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Creditors of Delta Air Lines, Inc., et al.

**UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK**

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	:	
In re:	:	Chapter 11
	:	
DELTA AIR LINES, INC., <u>et al.</u> ,	:	Case No. 05-17923 (PCB)
	:	
Debtors.	:	(Jointly Administered)
-----X		

**OBJECTION OF THE OFFICIAL COMMITTEE OF UNSECURED
CREDITORS OF DELTA AIR LINES, INC., ET AL., TO MOTION OF DP3
TO COMPEL THE CONTINUED PAYMENT OF COLLECTIVELY
BARGAINED FOR PENSION BENEFITS TO THE RETIRED PILOTS**

The Official Committee of Unsecured Creditors (the “Committee”) of Delta Air Lines, Inc. (“Delta”) and its affiliated debtors and debtors in possession in the above captioned chapter 11 cases (collectively, the “Debtors”), by and through its proposed counsel, hereby objects to the motion to compel the continued payment of collectively bargained for pension benefits to the retired pilots (the “Motion to Compel”) filed by DP3, Inc., d/b/a Delta Pilots’ Pension Preservation Organization (“DP3”), and respectfully states as follows:

Preliminary Statement

The Committee is sympathetic to DP3's arguments on behalf of the retired pilots, and understands how important the pension payments are to the pilots. Unfortunately, there is simply no basis to compel the Debtors (who have made a business decision not to seek authorization to make such pension payments) to continue to make such payments to or for the benefit of the pilots or to treat the pilots more favorably than all of the Debtors' other pre-petition unsecured creditors.

DP3 and Fiduciary Counselors rely upon inapplicable law and ignore binding Second Circuit precedent in an effort to elevate what are no more than pre-petition unsecured claims into immediately-payable administrative expense claims. The essence of their argument is that the Debtors' failure to pay certain of its pre-petition pension obligations constitutes an impermissible unilateral modification or termination of the Debtors' collective bargaining agreement with their pilots and that, pursuant to section 1113 of the Bankruptcy Code, the Debtors should be compelled to pay the pre-petition pension obligations that are currently due and continue making all such payments as they become due (absent relief under section 1113(e) of the Bankruptcy Code).

This argument is without merit, as the law in the Second Circuit is clear. According to the unambiguous decisions of the Court of Appeals for the Second Circuit in the *Ionosphere* chapter 11 cases, a debtor's failure to perform pre-petition obligations under a collective bargaining agreement does not constitute a unilateral modification or termination of that agreement under section 1113(f) of the Bankruptcy Code. Such a failure results, as with any other executory contract, only in the non-debtor party possessing a claim against the bankruptcy estate that is to be treated in accordance with the priorities set forth in section 507 of the

Bankruptcy Code. While Congress has provided certain exceptions to that priority scheme, it has only done so explicitly. It has not done so here.

Nothing in section 1113 or any other section of the Bankruptcy Code allows a debtor to ignore the priority scheme set forth in section 507 of the Bankruptcy Code in order to pay, as an administrative expense, pre-petition obligations under an unassumed collective bargaining agreement. To the extent that DP3 and Fiduciary Counselors argue otherwise, they are simply wrong.

Importantly, it is established law in the Second Circuit that pension obligations that arise from pre-petition service are pre-petition obligations of the estate, and must be treated as general unsecured claims. As discussed below, it appears that all of the pension obligations and payments that are the subject of the Motion to Compel relate to services performed for the Debtors well before the Petition Date, either because the relevant pension plan was frozen or because the beneficiaries retired pre-petition. Accordingly, such claims are merely pre-petition general unsecured claims and cannot be paid currently.

For all of these reasons and the reasons discussed below, the Committee respectfully requests that this Court deny the Motion to Compel.

Background

1. On September 14, 2005 (the “Petition Date”), each of the Debtors filed with this Court a voluntary petition for relief under chapter 11 of title 11 of the United States Code (the “Bankruptcy Code”). The Debtors continue to operate their businesses and manage their properties as debtors in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code.

2. On September 28, 2005, the Office of the United States Trustee for the Southern District of New York appointed the Committee pursuant to section 1102 of the Bankruptcy Code.

3. On September 14, 2005, the Debtors filed a Motion Pursuant to Sections 105(a), 362(d) and 363(b) of the Bankruptcy Code for Authorization to (i) Pay Prepetition Wages, Salaries, Employee Benefits and Other Compensation, (ii) Maintain Employee Benefits Programs and Pay Related Administrative Obligations, (iii) Allow Employees to Proceed with Outstanding Workers' Compensation Claims and (iv) Authorize Applicable Banks and Other Financial Institutions to Receive, Process, Honor and Pay All Checks Presented for Payment and to Honor All Fund Transfer Requests (the "Wages and Benefits Motion"). In the Wages and Benefits Motion, the Debtors stated that they were not seeking authority at that time to pay, on account of their defined benefit plans, including the Delta Pilots Retirement Plan (the "Pilot Defined Benefit Plan"), "any minimum funding or other contributions or payments that are on account of prepetition labor or otherwise give rise to prepetition claims." The Wages and Benefits Motion further provided that the Debtors were not seeking authority to pay pre-petition claims or obligations under any of the Debtors' non-qualified plans, including the Debtors' non-qualified pilot pension plans, the Delta Pilots Supplemental Annuity Plan and the Delta Pilots Bridge Plan (collectively, the "Pilot Non-Qualified Plans"), for any individual who retired prior to the Petition Date. With respect to employees retiring after the Petition Date, the Debtors sought authority to pay only those benefits attributable to post-petition services under the Debtors' non-qualified plans.¹

¹ DP3, in the Motion to Compel, makes the absurd suggestion that, "in an effort to circumvent the substantive and procedural protections of section 1113," the Debtors carved out pre-petition pension obligations from the relief that they sought in the Wages and Benefits Motion. This is not only a red herring, but it also defies

4. On September 23, 2005, DP3 filed the Motion to Compel, seeking an order requiring the Debtors to (i) continue payment of ongoing minimum funding contributions to the Pilot Defined Benefit Plan and (ii) continue payment to the retired pilots of certain benefits under the Pilot Non-Qualified Plans.

