found to have breached the duty of representation because, like the APA, it declined to distribute a settlement or other lump sum in accordance with a precise calculation of

damages. Indeed, in an analogous context, courts have expressly held that such an approach is not required. In assessing the APA's decision, the Arbitrator may look for guidance to the body of case law in which federal courts have assessed proposals for distributing the proceeds of class action settlements. In that context, proposed settlement distributions must be "fair, reasonable, and adequate." Fed. R. Civ. Proc. 23(e)(2); *In re Agent Orange Prod. Liab. Litig.*, 611 F. Supp. 1396, 1402 (E.D.N.Y. 1985), *aff'd in relevant part*, 818 F.2d 179 (2d Cir. 1987). Because the duty of fair representation imposes a similar, but lesser, standard, a monetary distribution that would pass muster in the class action context must also pass muster in the fair representation context.

Although class action settlements are often distributed in proportion to the harms suffered by class members, courts have recognized that a distribution need not adopt this approach because "equity in such a simple sense" may be "unattainable in complex cases." *Int'l Union, United Auto., Aerospace, & Agr. Implement Workers of Am. v. Gen. Motors Corp.*, 497 F.3d 615, 629 (6th Cir. 2007) (quoting *Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 855, 119 S.Ct. 2295, 144 L.Ed.2d 715 (1999)). Indeed, courts reject methodologies that attempt to quantify class members' specific harms where those harms are speculative or difficult to measure. *Agent Orange*, 611 F. Supp. at 1402-3, 9-10 (holding that damages were "far too speculative to serve as the primary basis for a distribution plan").[13]

Rather than pursuing "mathematical precision" in these cases, courts recognize that "the requirements of efficiency and administrability undoubtedly would permit alternative

[13] For example, in a suit based on exposure to a dangerous chemical, it was reasonable to provide the same payout to every exposed class member who later suffered a similarly severe disability, regardless of the individual's degree of exposure or the probability that the disability was caused by the chemical. *Agent Orange*, 611 F. Supp. at 1410-1415.

methods of disbursement." *See In re PaineWebber Ltd. Partnerships Litig.*, 171 F.R.D. 104, 133 (S.D.N.Y. 1997), *aff'd sub nom.*, 117 F.3d 721 (2d Cir. 1997). The values of simplicity, transparency, and ease of administration will often outweigh the notion that settlement distributions should precisely mitigate class members' damages. *Id.* at 135 (rejecting arguments that a distribution scheme should account for the relative strength of class members' claims, citing "ease of administration" and the avoidance of a "costly, speculative and bootless comparison" between the claims). Distribution schemes should "minimize transaction costs, be relatively easy to administer and involve relatively simple, understandable and objective" methodologies. *Agent Orange*, 611 F. Supp. at 1410. In addition, a distribution scheme may reasonably aim to "minimize[e] discord within the class where possible," even at the expense of a more sophisticated distribution methodology. *Id.* at 1415. *Cf. In re Warfarin Sodium Antitrust Litig.*, 391 F.3d 516, 539 (3d Cir. 2004) (approving a class action distribution that included class members who suffered no damage at all).

Here, the APA's situation is considerably more complex than that of typical class action settlement distribution. The Equity Stake did not arise as compensation for the settlement of a defined claim or set of claims by the APA or its members. Rather, the APA received the Equity Stake as part of a comprehensive collective bargaining agreement in which the Association waived "any and all claims APA has or might arguably have, on behalf of itself or the pilots represented by APA" under the Railway Labor Act or with respect to the abrogated collective bargaining agreement." See LOA 12-01, APA Exh. 5. Furthermore, while the parties generally understood the Equity Stake to be connected to the concessions in the 2013 CBA, the negotiation over the Equity Stake did not center on valuations of those concessions.

Nevertheless, the APA reasonably decided to use the equity distribution as a way of roughly mitigating the future impact of the concessions in the 2013 CBA. But there was no precise way to predict that impact, for all of the reasons described above and in the Declaration of Mark Stephens. Consequently, the APA was justified in adopting an approach based, like the settlement allocation in Agent Orange, on a general accounting of possible harm rather than on specific prognostications.

C. It was Reasonable for the APA to Distribute the Equity in Part Through the Inverse Seniority Silo

The APA reasonably determined that many of the concessions in the 2013 CBA, though affecting all pilots, would disproportionately harm junior pilots. In particular, changes to work rules and Scope would make it harder for junior pilots to advance to more lucrative positions. Consequently, the Association created the Inverse Seniority Silo, in which junior pilots would receive a greater payout than senior pilots. In doing so, the APA did not act arbitrarily, discriminatorily, or in bad faith.

Some challengers do not target the existence of the Silo but rather the methodology for distributing equity within that Silo. But the methodology, though necessarily imperfect, was far from irrational. In the Inverse Seniority Silo, the most junior eligible pilot receives twice the distribution of the most junior pilot, and the distribution to every pilot in between is filled in proportional to his relatively seniority.

First, it was reasonable for the union to opt for a simple linear scale rather than a more complicated scheme. Given the significant uncertainty in measuring contract damages—uncertainly only heightened in the uncertain realm of career stagnation—there was no guarantee that a more complex scheme would have ultimately been any more

accurate. Given the limited benefit, it was reasonable for the APA to choose a system that was simpler and therefore more transparent.[14]

The APA was also justified in choosing a 2-to-1 scale for the Silo, given the roughly 2-to-1 relationship between the highest and lowest of average pilot pay. The 2-to-1 scale was also in line with the methodology used by other pilot unions in similar situations.

