NRLN

NATIONAL RETIREE
LEGISLATIVE NETWORK

Proposal for Bankruptcy Law Reform Protecting Retiree Benefits in Bankruptcy

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Executive Summary

Tens of millions of U.S. retirees—especially those forced into early retirement by down-sizing—are dependent on their former employers for critical pension, healthcare, prescription drug, disability, survivorship, and life insurance benefits. Unfortunately, these benefits are at great risk when an employer files for bankruptcy: Even though these benefits are earned and critical for basic health and well-being, the retirees are seen as already having made their contribution. Unlike the other creditor constituencies of suppliers, lenders and active employees, retirees are not seen as necessary for the business going forward.

And unlike suppliers, lenders, and active employees, who can diversify their risk or make an adjustment as a company descends into bankruptcy, or who can recoup a portion of their losses out of future dealings with the restructured company, retirees who lose benefits in a bankruptcy typically lose those benefits forever, and they have no option to take back their four-decade investment in their employers' fortunes.

In view of that, Congress has already legislated special procedural and substantive protections for retirees' benefits in bankruptcy, because of the need to protect critical health and welfare benefits in a bankruptcy process that would otherwise result in retirees bearing an unfair share of the burden of cuts (losing everything before others give up anything). Unfortunately, recent large bankruptcy cases have highlighted (or even created) tragic shortcomings or loopholes in those protections in Bankruptcy Code Section 1114, thus pointing out the urgent need for legislative reform.

The National Retiree Legislative Network (NRLN) urges Congress to pass the most critical of these reforms as soon as possible:

- Congress should clarify Section 1114 of the Bankruptcy Code to reiterate that the protections of the statutorily-defined health and welfare retiree benefits extend to "any plan, fund, or program" providing those benefits (as the statutory language provides, but some courts have ignored), not just those benefits a debtor failed to reserve the right to modify outside bankruptcy. At the same time, the statute should require prompt appointment of a Section 1114 retiree committee in large bankruptcy cases and give bankruptcy judges additional flexibility to expand the power of a retiree committee (1) to represent retirees on modification of their collectively-bargained benefits when their union has chosen not to represent them on those issues and (2) to negotiate over claims for termination of non-qualified pension benefits in appropriate cases.

- Congress should provide that more broadly available pensions for workers and retirees may not be terminated in bankruptcy unless the debtor's executives also give up their richer (non-qualified) pensions and deferred compensation plans.

- Congress should generally require the continued minimum funding of defined benefit pension plans during a bankruptcy and provide an administrative claim for the pension fund if those minimum contributions are not made.

- Similar to the protections Congress has already added in Bankruptcy Code Section 1102(a)(4) for small business creditors, to ensure a representative creditors committee, Congress should add flexibility to allow a retiree representative on the creditors committee, particularly where unions have specifically declined to represent the interests of their retirees in negotiating over benefits.

Proposal for Bankruptcy Law Reform Protecting Retiree Benefits in Bankruptcy

Introduction

Tens of millions of American retirees on fixed incomes rely on benefits from their former employers for retirement income, critical medical treatment and essential benefits for their survivors. During their decades of work, retirees were promised these benefits as part of their "total compensation package." Unfortunately, millions of these retirees are finding that these critical benefits are the first things lost when their former employers go into bankruptcy. Because of current gaps in (and misinterpretations of) existing statutes, retirees often receive little or limited protection of their benefits.

The current deep recession has dramatically increased the impact of these devastating cuts. Companies providing retiree medical care and other essential benefits to retirees are disproportionately concentrated in cyclical industries—steel, automotive, manufacturing, airlines—which are especially hard hit in a recession. These are the same U.S. industries that have downsized repeatedly in the last decade, forcing millions of their workers into premature early retirement, before age 65, so they are not yet eligible for Medicare.

Once retirees lose critical benefits in a bankruptcy, they won't ever get them back, even when the economy or the company's fortunes improve. The buyers of assets out of bankruptcy—the ultimate shareholders of successor companies like "New Chrysler" and "New GM"—have little loyalty to the former workers of a predecessor company that just happened to have the same name.

The Impact of Bankruptcy on Retiree Benefits

In the aftermath of the LTV Steel Company bankruptcy, where over 79,000 retirees lost their health and life insurance benefits, Congress passed the Retiree Benefits Protection Act of 1988, adding Section 1114 of the Bankruptcy Code to create limited protections for "*any* plan, fund or program" that provides retiree medical, health, prescription drug, disability, or death benefits. (Emphasis added.) Unfortunately, in part because judges have ignored the statutory wording, the 1988 Act has not provided adequate protection for retirees who have suffered devastating financial losses in several recent bankruptcy cases.