5. The Debtors' Pilot Defined Benefit Plan has a quarterly minimum funding contribution payment due on October 15, 2005 in the approximate amount of \$34 million,² and the minimum funding contributions for the plan will be in excess of \$400 million in calendar year 2006. By agreement with the Air Line Pilots Association, International ("ALPA"), the Pilot Defined Benefit Plan was frozen as of December 31, 2004.³ Thus, the benefits accrued under the Pilot Defined Benefit Plan were for services performed for the Debtors prior to the Petition Date.

6. The Pilot Non-Qualified Plans are unfunded, and do not appear to have any assets set aside in a trust or earmarked for payment of the benefits provided thereunder. In essence, the Debtors write checks to the retirees for benefits owed under the Pilot Non-Qualified Plans in the approximate aggregate amount of \$75 million annually. The Committee is advised that most, if not all, of the beneficiaries under these plans retired long before the Petition Date. Notably, the Debtors sought and obtained authority through the Wages and Benefits Motion to make pension contributions for pilots who retire after the Petition Date on account of the post-petition services

logic. If the Debtors were required, as DP3 argues, to continue making such payments pursuant to section 1113 of the Bankruptcy Code, then there would be no need for the Debtors to seek authority to make such payments in the Wages and Benefits Motion. If, on the other hand, the Debtors were not required to make such payment, then the Debtors would have no obligation to include a request for authority to make payments on account of its pre-petition pension obligations. Such a request for relief would be strictly at the Debtors' discretion.

² The Committee expressly reserves its rights to challenge the validity or amount of any obligation of the Debtors described herein.

³ Since January 1, 2005, the pilots have instead accrued benefits under a defined-contribution 401(k) plan.

that they provide to the Debtors. Thus, the Motion to Compel only seeks to compel the Debtors to make payments to retired pilots for services performed prior to the Petition Date.

7. The Debtors' collective bargaining agreement with ALPA is entitled the Pilot Working Agreement (the "PWA"). The PWA includes an obligation to pay the entire cost of providing retirement benefits for pilots, and expressly references contributions to the Pilot Defined Benefit Plan.⁴ The PWA also states that, to the extent that the full retirement benefits cannot be paid by the Pilot Defined Benefit Plan because of limits imposed by the Internal Revenue Code, such benefits will be paid by the Pilot Non-Qualified Plans.

8. On or about September 30, 2005, the Pension Benefit Guaranty Corporation (the "PBGC") filed a limited response to the Motion to Compel, asserting, among other things, that until a pension plan is lawfully terminated, it must be funded in accordance with ERISA's minimum funding rules, and that the PBGC reserves its rights to seek to enforce such funding requirements.

9. On or about September 30, 2005, Fiduciary Counselors Inc. ("Fiduciary Counselors") filed a response (the "Fiduciary Counselors Response") in support of the Motion to Compel asserting that all of the Debtors' collectively bargained for pension plan obligations should be paid as administrative expense claims and that the Debtors cannot cease paying such obligations without first obtaining an order of this Court after complying with section 1113 of the Bankruptcy Code ("Section 1113").

⁴ See PWA, § 26.

Argument

10. DP3, in the Motion to Compel, asserts that the Debtors' decision not to make minimum funding contribution payments to the Pilot Defined Benefit Plan and the payments due under the Pilot Non-Qualified Plans constitutes a unilateral modification or termination of the PWA that is impermissible unless the Debtors first seek relief pursuant to section 1113(e) of the Bankruptcy Code.⁵ DP3 also argues that the Debtors' decision not to make these payments violates section 1113(f) of the Bankruptcy Code, which states that "[n]o provision of this title shall be construed to permit a trustee to unilaterally terminate or alter any provisions of a collective bargaining agreement prior to compliance with the provisions of this section." 11 U.S.C. § 1113(f). DP3 is seeking an order compelling the Debtors to continue making contributions to the Pilot Defined Benefit Plan and payments under the Pilot Non-Qualified Plans unless and until the Debtors obtain court authorization to cease making such payments under section 1113(e) of the Bankruptcy Code.

11. DP3's argument that the Debtors' decision to stop making payments on account of pre-petition claims constitutes a unilateral termination or alteration of the provisions of the PWA is incorrect as a matter of law. The minimum funding contributions to the Pilot Defined Benefit Plan and the payments to the retired pilots under the Pilot Non-Qualified Plans that are the subject of the Motion to Compel relate solely to services performed for the Debtors prior to the Petition Date. The Pilot Defined Benefit Plan was frozen as of December 31, 2004, after which the pilots ceased accruing additional service credit. Likewise, the Debtors' obligations under the

⁵ Section 1113(e) provides: "If during a period when the collective bargaining agreement continues in effect, and if essential to the continuation of the debtor's business, or in order to avoid irreparable damage to the estate, the court, after notice and a hearing, may authorize the trustee to implement interim changes in the terms, conditions, wages, benefits, or work rules provided by a collective bargaining agreement." 11 U.S.C. § 1113(e).