Furthermore, it was not irrational for the APA to include even the most senior pilots in the payout from the Silo. For example, Challenger Brian Smith argues that the APA should have started "the curve at zero," therefore giving no payout to the most senior pilot and giving extremely small payouts to other senior pilots.[15] The Committee considered and reasonably rejected this approach for several reasons. On a linear 0-to-1 scale, a junior pilot with seniority number 8000 would receive a distribution *eighty times* larger than the payout to the pilot with seniority number 100. It was reasonable to reject that result, particularly because even a senior pilot may nevertheless be junior to others in his bid status. Moreover, the combined effect of productivity and outsourcing changes will result in fewer trip options in every bid status, even for the pilot with the lowest seniority numbers. As Mr. Smith

[14] The alternative system proposed by Brian Smith illustrates the problem of complexity. Mr. Smith suggests a "point system to more accurately reflect the non-linear relationship where the top 75% of Group 4 Captains (line holding) score a zero, and scores gradually increase to 2 for the bottom 25% of Group 2 First Officers (reserve pilots)." Even in this broad sketch, the system seems difficult to understand. Mr. Smith later acknowledges that a precise version of this methodology would require a projection of pilots' "actual progression" in aircraft group and seat for each pilot over the next six years. But that projection alone would require an extremely complicated model that would likely be very imprecise.

[15] Challengers who make similar arguments include Eric Dean (Challenges 62 and 63), John Reynolds (Challenge 1097), and Kenneth Wuttke (Challenge 1143).

suggests through his alternative proposal, the only reasonable way to accomplish the objective of denying a payout to the most senior pilot would be to adopt a non-linear scale; as discussed above and in footnote 14, this would add enormous complexity to the model.

It is also worth noting that, while some challengers contend that the Inverse Seniority Silo should be more heavily weighted towards junior pilots, other challengers say that the Silo's methodology is unfair to senior pilots.[16] As the representative of all pilots, the APA had to balance these competing concerns, and it did so reasonably.

D. It was Reasonable for the APA to Distribute the Equity in Part Through the Per Capita Silo

Few challengers complain about the Per Capita Silo. Indeed, many pilots argue that the equity distribution should be entirely per capita.

As suggested by this pattern of challenges, the APA acted reasonably in including the Per Capita Silo. The Association understood that the impact of many contractual concessions would be spread across the pilot workforce to a roughly equal degree or would depend on future events, like a pilot's disability status, that could not be anticipated at the time of distribution. For similar reasons, pilot unions at Delta and Northwest also included a per capita silo.

The sole challenge to the methodology in the Per Capita Silo is based on a misunderstanding of the equity distribution scheme. Kenneth Wutke's challenge argues that changes to work rules disproportionately affect junior pilots by making it difficult for them

[16] For example, Larry Scerba's challenge (number 1164) claims that "APA's decision to distribute the scope-related equity on a 1:2 basis, with the most junior pilots receiving twice as much as the most senior pilot, is arbitrary, discriminatory, and bad faith conduct intended to disadvantage the minority group of AA's most senior pilots solely to advantage the membership majority of junior pilots."

to claim favorable trips and to advance to more lucrative positions. The APA agrees, which is why it created the Inverse Seniority Silo to account for these sorts of harms. But other aspects of the work rules changes affect all pilots, such as the obligation to perform increased flying. Moreover, the Per Capita Silo aims to mitigate harm from other contractual changes, such as the increased costs of active medical coverage. Mr. Wutke does not appear to dispute the importance of these changes or their roughly equal impact across the pilot group.

E. It was Reasonable for the APA to Distribute the Equity in Part Through the Years of Service Silo

The APA reasonably determined that the impact of many contractual concessions is closely linked to pay, age, or various measures of length of tenure at American. Rather than create separate silos for each of these factors, the APA recognized that all were correlated with years of service, *i.e.,* years since a pilot's Occupational Seniority Date. The APA therefore chose to create a single Years of Service Silo.

In choosing this approach, the APA gave significant weight to two of its guiding principles: the value of simplicity and the impossibility of creating any exact measure of damages. In light of these principles, it was reasonable for the APA to create a silo that employed a straightforward methodology that generally, though imperfectly, correlated to a variety of contractual harms. This approach is in line with class action allocation cases in which judges have favored "relatively simple, understandable, and objective" measures in place of complex attempts to predict uncertain harms. *See, e.g., Agent Orange*, 611 F. Supp. at 1410.

In creating the Years of Service Silo, the APA reasonably balanced the interests of subgroups within its membership, including senior pilots. The concern of this demographic is evidenced by the more than twenty challenges alleging that, despite the existence of the Years of Service Silo, the equity distribution scheme is unfair to senior and older pilots. It was reasonable for the APA to create at least one silo out of four that favored senior pilots. Notably, pilot unions at Northwest and Delta utilized silos that were weighted towards senior pilots.

Some challengers raise objections to the methodology in the Years of Service Silo. For example, some pilots argue that the impact of two of the harms associated with this silo, loss of the lump sum[17] and loss of retiree medical, depends on age rather than years of service. The APA agrees but determined that years of service was a reasonable proxy for age.

Brian Smith also argues that compensation harm is not linked to seniority because "these losses are shared equally on a percentage basis." This is both incorrect and misses the point. It is incorrect because senior pilots are better able to take advantage of various premiums, particularly the international premium, and therefore are more affected by the elimination of these premiums. But even if the harms were "shared equally on a percentage basis," *e.g.,* each pilot's pay decreased by 5%, the absolute impact would still be greater on those pilots whose pay under the 2003 CBA was highest: senior pilots.

[17] The Declaration of Michael Mellerski explains why loss of the lump sum was a real harm, separate and apart from the harm covered by the Pension Silo. *See* Mellerski Decl. at n. 6. Several challengers agree. Challenge 1143 states, "[t]here is no doubt that the loss of the lump sum affected the pilot group," and Challenge 1177 states, "[t]his loss of lump sum hurts us all, but could be argued it affects the older pilots much more because of less time to make up this loss."