Tens of thousands of salaried retirees for Delphi Corporation started out working for General Motors (GM), but were spun off to Delphi within the last ten years. Immediately after its bankruptcy filing, Delphi successfully opposed the appointment of a Bankruptcy Code Section 1114 retiree committee on the grounds that Delphi had no current intention to cut retiree medical benefits. Three and a half years later, on less than a month's notice, Delphi terminated all company-paid retiree health and insurance benefits. The bankruptcy court ruled that Delphi did not have to comply with Bankruptcy Code Section 1114 before terminating those benefits. The court did appoint a retiree committee to settle the appeal of that ruling, to get something for retirees, and a few months later the retirees had their pensions taken over by the PBGC as well. Here is a sampling of retiree reactions:

"I was one of the employees…in Flint, Michigan where our plant closed and some of us were basically forced to retire….I am now 60 years old…not old enough for…Medicare… My total [income] each month is a little over $1,800 [which] is less than Delphi's health insurance payment each month for my daughter and me (she is 22 years old and in college.) I am a diabetic…with no other means of getting my medication or having the routine 3 month check up. I won't be able to receive diabetic supplies any longer. For me it really does mean getting health insurance or eating. Either way I will lose the battle of life. Michigan has the highest unemployment rate at this time so getting another job will be nearly impossible."
--Brenda T., Delphi (involuntary) retiree.

"I am one of the 'desperate' retirees who will have no health coverage. I was forced into retirement at age 52 with the closure of the Kettering (Ohio) Operations. My wife, a nurse, works full time but her company does not offer healthcare benefits. We have both been pursuing employment opportunities, but the Dayton, OH market is stagnant. I have even interviewed in Minnesota, Georgia, Pennsylvania, as well as Ohio, but still no offers…. I sought quotes for personal coverage, but was denied because I have diabetes and high cholesterol. My plan is to drop healthcare but keep life insurance."
--Christopher L., Delphi (involuntary) retiree

"Jeanne and I are/were what is commonly described as a family living from paycheck to paycheck…. Then I became disabled (four heart attacks destroying one third of my heart, Adult Respiratory Distress Syndrome partially destroying one of the lobes in my lungs, and then came P.T.S.D.)… We were scraping by when Jeanne was diagnosed with cancer (she has had 4 operations so far). We thought things were returning to normal, then Delphi threw us a curve. No, change that, Delphi threw a bean ball at us and unfortunately it was right on target…. I have had to cancel having my defibrillator/pacemaker checked and/or adjusted for the past year, nor have I seen my cardiologist for the same period. I have stopped taking two of my medications, and am taking the most critical one every other day. And, all this before Delphi's latest move. This has literally placed Jeanne and I before a firing squad. The execution will take place on

April 1st this year. That is when our medical care ends, or we stop eating or we move into a car (a GM Cobalt, no less.)
--the MacKenzie family, Delphi retirees

Just months later, General Motors, ironically the buyer of some of the Delphi assets, filed its own bankruptcy and announced that it was cutting its retirees' life insurance benefits to a maximum of $10,000 for its over 123,000 salaried retirees. The bankruptcy court allowed this reduction and refused to apply the statute to limit General Motors additional announcement that there would be a two thirds reduction of remaining retiree health care benefits. Here are some GM retiree reactions:

"Due to the many job transfers I have accepted with GMAC during my tenure of 31 years, my wife has not been able to really secure a long time career of any type and has solely relied on the benefits GM has provided to us - we really need affordable continued coverage. At a time in our lives where insurance coverage is needed the most - during retirement - it is not good to take this away from us at the late stages in life. Had we begun our career later in GM's lifespan where pension plans were not afforded and insurance premiums were higher we would have been prepared more for this - but during my tenure and time - we always counted on the pension plan of GM and put all we could into it while raising 6 kids - we can't lose it now - it would kill us both."
--Tim and Pam C. (GM)

"With the cost of food, utilities all going up you have to choose between eating, paying bills, or your meds."
--Rita S. (GM)

"The combination of the cuts in health care and life insurance will force me to spend over half of my gross pension income on health insurance and life insurance. Or looking at it from a net pension income (after taxes) perspective, these two expenses will take at least 70% of my net pension. These are expenses that I did not plan for during my working years because GM always told us that they would cover these expenses. Note that the other 30% of my net pension income will have to cover all my other expenses (food, shelter, transportation, etc)."
--Terry M. (GM)

"I am a GM Salaried Retiree who worked for Buick for 41 years in management capacities… I also served 2 1/2 years in the US Navy starting in March 1944 and served as an officer on an LST in the Pacific…Reducing my total insurance …to $10,000,virtual burial insurance, is a devastating blow. Upon my death, my wife will also receive a reduced pension and will have a lower standard of living. At my age, purchasing insurance will be unaffordable. The insurance has been part of my estate financial planning for years. I also suffered a considerable loss in GM stock, much of it purchased through the stock savings plan but that was my risk.

It does not seem that unrepresented employees and retirees should bear these large losses without reconsidering the impact and hardship that is being placed on GM family members."
--Raymond J. (GM)

In other currently pending bankruptcies of companies from telecommunications (Nortel Networks) to materials (Lyondell Chemicals) to retail (Circuit City) to financial firms to practically every other kind of business, millions of retirees are looking at potentially losing all their benefits.