Pilot Non-Qualified Plans primarily relate to retired pilots whose employment terminated prior to the Petition Date (with respect to pilots retiring after the Petition Date, the Debtors already have sought authority to pay the funding obligations specifically attributable to the beneficiaries' performance of post-petition services for the Debtors).⁶ None of the funding obligations that are the subject of the Motion to Compel arise from the performance of post-petition services for the Debtors. Under established Second Circuit precedent and the decisions of a majority of courts that have considered the issue, the Debtors' pension funding obligations relating to pre-petition services do not constitute administrative expense claims and, therefore, they may not be paid currently. Accordingly, this Court should deny the Motion to Compel.

A. Section 1113 Does Not Require The Debtors To Make Payments On Account Of Pre-Petition Services Pending The Debtors' Decision To Assume Or Reject The PWA

12. Congress enacted Section 1113 in response to the United States Supreme Court's decision in *NLRB v. Bildisco & Bildisco*, 465 U.S. 513 (1984). In *Bildisco*, the Court announced a heightened standard for judicial determinations concerning when a collective bargaining agreement can be rejected. *See id.* at 523-27. The court also held that "a debtor in bankruptcy, prior to obtaining judicial approval to reject the collective bargaining agreement, may unilaterally terminate or modify provisions of the agreement without committing an unfair labor practice under either § 8(a)(5) or § 8(d) of the NLRA," essentially allowing a debtor to rescind a collective bargaining agreement immediately after a chapter 11 filing. *See In re Century Brass Prods., Inc.*, 795 F.2d 265, 272 (2d Cir. 1986) (citing *Bildisco*, 465 U.S. at 534). This second

⁶ Unlike qualified pension benefits, which are paid by a separate juridical entity (namely, the qualified plan itself), benefits provided by the Pilot Non-Qualified Plans are paid to retirees by the Debtors themselves, and any right to receive payments under these plans is "no greater than that of an unsecured general creditor of the company." Pilot Non-Qualified Plans, at § 8. Thus, the plans themselves contain language acknowledging their status as general unsecured creditors.

part of the *Bildisco* decision, which allowed the unilateral termination or modification of a collective bargaining agreement, prompted a flurry of legislative activity and ultimately resulted in the enactment of Section 1113. *See id.*

13. Section 1113, in subsections (a) through (e), imposes certain procedural limitations upon a debtor's ability to reject or modify a collective bargaining agreement and creates an expedited form of collective bargaining. 11 U.S.C. § 1113(a)-(e). Section 1113(f) prohibits a debtor from unilaterally terminating or altering a collective bargaining agreement before the debtor complies with the other requirements of Section 1113. 11 U.S.C. § 1113(f).

14. Notwithstanding the procedural dictates of Section 1113 relating to assumption, rejection and alteration of collective bargaining agreements, collective bargaining agreements are simply executory contracts. *See In re The Leslie Fay Cos.*, 168 B.R. 294, 300 (Bankr. S.D.N.Y. 1994). As such, they are subject to section 365 of the Bankruptcy Code and the other Bankruptcy Code provisions governing claims and obligations arising from such contracts. *See In re Moline Corp.*, 144 B.R. 75, 78 (Bankr. N.D. Ill. 1992) (stating that “[c]ollective bargaining agreements are simply executory contracts with a special provision governing their assumption or rejection . . .”). Under section 365 of the Bankruptcy Code, subject to certain exceptions, a debtor may assume or reject its executory contracts at any time before confirmation of a plan of reorganization. *See* 11 U.S.C. § 365(d)(2). During that period, the fact that a non-debtor party to an executory contract continues to provide services under its contract does not alter its position as a general unsecured creditor on account of any pre-petition claim that it holds. *See In re Whitcomb & Keller Mortg. Co.*, 715 F.2d 375, 379 (7th Cir. 1983) (finding that a creditor that continued to provide post-petition services in accordance with an executory contract “did not alter [its] position as a general unsecured creditor on its *pre-petition* claim”); *U.S. Fin., Inc. v.*

Pacific Tel. & Tel. Co., 594 F.2d 1275, 1279-80 (9th Cir. 1979) (finding that a telephone company's continuation of services post-petition did not give it the right to collect unsecured pre-petition debt).

15. Courts considering this issue with regard to collective bargaining agreements have found that nothing in section 1113(f) of the Bankruptcy Code alters the generally applicable rule that a debtor is not required to pay obligations that accrued prior to the petition date at any time before it assumes a collective bargaining agreement in accordance with sections 365 and 1113 of the Bankruptcy Code. *See In re Moline*, 144 B.R. at 79 (finding that the debtor was not required to pay union its pre-petition claims for medical benefits and vacation pay arising out of collective bargaining agreements because debtor had not yet determined whether to assume or reject such agreements). These courts, including the Court of Appeals for the Second Circuit, have reasoned that a debtor's failure to pay pre-petition obligations required by a collective bargaining agreement does not terminate or alter the agreement in any way and, therefore, does not violate section 1113(f) of the Bankruptcy Code. *See In re Ionosphere Clubs, Inc. (Ionosphere II)*, 22 F.3d 403, 407 (2d Cir. 1994) (stating that payment of benefit claims pursuant to the priorities set forth in section 507 is not equivalent to employer avoidance of obligations under a collective bargaining agreement); *In re Moline Corp.*, 144 B.R. at 79 (stating that a debtor failing to make payments when due may have breached the collective bargaining agreement, but the debtor has neither "altered nor terminated" the collective bargaining agreement—the contract is exactly the same collective bargaining agreement the parties entered into before the chapter 11 case and, therefore, "the debtor has not violated § 1113(f)"); *see also In re UAL Corp.*, No. 02 B 48191 (Bankr. N.D. Ill.), Transcript of March 18, 2005 Omnibus Hearing ("UAL 3/18/2005 Hearing Tr.") at 63 (concluding that "[a] debtor-in-possession or trustee does not, quote, 'modify,' close