Mr. Smith concedes that the impact of lost vacation is directly connected to years of service and suggests that the APA should have attempted to calculate monetary damages for each pilot associated with this change. But the APA properly rejected the approach of valuing each and every change to the CBA, and in any case, assigning a monetary value to a lost week of vacation is far from a straightforward task.

F. It was Reasonable for the APA to Distribute the Equity in Part Through the Pension Silo

The challengers seem to agree that the APA was wise to include a silo mitigating the impact of the freeze of the defined benefit pension plan, or A Plan. Indeed, some pilots think a much larger portion of the distribution should have been used for that purpose. (For a discussion of why the APA's silo allocation decision was reasonable, *see* pages 42-43 below.)

The Declaration of Michael Mellerski discusses the model used in the Pension Silo at length, and that discussion makes clear that the model was reasonable. Here, the APA responds to specific challenges to the methodology.

First, some pilots have noted that the model assigns outcomes based on the harm expected to be incurred by a "generic pilot" with a given age and seniority.[18] In other words, the model generally does not attempt to account for the individual circumstances of pilots (although it does utilize pilots' pension credited service). This is consistent with the APA's overall approach of declining to take on the impossible task of predicting the specific harms to be incurred by specific pilots, an approach that has been validated by courts allocating the proceeds from class action settlements. *See supra* at 30-33

[18] Challenges 1143 and 1196 target this aspect of the Pension Silo.

There are further reasons why a more tailored methodology would have been suspect. The goal of the Pension Silo is to predict the size of the benefit that pilots would have received under the A Plan if the A Plan had not been frozen. That benefit would have been determined based on pilots' earnings during their last five years of work at American. But of the many factors that could influence a pilots' future earnings, only seniority can be predicted with any reasonable level of confidence. Other factors are based largely on pilots' preferences and behavior, *e.g.,* whether a pilot will choose to upgrade to a more lucrative aircraft or seat, even if it means flying out of a different base or sacrificing quality of life. As demonstrated in the Declaration of Michael Mellerski, any attempt to predict an individual's future pay based on the individual's current pay could be characterized as unfair to some group of pilots. And any attempt to calculate a pilot's benefit from the frozen A Plan could be seen as similarly unfair.[19]

Another challenge claims that the model in the Pension Silo should have assumed that furloughed pilots would receive credit under the A Plan for their time on furlough. But the A Plan, by its terms, does not give such credit, and it is unclear whether furloughed pilots will receive it. Although the APA has negotiated in the past for specific groups of furloughed pilots to receive pension credited service for time on furlough, the existing group of affected pilots is very large and the Company would place a high value on a possible change.

[19] Challenge 51 is simply incorrect when it says that the model in the Pension Silo does not account for the frozen A Plan benefit. Like the other elements of the model, a pilot's frozen benefit is calculated based on the pilot's age, seniority, and pension credited service.

G. It was Reasonable for the APA to Prorate Two Silos for Pilots Who Are Required to Retire during the Term of the 2013 CBA

Some pilots complain that the APA should not have prorated the Inverse Seniority Silo and Per Capita Silo for pilots who will be legally required to retire during the term of the 2013 CBA. But the APA's proration decision was entirely reasonable. As discussed above, the APA did not breach its duty of fair representation when it decided that the equity distribution should aim to mitigate harms arising from the concessions in the 2013 CBA. The term of that agreement is January 1, 2013 to January 1, 2019. Consequently, the APA was justified in providing a lesser distribution to pilots who were legally required to leave active service for a portion of that period.[20]

The APA did not engage in age discrimination by considering the legal retirement age in its decisions. *See, e.g., Criley v. Delta Air Lines*, 119 F. 3d 102, 105 (2d Cir. 1997) (holding that consideration of "the business effects of the federally mandated retirement age" are distinct from "assumptions about employees' abilities based on their age" and do not constitute age discrimination). On similar facts, the Sixth Circuit upheld the decision of the Northwest pilot union to prorate a monetary distribution based on projected retirement at the mandatory retirement age. *Bondurant v. Air Line Pilots Ass'n*, 679 F.3d 386, 396 (6th Cir. 2012).

The APA prorated the Inverse Seniority Silo and Per Capita Silo because those silos correspond to harms incurred exclusively during a pilot's active service. In contrast, the Years of Service Silo accounts for loss of retiree medical coverage and the lump sum option

[20] No challenger contends that Congress will alter the mandatory retirement age during the term of the 2013 CBA.

in the pension plan, while the Pension Silo mitigates harm arising from the freeze of the pension plan. These harms occur after retirement. Consequently, it was reasonable for the APA to prorate two Silos, but not all four.

One challenger has urged a more complicated proration formula for the Inverse Seniority Silo, noting that some work rules changes do not take effect immediately, so that a pilot retiring after three years under the contract might be less than half as affected as a pilot who works through the entire term. But while a more complicated formula *might* have been more accurate, it would have added significant complexity and might have missed the mark in any case. After all, aside from work rules, a significant factor in the Inverse Seniority Silo was Scope changes. These changes took effect immediately and will have consequences over time that are impossible to predict because they depend on the Company's business decisions with respect to outsourcing.

H. The APA's Weighting of the Silos was Reasonable

Several challengers claim that the allocation of funds between the silos should be readjusted. Although there were many possible ways in which the silos could have been weighted, the allocation adopted by the APA was within the "wide range of reasonableness" afforded to unions under the duty of fair representation. *O'Neill*, 499 U.S. at 67. As argued extensively at pages 30-33 above, the APA made a reasonable decision not to base the allocation on an attempt to exactly measure damages associated with different silos. A proportional distribution of that kind was not required, even under the higher standard applicable in the class action settlement context. Indeed, the APA likely would have withstood legal challenges under the duty of fair representation even if it had adopted a purely per capita distribution, *i.e.,* a 100% weighting to the Per Capita Silo. The Association

should not be penalized for taking on the more difficult task of utilizing several silos in its distribution—a decision that necessitated a difficult decision regarding the weighting between the silos.