quote, an executory contract by failing to make payment during bankruptcy of amounts that are due under the contract on account of pre-petition services.”);⁷ cf. *In re Roth American, Inc.*, 975 F.2d 949, 956-58 (3d Cir. 1992) (concluding that Section 1113 does not create a superpriority for claims under an unrejected collective bargaining agreement). The debtor remains obligated to perform under the collective bargaining agreement, but its failure to perform does not constitute an alteration of the agreement—it merely creates a claim, the priority of which is to be determined by section 507 of the Bankruptcy Code and other provisions concerning the priority of claims, including, without limitation, section 502(g) of the Bankruptcy Code.⁸ See *Ionosphere II*, 22 F.3d at 407; *In re Moline Corp.*, 144 B.R. at 79.⁹

16. In this case, the Debtors’ failure to pay their pre-petition obligations under the PWA does not in any way constitute a “termination or alteration” thereof. The PWA will remain the same collective bargaining agreement that the parties entered into before the chapter 11 cases

⁷ The *UAL Corp.* decision has been appealed to the United States District Court for the Northern District of Illinois.

⁸ Section 502(g) of the Bankruptcy Code provides that a claim arising from the rejection (under section 365 or under a plan) of an executory contract or unexpired lease of the debtor that has not been assumed shall be determined, and shall be allowed or disallowed under section 502 as if such claim had arisen before the date of the filing of the petition. See also 11 U.S.C. § 365(g) (“the rejection of an executory contract or unexpired lease of the debtor constitutes a breach of such contract or lease – (1) if such contract or lease has not been assumed under this section or under a plan confirmed under chapter 9, 11, 12 or 13 of [the Bankruptcy Code], immediately before the date of the filing of the petition . . .”).

⁹ DP3 argues that the Debtors should be deemed to have assumed the PWA, citing to *Adventure Res., Inc. v. Holland*, 137 F.3d 786, 796-97 (4th Cir. 1998), which stands for the proposition that an executory contract that is not rejected by a debtor is deemed assumed. *Adventure Res.*, 137 F.3d at 798. This proposition has been soundly rejected by other courts. See *In re Family Snacks, Inc.*, 257 B.R. 884, 904 (8th Cir. B.A.P. 2001) (a debtor “cannot assume an executory contract by inaction.”); *In re Gateway Apparel, Inc.*, 238 B.R. 162, 164 (Bankr. E.D. Mo. 1999) (“the intention to assume must be clearly declared by the Debtor in Possession or Operating Trustee; and notice of this intention must be given to the necessary parties.”). The courts of this circuit and elsewhere have consistently held that assumption requires a formal motion before the bankruptcy court and cannot be deemed to have occurred by conduct. *In re Enron Corp.*, 300 B.R. 201, 213 (Bankr. S.D.N.Y. 2003) (stating that debtor cannot assume a contract by implication, as notice to creditors and court approval are specifically required before contract may be assumed and its burdens can be imposed on estate); *In re Child World, Inc.*, 147 B.R. 847, 852 (Bankr. S.D.N.Y. 1992) (stating that an assumption of a contract cannot be implied because it requires specific court approval pursuant to a motion in accordance with Fed. R. Bankr. P. 6006); *In re Whitcomb & Keller Mortg. Co.*, 715 F.2d 375, 380 (7th Cir. 1983) (stating that assumption or adoption of the contract can only be effected through an express order of the bankruptcy court).

and the Debtors will remain obligated thereunder. The priority of the amounts ultimately due will be addressed after the Debtors ultimately decide to assume or reject the PWA. At that time, either (upon assumption) the Debtors will be required to cure all past defaults under the PWA, essentially requiring payment in full, or (upon rejection) the unpaid pre-petition accruals may be asserted against the Debtors' estates as pre-petition claims pursuant to section 502(g) of the Bankruptcy Code (or entitled to any priority that is applicable under section 507 of the Bankruptcy Code). Immediate payment, as DP3 requests, is neither mandated nor allowed.

B. The Pension Obligations At Issue, Which Relate To The Performance Of Pre-Petition Services, Do Not Constitute Administrative Expenses And May Not Be Paid Currently Under Established Second Circuit Law

17. As described above, DP3 contends that Section 1113(f) requires the Debtors to continue to pay minimum funding contributions and payments due to retired pilots relating to pre-petition services performed for the Debtors. This is contrary to Second Circuit authority specifically on point. In the Second Circuit, as well as a majority of courts that have considered this issue, pension benefits accrued on account of pre-petition services are not entitled to administrative priority.

1. The Court Of Appeals For The Second Circuit Has Ruled That Section 1113 Does Not Alter The Priority Scheme Embodied In Section 507 Of The Bankruptcy Code

18. The Second Circuit has specifically considered the preemptive scope of section 1113(f) of the Bankruptcy Code in two decisions from the *In re Ionosphere Clubs, Inc.* chapter 11 cases: *In re Ionosphere Clubs, Inc. (Ionosphere I)*, 922 F.2d 984 (2d Cir. 1990), and *In re Ionosphere Clubs, Inc. (Ionosphere II)*, 22 F.3d 403 (2d Cir. 1994). The second decision, *Ionosphere II*, confirms the Second Circuit's view that the priorities set forth in section 507 of

the Bankruptcy Code should apply to claims arising under collective bargaining agreements, and that claims relating to pre-petition services under a collective bargaining agreement will not be accorded administrative expense priority, absent assumption of the collective bargaining agreement.