The most common challenge to the APA's silo weighting is that the Pension Silo should have been weighted more heavily because the freeze of the A Plan represents more than 30% of the harm that pilots will incur as a result of the concessions in the 2013 CBA. But even assuming that the APA was obligated to allocate between the silos in proportion to predictions of harm, this argument is based on invalid data. In particular, challengers seem to be comparing predictions of harm from non-pension concessions during the term of the 2013 CBA, *i.e.,* until January 1, 2019, with predictions of harm from the freeze of the A Plan during the entire future careers of all active pilots, *i.e.,* more than thirty years into the future. This comparison arises in part from slides prepared by Lazard to describe the magnitude of various types of contractual harm. As explained in the Declaration of Andrew Yearley from Lazard, those slides were not consistent in the time frames used in measuring harms from freeze of the pension plan as compared to the other concessions.

The Committee decided instead to use more comparable time frames: a six year term for most contract concessions but a twelve year term, the average remaining career of pilots at American, for the freeze of the A Plan. This produced a calculation indicating that 33% of the harm was associated with the pension freeze. But the Committee would have been justified in measuring the impact of the freeze over a six-year period, like the other concessions, in which case the pension damages would have been an even smaller proportion.

I. The Silo Structure Did Not Constitute Discrimination Against Junior or Senior Pilots

Some pilots have claimed that the equity distribution scheme is unfair to senior pilots, while others have claimed it is unfair to junior pilots. To prevail in showing discrimination, these pilots must prove not only that they were treated differently but that discrimination was intentional, severe, and unrelated to legitimate union objectives. *See supra* at 26.

No pilot has produced any direct evidence of this kind of discrimination against any seniority group. Instead, the evidence suggests that the Committee's process was not biased towards any seniority group. A powerful indicator of this is the membership of the Committee, which included pilots who were very senior (Doug Pinion, seniority number 311) very junior (Dave Quinlan, seniority number 6476). Similarly, the ages of Committee members range from 49 to 59.

Moreover, the projected payouts to pilots are graphed against their seniority, there is no pattern favoring junior or senior pilots. The variation within any given seniority range exceeds the variation between that seniority range and any other. To the extent that the payout data shows peaks or valleys, this is a product only of the reasonable assumptions and methodology employed by the Committee.

IV. The APA's Eligibility Decisions Were Not Arbitrary, Discriminatory, or in Bad Faith

A. The APA Acted Reasonably in Excluding Pilots Who Retired Prior to January 1, 2013, as These Pilots Were Not Affected by the Concessions in the 2013 CBA

One challenger complains that APA should have allowed pilots to receive a share of the equity even if the pilots retired prior to January 1, 2013, the effective date of the

agreement by which APA received the equity. The challenger, Stephen Cox, retired on November 1, 2012, during the period that APA had no collective bargaining agreement with the Company and no right to the Equity Stake.[21] The Association had advised pilots as early as July 2012 that, if they retired prior to the date on which APA obtained the equity, they would not receive a payout. Stephens Decl. at ¶ 49 and APA Exh. 36.

The APA was justified in excluding pilots who retired prior to the date that the APA received the Equity Stake. First, retired pilots are no longer employees of the Company and thus not persons to whom the union owes a duty of fair representation. *See, e.g., Allied Chem. & Alkali Workers, Local 1 v. Pittsburgh Plate Glass Company*, 404 U.S. 157 (1971). At the time that the APA received the equity, the Association owed no duty to Mr. Cox or to others who had retired.

Second, as argued extensively above, the APA reasonably decided to use the term of the 2013 CBA as the reference period for determining eligibility and methodology. Under this "forward looking" approach, payouts were inappropriate for pilots who left the employment of the Company prior to January 1, 2013, whether through retirement, resignation or termination. These pilots were simply unaffected by the concessions in the 2013 CBA.

The decision to exclude retirees was particularly reasonable because changes to retiree benefits are subject to Section 1114 of the Bankruptcy Code, 11 U.S.C. § 1114. A committee of retired American employees is litigating on behalf of all such pilots to oppose

[21] Indeed, this pilot retired before the A Plan freeze took effect on November 1, 2012, and well before the effective date of the 2013 CBA.

termination of coverage and, if coverage is terminated, to secure a separate bankruptcy claim.[22]

B. The APA Acted Reasonably in Excluding Pilots Who Chose Not to Return from Furlough

Several challengers say that the equity distribution scheme is unfair to pilots on furlough. Some of these challenges specifically complain that the distribution excludes pilots who were offered recall but exercised their contractual right to decline to return, or "defer recall." Under the contract, furloughed pilots can remain in this "deferred" status indefinitely.

As an initial matter, the APA maintains that it has no duty of fair representation to any furloughed pilot who has disclaimed a present intention to return from furlough to American, including pilots who intend to remain employed at US Airways. It is immaterial that these pilots may change their mind in the future.