19. In *Ionosphere II*, the Court of Appeals for the Second Circuit held that the priorities set forth in section 507 of the Bankruptcy Code apply to unpaid pre-petition claims arising under collective bargaining agreements, and that such claims are treated as general unsecured claims or priority unsecured claims (as applicable), absent assumption of the agreement by the debtor. See *Ionosphere II*, 22 F.3d at 407-08. Specifically, the Second Circuit held that vacation pay accrued pre-petition by employees under an unassumed collective bargaining agreement was not entitled to administrative expense priority on account of section 1113(f). See *id.* at 408. The court found that “application of the priority scheme of section 507 will not allow [the company] unilaterally to modify or terminate its obligations under the CBAs,” because the company’s “obligation to satisfy in full the vacation pay claims remains unchanged. Section 507 only establishes the priority of those claims, it does not affect the underlying obligation.” *Id.* at 407. In this regard, the court recognized that:

Judicial ordering of benefit claims pursuant to § 507 is not equivalent to employer avoidance of obligations under a collective bargaining agreement. The collective bargaining agreement is respected, but the financial obligations issuing from it are accorded priority consistent with the Bankruptcy Code. Moreover, application of the priority scheme does not conflict with the purpose of section 1113.

Id. (internal quotation marks and citation omitted).

20. The court also noted that Section 1113 “does not address the priority to be accorded claims arising from a debtor’s obligations under a CBA.” *Id.* at 408.¹⁰ According to the Second Circuit, a court must assume that Congress intended that only the priorities set forth in section 507 should apply to these claims.¹¹ *Id.* Therefore, such benefit claims are “accorded first-priority status as administrative expenses only to the extent . . . attributable to postpetition work.” *Id.* In contrast, claims for services rendered pre-petition are not entitled to administrative priority. *See id.* at 405.¹²

¹⁰ In so holding, the Second Circuit expressly declined to follow the Sixth Circuit’s decision in *In re Unimet Corp.*, 842 F.2d 879 (6th Cir. 1988), to the extent that the Sixth Circuit’s opinion in that case could be read to grant superpriority to all claims for collectively bargained benefits. *See Ionosphere II*, 22 F.3d at 408 (noting that “[t]o the extent that *Unimet* can be read in this manner, it is inconsistent with our analysis in *Ionosphere I* and we reject it.”).

¹¹ In *Ionosphere II*, the court further noted that, when Congress has intended to alter the general priority scheme, it has done so explicitly. *Id.* Further support for the construction of section 1113 adopted in *Ionosphere II* can be found by comparing section 1113 with sections 1110 and 1114 of the Bankruptcy Code, each of which explicitly overrides the priority scheme set forth in section 507 of the Bankruptcy Code. Section 1110(a) of the Bankruptcy Code expressly mandates the payment of all pre-petition claims as the price of preserving the option of assuming an aircraft lease or financing arrangement. Section 1114 of the Bankruptcy Code, which provides for the payment of certain benefits to retired employees, expressly addresses the timing of payment and priority of such claims. *See* 11 U.S.C. § 1114(e)(1) (requiring debtor to “timely pay” any retiree benefits); *and* 11 U.S.C. § 1114(e)(2) (“Any payment for retiree benefits required to be made before a plan confirmed under section 1129 of this title is effective *has the status of an allowed administrative expense as provided in section 503 of this title*”) (emphasis added). Had Congress intended for section 1113 to create a similar superpriority for pre-petition pension claims, it would have either incorporated language similar to that of sections 1110 and 1114 into section 1113, or amended section 507 of the Bankruptcy Code to reflect this intent. *See Certified Air*, 300 B.R. 355, 367-69 (Bankr. C.D. Cal. 2003) (stating that Congress’s failure to include in section 1113 language creating an exemption for immediate payment of any wages or benefits due under a collective bargaining agreement is evidence that Congress did not intend section 1113 to be exempt from the priorities set forth in 507(a)).

¹² In the Motion to Compel, DP3 suggests that the ruling in *Ionosphere II* is inconsistent with the Second Circuit’s prior ruling in *Ionosphere I*. As an initial matter, the rulings in *Ionosphere I* and *Ionosphere II* are not inconsistent. In *Ionosphere I*, the Court of Appeals for the Second Circuit held that section 1113(f) prohibits “the application of any other provision of the Bankruptcy Code when such application would permit a debtor to achieve a unilateral termination or modification of a collective bargaining agreement without meeting the requirements of § 1113.” *Ionosphere I*, 922 F.2d at 990–91. Acknowledging the axiom of statutory interpretation that “[w]hen two statutes are capable of co-existence, it is the duty of the courts . . . to regard each as effective,” the Second Circuit concluded that it would “give effect to the automatic stay to the extent that its application [was] not in irreconcilable conflict with § 1113.” *Id.* at 991 (quoting *Radzanower v. Touche Ross & Co.*, 426 U.S. 148, 155 (1976)). By ruling that the priorities of payment set forth in section 507 of the Bankruptcy Code co-exist with Section 1113, the court in *Ionosphere II* held, effectively, that section 507 of the Bankruptcy Code is not in irreconcilable conflict with Section 1113. *See Ionosphere II*, 22 F.3d at 408. Accordingly, the *Ionosphere I* and *Ionosphere II* decisions are not inconsistent.

**2. An Overwhelming Majority Of Courts
Have Concluded That Section 1113 Does
Not Alter The Priority Scheme Embodied
In Section 507 Of The Bankruptcy Code**

21. The Second Circuit's decision in *Ionosphere II* is in accord with, and relies upon, the Third Circuit's decision in *Roth American*, 975 F.2d at 955-56. In *Roth American*, the Court of Appeals for the Third Circuit rejected the appellant union's assertion that Section 1113 required that the full amount of its claims for vacation pay and severance pay be accorded first priority as administrative expenses. *Id.* at 958. Instead, noting that neither the language nor the legislative history of Section 1113 evinced Congressional intent to address the priority to be assigned to collectively bargained claims, the Third Circuit accorded administrative priority only to those benefits earned as compensation for services rendered post-petition. *Id.* at 956.

22. The majority of lower courts have followed the course charted by *Roth American* and *Ionosphere II*. See, e.g., *In re Rayman, Martin & Fader, Inc.*, 170 B.R. 286, 291 (D. Md. 1994) (concluding that Section 1113 does not establish a super-priority for a union's claims under a collective bargaining agreement, although claims may be eligible for a third priority under section 507); *In re Chateaugay Corp.*, 130 B.R. 690, 700 n.13 (S.D.N.Y. 1991), *opinion withdrawn and vacated as moot*, No. 90 Civ. 6048 (KTD) (S.D.N.Y. Jun 16, 1993); *In re Fleming Packing Corp.*, 2004 Bankr. LEXIS 1384, at *10-12 (Bankr. C.D. Ill. Aug. 31, 2004)

DP3 suggests that the purported inconsistency can be explained by the fact that *Ionosphere I* was decided in the context of a potential reorganization, whereas *Ionosphere II* was decided in the context of an impending liquidation. See Motion to Compel, at p. 12. First, the court in *Ionosphere II* made no reference to this matter in its ruling. Second, the distinction is irrelevant. Section 1113 is equally applicable to either a reorganization or liquidation under chapter 11 of the Bankruptcy Code. See 11 U.S.C. § 103(g); cf. *In re Rufener Constr., Inc.*, 53 F.3d 1064, 1065 (9th Cir. 1995) (section 1113 does not apply in liquidations under chapter 7 of the Bankruptcy Code); and compare 11 U.S.C. § 1113(a) (applicable to "debtor in possession, or the trustee if one has been appointed under the provisions of [chapter 11], other than a trustee in a case covered by subchapter IV of [chapter 11], other than a trustee in a case covered by subchapter IV of [chapter 11] and by title I of the Railway Labor Act") with 11 U.S.C. § 1113(f) (applicable to "trustee").

(concluding that “claims for wages and benefits due under a [collective bargaining agreement] are not, *ipso facto*, entitled to treatment as administrative expenses but are to be accorded priority consistent with Section 507”); *In re Certified Air Technologies, Inc.*, 300 B.R. 355, 369 (Bankr. C.D. Cal. 2003) (“Had Congress intended for § 1113 to create a super-priority for pre-petition wage and benefit claims arising under a collective bargaining agreement, it would have either included language in § 1113 similar to that incorporated into § 1114 or amended § 507 to reflect the change it intended.”); *In re Kitty Hawk, Inc.*, 255 B.R. 428, 436 (Bankr. N.D. Tex. 2000) (“The Court chooses to follow the *Roth American* and *Ionosphere II* courts because their decisions are consistent with this Court’s view of its obligation to avoid construing the Code in a fashion that creates conflict between and among the various provisions of the Code or a reading of the Code that causes one section (here, section 1113) to nullify other sections (sections 503 and 507).”); *In re Family Snacks, Inc.*, 249 B.R. 915, 922 (Bankr. W.D. Mo. 2000), *aff’d in part, rev’d in part*, 257 B.R. 884 (8th Cir. B.A.P. 2001) (characterizing as the “better view” *Ionosphere II*’s holding that section 1113 was not enacted to re-order the priority in which claims would be paid); *In re Wean, Inc.*, 171 B.R. 528, 531-32 (Bankr. W.D. Pa. 1994) (capping any severance pay claims attributable to the 90 days pre-petition at the statutory third priority amount, with any amounts in excess of the priority limit constituting general unsecured claims); *In re Moline Corp.*, 144 B.R. 75, 79 (Bankr. N.D. Ill. 1992).

23. Recently, the Bankruptcy Court for the Northern District of Illinois, in a similar set of circumstances, followed the *Ionosphere II* approach in the *UAL Corp.* chapter 11 cases (United Airlines), observing that “most of the reported decisions have held that a claim for breach of a collective bargaining agreement gives rise to an administrative expense only if the claim meets the requirements for administrative expense treatment under Sections 503 and 507,”

and concluding that “[t]he reasoning of these decisions . . . is entirely persuasive.” *See* UAL 3/18/2005 Hearing Tr. at 63.

24. In electing to adopt the analysis of *Ionosphere II*, the bankruptcy court reasoned that a debtor in possession’s failure to pay pre-petition pension obligations does not constitute an impermissible alteration of a collective bargaining agreement. *Id.* Moreover, the bankruptcy court observed that, in pointed contrast to section 1114(e)(2) of the Bankruptcy Code, which also addresses employee benefits, section 1113 of the Bankruptcy Code is notably devoid of language expressly according priority to obligations arising pre-petition. *Id.* at 64.