In any case, the APA's decision to exclude certain furloughed pilots from the distribution was not arbitrary, discriminatory, or in bad faith. Furloughed pilots are not currently affected by the concessions in the 2013 CBA for the simple reason that they are not working at American Airlines. And furloughed pilots may never be affected by those concessions because they may never return to American. Indeed, many furloughed pilots do not return. McDaniels Decl. at ¶¶ 18-19 & n.4. Many of these pilots have established careers

[22] *See AMR Corp. v. Committee of Retired Employees,* Adv. Pro. No. 12-1744 (SHL) (Bankr. S.D.N.Y.). APA elected not to represent retired pilots in the bankruptcy court, precisely because it did not owe them a legal duty and the assumption of that duty would have created innumerable conflicts between active and retired pilots over their benefits, the retired pilots' entitlement to vote in the event of a new proposed collective bargaining agreement, and the distribution of any equity received.

at other airlines or in other fields of work. *Id.*[23] The APA was not obligated to reduce the equity payout to working American pilots in order to provide equity to pilots who might never return to American, many of whom now work for competitors.

The APA's decision was particularly reasonable because all pilots on furlough have now been offered an opportunity to return to American—meaning that any pilot who remains on furlough made a voluntary choice not to return. Every furloughed pilot at American was offered recall by May 6, 2013, and every pilot who accepted recall by that date has been scheduled for a training class. McDaniels Decl. at ¶ 16. Pilots who have chosen not to accept recall are particularly unlikely to return in the future. See McDaniels Decl. at ¶¶ 18-19.

In a case similar to this one, the Northern District of Illinois held that it was reasonable for the pilot union at United to exclude furloughed pilots from a monetary distribution. *Hudson v. Air Line Pilots Ass'n Int'l*, 415 BR 653 (N.D. Ill. 2009). As the court noted, the union was legitimately concerned that it had "no way of knowing which

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[23] *E.g.,*

> **From:** Kruczko, Serge [mailto:Serge.Kruczko@jetblue.com]
> **Sent:** Tuesday, June 11, 2013 3:52 PM
> **To:** Myers, Mark R.
> **Subject:** Motion to Dismiss certain Challenges
>
> To whom it may concern, I am in opposition for the APA to dismiss certain challenges, particularly pilots unable to return by the end of the SQP upon exercising their right of deferral under letter T

APA Exh. 54 (Serge Kruczko's correspondence regarding his challenge from a JetBlue email account).

furloughed pilots ultimately would accept recall." *Id.* at 661. Consequently, the union had "rational reasons for treating differently furloughed pilots who had not accepted recall as of United's exit from bankruptcy." *Id.* at 663.

Letter T does not alter this analysis. That letter provides that pilots "may defer recall to American Airlines for three (3) years after the last pilot with recall rights is notified of recall." Letter T does not provide, however, that a pilot who has deferred recall must be treated the same as an active pilot in every respect. A pilot who has actually returned to active service at American is not similarly situated to a pilot who merely retains a right to return. The APA was entitled to treat these distinct cases differently.

Furthermore, the APA did not act irrationally in concluding that it could not hold a reserve of funds to distribute to pilots who actually returned from furlough after the end of the Supplementary Qualification Period. For several reasons, a holdback of this kind was legally and logistically unworkable. *See supra* at 7.

The Hudson Court directly addressed a similar decision by another pilot union. There, as here, the union decided not to hold back money for returning furloughees due primarily to tax concerns. *Hudson*, 415 BR at 661. The court found that the union's decision did not breach the duty of fair representation. *Id.*

For all of the reasons above, it was reasonable for the APA to exclude furloughed pilots now working at US Airways. These pilots note that they will be governed by a version of the 2013 CBA after the merger of American and US Airways. But, for these pilots, the 2013 CBA is not concessionary at all—in fact, it represents a vast improvement over the terms and conditions of employment at US Airways. Stephens Decl. at ¶ 60. Moreover, an equity payout to US Airways pilots would constitute a form of double dipping because these

pilots will presumably receive a share of the $40 million lump sum provided to the US Airways pilot union as part of the merger agreement. *Id.*

C. The APA Acted Reasonably in Providing Payouts to Former Pilots Receiving Long Term Disability Benefits

APA is treating pilots on the Long Term Disability plan as active pilots, eligible for all four silos, if they were still on the American Airlines Pilots' System Seniority List as of January 1, 2013. The same is true for pilots on Sick Leave of Absence and Unpaid Sick Leave of Absence, who are generally waiting to quality for LTD. The APA acted reasonably in making this inclusive decision because pilots on LTD, SLOA, or SLOA do not choose to take that status, and because most of these pilots are trying to return to flying as active employees.

Five years after exhausting sick leave, a sick or injured pilot falls off the Pilots' System Seniority List. *See* McDaniels Decl. at 24. Because these pilots have no right to return to active service at American, the APA reasonably decided not to treat them as if they were active pilots. However, APA decided that these pilots should be eligible for one or two silos, so long as they were receiving disability benefits as of January 1, 2013.[24]

The eligibility criteria created by the APA are a reasonable attempt to match these pilots' payouts to the actual harm they may experience as a result of the 2013 CBA. Pilots who began receiving disability benefits prior to February 1, 2004, receive their medical coverage from the retiree medical coverage provided under the A Plan; pilots who began

[24] For a variety of institutional reasons, unions will frequently take actions to protect benefits or groups that are no longer within the scope of their legal duty. *See, e.g., Pittsburgh Plate Glass,* 404 U.S. 157, 182 n.20 (1971); *Int'l Union, United Auto Workers v. Yard-Man, Inc.,* 716 F.2d 1476 (1983).

receiving disability benefits after that date receive the same medical coverage as active pilots. Because this second group of pilots was harmed by changes to the active medical plan, but the first group was not,[25] the APA made the second group eligible for a payout from the Per Capita Silo. APA is making both groups eligible for a distribution from the Pension Silo because, under the A Plan, all pilots on disability continued to accrue credited service for pension benefits until age 60.

V. The Treatment of Pilots who Came to American from a Prior Carrier was not Arbitrary, Discriminatory, or in Bad Faith

A. The Treatment of Former TWA Pilots was Reasonable

Two principal challenges are asserted by the former TWA pilots: (1) APA should have used their date of hire at TWA for the Inverse Seniority Silo, and (2) the arbitration process established in LOA 12-05 may not afford the former TWA pilots complete relief from the abrogation of Supplement CC and loss of fenced flying in St. Louis.