25. It is also notable that, like the Debtors, the debtors in the *U.S. Airways, Inc.* chapter 11 cases filed a “Wages and Employee Benefits” motion on their petition date. As in the Wages and Benefits Motion, the *U.S. Airways* debtors did not seek discretionary authority to continue their contributions to defined benefit pension plans and non-qualified pension benefits. In fact, the *U.S. Airways* debtors did not pay any pre-petition funding obligations to their qualified plans for the duration of their chapter 11 cases. The bankruptcy court never ruled on whether the *U.S. Airways* debtors should have been required to make such payments, as the plans were ultimately terminated. Similarly, Northwest Airlines Corporation, which filed its voluntary petition for relief under chapter 11 of the Bankruptcy Code on the same day as the Debtors, did not pay its qualified pension plan contribution that came due the day after its petition date.

26. In following *Ionosphere II*, the law of this circuit, the majority of courts have held that a debtor is not required (or even permitted) to pay claims that accrued prior to the petition date under a collective bargaining agreement, notwithstanding the application of Section 1113.

3. Because DP3 Has Not Demonstrated That The Debtors' Pension Funding Obligations Constitute Administrative Expenses, They May Not Be Paid Currently

27. A party seeking post-petition administrative expense status for its claim bears the burden of proving such entitlement. *In re Hemingway Transport, Inc.*, 954 F.2d 1, 5 (1st Cir. 1992). Because of the strong policy favoring ratable distribution among similar claimants, priority status is narrowly construed. *Trustees of Amalgamated Ins. Fund v. McFarlin's, Inc.*, 789 F.2d 98, 100-01 (2d Cir. 1986). DP3 has not met its burden.

28. In the Second Circuit, courts have consistently denied administrative expense status to pension funding claims. *See Amalgamated Ins. Fund.*, 789 F.2d at 101-102 (“debt is not entitled to priority simply because the right to payment arises after the debtor in possession has begun management of the estate”); *In re Chateaugay Corp.*, 130 B.R. 690, 697 (S.D.N.Y. 1991); *In re Finley, Kumble, Wagner, Heine, Underberg, Manley, Myerson & Casey*, 160 B.R. 882, 891 (Bankr. S.D.N.Y. 1993). In *Chateaugay Corp.*, for instance, the PBGC argued that the debtors’ statutory obligations were triggered by the post-petition termination of the debtors’ employee benefits plan, thus according its obligations post-petition priority status. 130 B.R. at 697. The Court ruled against the PBGC, stating that the PBGC's claims were pre-petition contingent claims because the labor giving rise to the pension obligations was performed pre-petition. *See id.* In *Finley, Kumble*, the Bankruptcy Court for the Southern District of New York held that a minimum contribution obligation with regard to a pension plan was properly classified as a general unsecured claim, finding that no benefit had accrued to the estate, as all of the services relating to the relevant pension benefits had been performed before the debtor’s bankruptcy filing. *See* 160 B.R. at 893; *Pension Benefit Guar. Corp. v. LTV Corp.*, 875 F.2d 1008, 1019, *rev'd on other grounds*, 496 U.S. 633 (1989) (holding that acts giving rise to debtor’s pension

debts were the pre-petition labor of its employees, rather than the post-petition termination of the plan).

29. The Second Circuit is not alone in this treatment of pension obligations. For example, the Court of Appeals for the Sixth Circuit, in *In re Sunarhauserman, Inc.*, 126 F.3d 811, 821 (6th Cir. 1997), held that administrative priority applied only to the post-petition normal cost component of a claim by the PBGC. Likewise, the Tenth Circuit has held that a claim for minimum funding contributions was not entitled to administrative priority status. *In re CF&I Fabricators of Utah, Inc.*, 150 F.3d 1293, 1300 (10th Cir. 1998); *see also In re Bayly Corp.*, 163 F.3d 1205, 1211 (10th Cir. 1998) (holding that the PBGC's claim for unfunded benefit liabilities predicated on pre-petition employment represented a pre-petition contingent claim not entitled to priority); *In re Kent Plastics Corp.*, 183 B.R. 841, 847-48 (S.D. Ind. 1995) (holding that claims for minimum funding contributions based upon and related to pre-petition services are unsecured claims).

30. Because the Pilot Defined Benefit Plan was frozen as of December 31, 2004, and the pilots have not accrued additional service credit since December 31, 2004 under that plan, all minimum funding contributions necessarily relate to pre-January 1, 2005 service. Similarly, the obligations under the Pilot Non-Qualified Plans for which the Motion to Compel seeks immediate payment concern pilots who retired prior to the Petition Date. Based upon the reasoning in *Finley, Kumble, LTV* and other precedent in the Second Circuit, the minimum funding contributions due under the Pilot Defined Benefit Plan and the obligations under the Pilot Non-Qualified Plans are not entitled to be paid in full on a current basis (as if they were administrative expense claims) because all of the services relating thereto were performed prior to the Petition Date.