The APA acted reasonably in constructing silos using former TWA pilots' actual occupational seniority, which determines their placement on the seniority list, and in using their actual pension credited service in the Pension Silo. Some former TWA pilots insist that the APA should have used their TWA date of hire in the Years of Service even though that date does not correspond to seniority placement.[26] The APA acted reasonably in rejecting

[25] The Company's proposal to terminate retiree medical coverage under the A Plan is the disputed subject of litigation by the Section 1114 Committee in the bankruptcy proceeding. *AMR Corp. v. Committee of Retired Employees*, Adv. Pro. No. 12-1744 (SHL) (Bankr. S.D.N.Y.).

[26] Tellingly, these challenges do not argue that their date of hire at TWA should be used in both the Years of Service and the Inverse Seniority Silos because the result would be a lesser payout from the latter silo that would likely outweigh the greater payout from the former.

that course. Rather than make a special exception for former TWA pilots, the Association used Occupational Date for all pilots in both the Inverse Seniority Silo (through the corresponding seniority number) and Years of Service Silo.[27] Indeed, this decision benefited most former TWA pilots. Although these pilots were deemed to have lesser years of service under this approach, they were also deemed to be more junior for the purposes of the Inverse Seniority Silo, which is weighted towards junior pilots and which is weighted significantly more heavily than the Years of Service Silo. Consequently, the distribution to former TWA pilots from the Inverse Seniority, Years of Service, and Per Capita Silos looks virtually identical to the payout to other pilots: 85% of former TWA pilots receive more than $80,000 from these silos, as do 88% of "native" American pilots.

Similarly, the assumptions in the Pension Silo were reasonable and did no harm to former TWA pilots. The Pension Silo used these pilots' actual pension credited service in calculating their harm from the freeze of the pension plan. The Silo used actual historical pay data for former TWA pilots to project future pay, thereby giving these pilots the benefit of their history of protected flying under Supplement CC. And the Silo used a reasonable assumption of when the fences in Supplement CC would end, January 1, 2023; after that date, the model grants former TWA pilots the higher of their pay projection from the general pilot model and the former TWA model. All of these assumptions were realistic, reasonable, and fair.

This distinction is not pertinent to the Per Capita or the Pension silos. An earlier Occupational Seniority Date would not confer years of service credit under the A Plan.

[27] Indeed, it begs the question. If APA were to make up a date for the TWA pilots based on their starting date with that carrier, what rational basis would it have not to do it for the Ozark pilots merged into TWA, the Reno pilots and the Air Cal pilots?

In this first category of challenges, most former TWA pilots are actually complaining about their placement on the Pilots' System Seniority List under Supplement CC. The Pilots' System Seniority List became effective for the former TWA pilots in March 2002, and a class action challenge to the list was conclusively decided by the United States Court of Appeals for the Third Circuit. *Bensel v. Allied Pilots Ass'n*, 271 F. Supp. 2d 616 (D.N.J. 2003), *aff'd*, 387 F.3d 298 (3d Cir. 2004), *cert. denied*, 544 U.S. 1018 (2005).[28] The equity distribution proceedings do not provide a proper forum for relitigating seniority integration issues.

The second principal argument is that the equity distribution should await the results of the arbitration process established under LOA 12-05, as the former TWA pilots who benefitted from the fenced St. Louis flying may still be harmed. But LOA 12-05 established "final and binding interest arbitration" to "establish certain terms of the [2013] CBA as a substitute for the loss of Supplement CC flying opportunities in order to *resolve all issues* related to the impact on TWA Pilots of termination of Supplement CC." (Emphasis added). Thus, the APA had no obligation to use the equity distribution process as a further remedy for these issues.

[28] Despite the Third Circuit decision, two new lawsuits have been filed against APA seeking to reopen the Pilots' System Seniority List that went into effect in March 2002. *Krakowski v. Am. Airlines, Inc.,* No. 4:12-cv-00954-JAR (E.D. Mo.), now pending before the United States Bankruptcy Court for the Southern District of New York; *Krakowski v. Am. Airlines, Inc.,* No. 4:13-cv-00838-JAR (E.D. Mo.) (pending on motion to transfer). Some of the challenges allege that the listing their date of hire at TWA on their Company identification badge has some special significance. This Company Date is used for very limited purposes, principally vacation accrual. AMR has an inter-company transfer policy that gives employees a Company Date based on when the employee went to work for an affiliate.

Moreover, as discussed extensively in this Statement and in the Declaration of Mark Stephens, the APA could not hold the Equity Stake for any significant period of time, for numerous legal and logistical reasons. *See supra* at 7. The Committee spent six months developing the silo structure, methodology, and allocation. They could not afford to wait even longer to receive the decision in LOA 12-05, consider its implications, formulate a new silo based on those implications, and readjust the remaining silos and allocation of funds between the silos in order to accommodate for the new silo.[29] Instead, the Committee was justified in acting based on the information available when it developed the equity distribution scheme.

B. The Treatment of Former Eagle Pilots was Reasonable

Former American Eagle pilots came to American pursuant to the provisions of the now-expired Supplement W, commonly known as the "Eagle Flowthrough Agreement" because it created a path for the pilots at AMR's commuter affiliate to "flow up" to American should they wish to and for American pilots to "flow down" in the event of a furlough. Challenges relating to former Eagle pilots fall into two broad categories: (1) those asserting that Pension Silo calculations do not reflect credited years of service in the A Plan that were awarded by Arbitrator George Nicolau in an April 2010 arbitration award, and (2) those asserting that APA should have used the equity distribution process to redress certain disadvantages suffered by pilots in the past.