31. Fiduciary Counselors, in their brief, rely heavily on a single unreported decision of the United States District Court for the Southern District of New York, which purports to require the payment of unpaid pension contributions that become payable post-petition. *In re 1655 Broadway Restaurant Corp.*, 1997 WL 104961 (S.D.N.Y. March 7, 1997).¹³ The facts of the *1655 Broadway* case are decidedly unclear. In ordering the debtor to pay post-petition accrued and unpaid pension and welfare fund contributions, the court held that “[s]ince at no time did the Debtor move to reject or modify the CBA nor receive Court approval for rejection or modification of the CBA . . . the Debtor’s failure to make payments to the Funds as required under the CBA constitutes a unilateral modification of the CBA not permitted under 11 U.S.C. 1113(f).” *Id.* at 2. Importantly, the *1655 Broadway* Court appears to be describing benefits that accrued post-petition. This conclusion is supported by the court’s analogy to payments made to post-petition trade creditors and post-petition payments made to secured creditors. *Id.* In addition, the pension plans in question in the *1655 Broadway* case were multi-employer plans, under which contributions are typically made on a current basis for substantially contemporaneous services and not for past service. *Id.* at *1-2. Moreover, in its ruling, the court in *1655 Broadway* directed the debtor to pay its “*post-petition* accrued and unpaid” pension

¹³ Fiduciary Counselors also cite cases from outside the Second Circuit that have ruled that pension funding claims coming due post-petition are entitled to priority status. *See In re Hoffman Brothers Packing Co.*, 173 B.R. 177 (9th Cir. B.A.P. 1994); *In re WCI Steel, Inc.*, 313 B.R. 414, 418 (Bankr. N.D. Ohio 2004); *Eagle, Inc. v. Local No. 537 of United Ass’n of Journeymen*, 198 B.R. 637 (D. Mass. 1996); *In re Acorn Bldg. Components, Inc.*, 170 B.R. 317 (E.D. Mich. 1994); *In re Arlene’s Sportswear, Inc.*, 140 B.R. 25 (Bankr. D. Mass. 1992). Not only are these cases not binding on this Court, but the rationale of these cases has been rejected by the Second Circuit’s *Ionosphere/Roth American* line of cases. In fact, the bulk of these cases rely on *In re Unimet*, 842 F.2d 879 (6th Cir. 1988), which was rejected in *Ionosphere II* and *Roth American*. *See Ionosphere II*, 22 F.3d at 408 (“To the extent that *Unimet* can be read [to require a superpriority for all claims for collectively bargained benefits], it is inconsistent with our analysis in *Ionosphere I* and we reject it.”); *Roth American*, 975 F.2d at 957 (after considering *Unimet*, the court concluded that Section 1113 does not create a superpriority or automatic first priority for claims under an unassumed collective bargaining agreement). In addition, as noted by the court in *Roth American*, “it is not clear whether the Sixth Circuit in *Unimet* determined *what priority* should be accorded the Union’s claim; the court only reversed the judgment of the district court ‘to the extent that it held that 11 U.S.C. § 1113 does not protect the interests of retirees.’” 975 F.2d at 957 n.10 (quoting *Unimet*, 842 F.2d at 886) (emphasis added).

obligations. *Id.* at *2 (emphasis added). It did not, as Fiduciary Counselors states, rule that the debtor was required to make any payments “which came *due* post-petition.” Fiduciary Counselors Response, at p.9. In any event, to the extent that Fiduciary Counselors cites *1655 Broadway* to support the proposition that benefits that accrue pre-petition are payable post-petition, that holding is contrary to the law established by the Second Circuit in *Ionosphere II*.¹⁴

32. Fiduciary Counselors also attempts to draw a distinction between pension benefits and vacation pay and severance. However, the cases cited to by Fiduciary Counselors, *Alabama Power Co. v. Davis*, 431 U.S. 581, 592-93 (1977), and *Colombia Packing Co. v. Pension Benefit Guar. Corp.*, 81 B.R. 205, 208 (D. Mass. 1988), merely note that employees may choose to substitute future benefits for current wages. These cases do not address the interplay between sections 1113 and 507 of the Bankruptcy Code, nor do they explain why pension benefits should be treated differently than vacation pay or severance benefits (which also represent accruing future benefits) under the priority scheme of the Bankruptcy Code.

33. Simply stated, to the extent that the Debtors’ obligations to fund their pension plans arose out of the performance of pre-petition services, such obligations constitute pre-petition unsecured claims, are not administrative expense claims, and may not be paid currently.

34. As discussed above, it appears that all of the pension obligations and payments that are the subject of the Motion to Compel relate to services performed for the Debtors well before the Petition Date, either because the relevant plan was frozen (as in the case of the Pilots

¹⁴ In any event, the *1655 Broadway* case is not binding precedent in these proceedings because it is the decision of one district court judge in a multi-judge district. See *In re Jamesway Corp.*, 235 B.R. 329, 336 n.1 (Bankr. S.D.N.Y. 1999).

Defined Benefit Plan) or because the beneficiaries retired pre-petition (as in the case of the Pilot Non-Qualified Plans). Accordingly, this Court should deny the Motion to Compel.

Conclusion

DP3 accuses the Debtors of violating Section 1113(f) by ceasing to make minimum funding contribution payments to the Pilot Defined Benefit Plan and payments owing under the Pilot Non-Qualified Plans, arguing that such cessation constitutes an impermissible unilateral modification or termination of the PWA. This position is directly contrary to binding precedent of this circuit and the decisions of courts that have considered this issue. Under these rulings, including the Second Circuit's decision in *Ionosphere II* and the Third Circuit's decision in *Roth American*, the Debtors' failure to make the subject payments pending assumption or rejection of the PWA does not constitute a unilateral alteration or modification of the PWA that would require this Court's prior approval. Instead, such failure merely gives rise to claims against the Debtors' estates. Such claims, because they arise solely from services performed prior to the Petition Date, are pre-petition general unsecured claims, and are not entitled to administrative expense priority. Given such status, there is no legal basis to compel the Debtors to pay these obligations currently.

WHEREFORE, the Committee respectfully requests that the Court deny the Motion to Compel.

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New York, New York

Respectfully submitted,

/s/ Lisa G. Beckerman

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