[29] APA has already created significant tension within the bankruptcy by not having a final equity distribution decision until early September given that the court has scheduled a Plan Confirmation hearing on August 15, 2013, and the Debtor has consistently stated that it intends to exit bankruptcy at the end of August.

With respect to the first group of challenges, all but one of them base their challenges on Arbitrator Nicolau's ruling that Eagle pilots coming to American pursuant to his award would have the one-year waiting period for participation in the A Plan waived. *See* McDaniels Decl. at ¶ 23; APA Exh. 55. APA recognizes that the data it received from American may have erroneously denied some former Eagle pilots the A Plan participation credit they were due under the Nicolau award; their participation credit should have dated back to their arrival at American, rather than imposing a one-year waiting period. APA is working with American to determine which pilots were affected and is working to resolve this data issue before the distribution.

Challenge 1121 asserts that the challenger should have five more years of service credit in the A Plan based on a simple misreading of the Nicolau award. Arbitrator Nicolau did not make any award that would result in an additional five years of service credit challenging pilot. *See generally* APA Exh. 55 at 18-21.

The second category of challenges relating to former Eagle pilots asserts that the Committee should have used the equity distribution to redress perceived inequities faced by pilots in the past. These challenges argue that the Committee should have engineered counterfactual calculations by, for example, considering former Eagle pilots' Classification Dates to be coincident with their Occupational Dates[30] or considering their participation in

[30] Eagle pilots who flowed up to American pursuant to Supplement W received Occupational Dates at the same time they received American seniority numbers, which in many cases predated their arrival at American by several years, but they received Classification Dates only when they actually began working at American. *See* McDaniels Decl. at ¶ 11.

the A Plan to date back to American's merger with TWA.[31] However, APA's creation of an equity distribution model based on forward-looking harms resulting from concessions in the 2013 CBA was not arbitrary, discriminatory or in bad faith, *see supra* at 27-30, and these challengers' efforts to remake the equity distribution to redress harms as much as decades old should be denied.

C. The Treatment of Former Reno Pilots was Reasonable

Reno Airlines was acquired by AMR and merged into American in 1999. Several former Reno pilots argue that the YOS Silo should be based on their date of hire at Reno and not their Occupational Seniority Date at American. APA incorporates the position it has taken in Section V(A), with respect to former TWA pilots.

D. The Treatment of Former AirCal Pilots was Reasonable

One challenger asserts that the 1987 Air Cal merger created injury that should be remedied through the equity distribution, because the Air Cal pilots suffered particular injury as B Scale pilots under Supplement B. As with all B Scale pilots, the Air Cal pilots' pension credit, based on a reduced salary and significantly more limited defined contribution and defined benefit plans, are less than those of an A Scale pilot. Given that the equity distribution is based on prospective injury, APA is not redressing the injury by Supplement B. As noted, all pilots have been on the same benefit plans since 1991 and on the same pay scales since August 2001.

[31] One of the challengers grouped with this category is a pilot hired directly at American, rather than a former Eagle pilot. His complaint alleges that the equity distribution should have been used to remedy the harm he suffered when his recall from furlough was delayed by Arbitrator Nicolau's ruling that a significant number of Eagle pilots should flow up to American ahead his recall.

VI. The Treatment of Pilots Covered by Supplement B was not Arbitrary, Discriminatory, or in Bad Faith

A number of the A Scale pilots challenge the equity distribution on the basis of the Company's 1983 promise not to diminish their retirement benefits. At no point in the bankruptcy labor negotiations or litigation did the Company put a value on the elimination of Supplement B. On the contrary, the injury to the A Scale pilots through the freeze of the A Plan and elimination of the lump sum was entirely subsumed within and coincident with the injury suffered by every other pilot at American. Moreover, APA's success in preserving the A Plan, albeit frozen without the lump sum, benefits the most senior pilots who would have received a greatly diminished benefit from the PBGC in the event of a termination.

It would have been irrational for the APA to create a special category of damages for the A Scale pilots. A Scale and B Scale pilots have been on the same benefit plans since 1991 and on the same pay scales since 2001. Nor can APA's treatment of the A Scale pilots be characterized as discriminatory or in bad faith.[32]

Throughout the bankruptcy proceeding, the A Scale pilots repeatedly argued for special treatment, a contention that the bankruptcy court also repeatedly rejected.[33] These

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[32] Conversely, because the methodology is forward rather than backward looking, APA did not consider a remedy for the injury suffered by B Scale pilots under Supplement B.

[33] *See, e.g., In Re AMR Corporation,* Case No. 11-15463 (SHL), Doc. 2134 (April 3, 2012), APA Exh. 37. The Court rejected this motion on the basis that Supplement B was just another part of the labor contract subject to Section 1113. Doc. 4044 at 100-105 (August 15, 2012), excerpts attached as APA Exh. 38. The same A Scale pilots objected to entry of an order approving the new APA/AA collective bargaining agreement that was before the Court on December 19, 2012, on the basis, among other things, that the Court had no authority to extinguish the grievances of Larry Scerba and others protesting the Company's Section 1113 motion to abrogate Supplement B. APA Exh. 39. American objected on the

pilots appeared and objected to the Company's motion to freeze the A Plan but eliminate the lump sum option. The bankruptcy court found their arguments unpersuasive and, on December 19, 2012, ordered that an "amendment of the Pilot Plan to eliminate the lump sum and installment forms of optional benefit payments is necessary to avoid termination of the Pilot Plan before American emerges from chapter 11 of the Bankruptcy Code." APA Ext. 41 at 2.

VII. The Application of the Eligibility Criteria to Lawrence Meadows, Kathy Emery and Wallace Preitz was not Arbitrary, Discriminatory, or in Bad Faith

A. The APA Reasonably Applied the Eligibility Criteria to Lawrence Meadows

Lawrence Meadows, a former pilot receiving disability benefits, complains that he is receiving a payout from only two silos. But that is the correct outcome when the APA's reasonable eligibility rules are applied to Mr. Meadows. First, Mr. Meadows is not on the American Airlines seniority list; he has been inactive for more than five years, starting when he began receiving disability benefits in July 2004. Consequently, Mr. Meadows does not qualify for a full distribution from all four silos. This outcome makes good sense because, as a former pilot who has been removed from the seniority list, Mr. Meadows is much less

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basis that Supplement B no longer existed and that the grievance challenging American's right to file a Section 1113 motion over Supplement B had already been ruled upon on two prior occasions by the Court. Doc. 5626 at 13-14 (December 7, 2012). The Court held that the "grievances filed by the Supplement B Pilots challenging the Debtors' ability to abrogate the collective bargaining agreement with APA are moot and not subject to the grievance and arbitration provisions of the New CBA." APA Exh. 40. Just after the procedural hearing in this equity dispute, counsel for the A Scale pilots filed *Scerba v. Allied Pilots Association*, Case No. 13-03694 (S.D.N.Y.) (complaint served June 17, 2013), alleging that APA breached its duty to the A Scale pilots in the course of the Section 1113 negotiations and litigation.

affected by the 2013 CBA than are active pilots. Mr. Meadows will incur no harm from the concessions associated with the Inverse Seniority Silo or the Years of Service Silo, and he therefore should not be eligible for those silos. Mr. Meadows does not appear to argue that he will be affected by these changes.

It makes no difference that Mr. Meadows returned to LTD status in 2011 after his benefit was previously terminated. For the purposes of determining whether Mr. Meadows is on the seniority list, and therefore whether he might return to active service at American, the important date is when Mr. Meadows originally began receiving LTD benefits, which in turn determined when he would be removed from the seniority list.

B. The APA Reasonably Applied the Eligibility Criteria to Kathy Emery and Wallace Preitz

As an initial matter, the APA submits that it has no representational duty to former pilots who have been dropped from the seniority list because they have been inactive for more than five years from the beginning of their disability benefits, including Mr. Preitz and Ms. Emery.

Although the APA owed no duty to pilots on LTD who had been inactive for more than five years, the Committee reasonably decided to make those pilots eligible for a partial share of the equity for the reasons described above. *See supra* at 49-50. However, the Committee reasonably concluded that former pilots who are no longer on the seniority list, are not on leave, and are not receiving LTD benefits would not suffer harm from the concessions in the 2013 CBA and should therefore be excluded from the distribution.

Mr. Preitz and Ms. Emery fall into this category. They are not similarly situated to pilots on the long term disability plan for the simple reason that they are not receiving disability benefits, and therefore are unaffected by concessions in the 2013 CBA.[34]

Neither are these pilots on TAG status. Mr. Preitz and Ms. Emery were not terminated for cause, and there is no pending grievance or lawsuit that could result in their reemployment as American pilots. Therefore, they do not meet APA's definition of TAG. See McDaniels Decl. at ¶¶ 14, 25.[35] For the same reason, they are not similarly situated to pilots on TAG status.

Both Ms. Emery and Mr. Preitz have asserted that the Dallas-Fort Worth base grievance filed May 22, 2012 ("Dallas Base Grievance"), APA Exh. 60, if successful, would result in their reinstatement. But that is not the case. McDaniels Decl. at ¶ 26. The Dallas Base Grievance seeks to accomplish two objectives: (1) to require advance notice from the Company for anyone about to fall off of the seniority list pursuant Section 11 and Supplement F, so these individuals understand the urgency of trying to reclaim their First Class Medical certification; and (2) to win reinstatement for pilots who have their First Class Medical certification and are ready to return to active status. *Id.* Neither Mr. Preitz nor Ms. Emery will be affected by the outcome of this grievance. Both of them are already

[34] The APA is not obligated to assume these pilots will return to LTD, regardless of pending grievances and lawsuits. By representing Ms. Emery in her December 10, 2007 grievance, the APA did not incur an obligation to treat her in the equity distribution as if she had already prevailed.

[35] The Arbitrator should defer to APA's interpretation of its own internal policies. *See, e.g., Nellis v. Air Line Pilots Ass'n*, 815 F.Supp. 1522, 1538 (E.D. Va. 1993), *aff'd*, 15 F.3d 50 (4th Cir. 1994) (holding that the court should defer to the union's interpretation of its own internal policies unless that interpretation is "patently unreasonable").

off the seniority list and have been for extended periods of time, and neither of them has a First Class Medical certificate.

Similarly, Ms. Emery has asserted that her December 10, 2007, grievance would lead to her reinstatement if successful. That is not the case. Her grievance seeks (1) to return her to LTD and (2) to make her whole for an indeterminate period in 2007 when she should have been on Pay Withheld ("PW") status pending a hearing. *See* McDaniels Decl. at ¶ 27. Her grievance does not seek to, and could not, reinstate her as a pilot at American.

Finally, Ms. Emery and Mr. Preitz have asserted that their ERISA lawsuits make them similarly situated to pilots on TAG. However, counsel for Ms. Emery dismissed her lawsuit without prejudice, and even if she were to prevail, it would not reinstate her to the seniority list. Similarly, Mr. Preitz's lawsuit would not reinstate him to the seniority list.

The Committee reasonably concluded that Ms. Emery and Mr. Preitz—who are not on the seniority list, are not on leave, and are not receiving LTD benefits—would not suffer harm from concessions in the 2013 CBA and should therefore be excluded from the distribution.

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Respectfully Submitted,

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