Review of Current Law

Bankruptcy Code Section 1114 doesn't prohibit termination or modification of retiree health, life insurance, disability, survivorship and other welfare benefits during bankruptcy, but it does require a process and some limited fact finding that the circumstances justify those modifications. Specifically, in a Chapter 11 bankruptcy case, before these defined benefits are terminated or modified, the bankruptcy debtor must negotiate with an "authorized representative" of the affected retirees—either a union or a committee of retirees appointed in the case under Section 1114. If no agreement is reached with the authorized representative, the debtor can only make the proposed changes if the court rules that the changes are fair under the circumstances, including a consideration of the treatment of other creditors. The court has to find that the changes are clearly favored by a balance of the equities.[1]

Congress extended these protections further in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, to close a potential loophole, adding Bankruptcy Code Section 1114(*l*) which also gives the bankruptcy court the right to reinstate benefits that were modified or terminated within the 180 days before a bankruptcy filing, if the debtor was insolvent at the time of the benefit modification. That prevents a debtor from making cuts on the eve of a bankruptcy filing to avoid the protections of Bankruptcy Code Section 1114, which until then only protected retirees against benefit cuts made during the bankruptcy case.

Congress provided even further relief in 2009, passing the American Recovery and Reinvestment Act, which broadened the definition of "qualifying coverage" for the Health Coverage Tax Credit ("HCTC") to include benefits sponsored by a Voluntary Employee Benefit Association (a "VEBA") set up either by a Section 1114 retiree committee or by order of a bankruptcy judge in a bankruptcy case. The HCTC is a tax credit that pays a portion of the healthcare premium costs of eligible retirees age 55 through 64 whose pensions have been taken over by the Pension Benefit Guaranty Corporation ("PBGC".)

[1]In provisions similar to the heightened standards for rejecting a collective bargaining agreement under Bankruptcy Code Section 1113, Section 1114(f) of the Bankruptcy Code requires the debtor to make a proposal for change to the retiree representatives, along with relevant information to evaluate the proposal. If the proposal is rejected without good cause by the representative, under Bankruptcy Code Section 1114(g), the debtor can still make the change to benefits, but only if the debtor persuades the court that the modification "is necessary to permit the reorganization of the debtor and assures that all creditors, the debtor, and all of the affected parties are treated fairly and equitably, and is clearly favored by the balance of the equities." Section 1114 only protects the benefits for the duration of the bankruptcy, not after confirmation of a bankruptcy plan, unless as part of the negotiating process the bankruptcy debtor agrees to protect the benefits for a time after confirmation, as provided in Bankruptcy Code Section 1129(a)(13).

Bankruptcy Judge Speaks

When Retiree Section 1114 Committees Are Authorized, the Process Works

In court remarks of Hon. Adlai S. Hardin, Bankruptcy Judge for the Southern District of New York, approving the agreements struck separately by Delta Air Lines with the separate retiree committee representing its retired pilots, involving over half a dozen different groups with separate benefits and the retiree committee representing its retired non-pilots (both union and non-union) including those with retirement packages under several different early retirement programs, some contractual and some amendable. The negotiated changes saved Delta many tens of millions of dollars a year, but preserved some subsidies for essential retiree benefits:

I have seen so clearly in this Delta case how important and how wise Congress was in the provisions written into Sections 1113 and 1114... One of the protections built in, which I'm sure that every judge that's ever had to administer this kind of issue is deeply grateful for, is the provision requiring the appointment of committees that have to be paid for by the debtor, out of the debtor's estate, to represent constituencies of debtor employees who have differing interests, and everything that we've heard today underscores the importance of the 1114 committee. I had no idea what a good thing I was doing in granting the motion for an 1114 committee. I thought it was right at the time, but I didn't have the slightest idea how important that decision was.

* * *

So we have here a situation where two committees, for different segments of retired employees, have been appointed... And there were conflicting interests amongst the various constituents. No doubt about it.... What Congress did do was the authorization to appoint a committee with the fiduciary responsibility of the individuals on that committee and the professionals, to look out for all of the different constituencies within their particular groups.

* * *

Counsel for the committees has spoken glowingly of the performance and the dedication of these committees, both of them, and their chairpersons. I don't know how many people here, other than the professionals, have really spent a little time looking at the term sheets [setting out the specific agreement on modifications to health benefits]. I have. They are complex. They're *detailed. They reflect the degree of effort and the attention to the interest of varying different groups. Maybe they're not perfect, but they represent an enormous diligent, good-faith effort.*

* * *

I am confident, based upon what I have seen and heard, that they have done so in as fair and equitable manner as would be possible, and it is always preferable for parties to reach an agreement which they, in their own respective adversarial and competing interests, have concluded is best for their respective clients. It's better to have it done that way than to litigate and have a Court have to master all of the issues and basically force a result.

So I will add one more point. I cannot imagine any possible way, as a practical matter, that… hundreds, probably thousands of people with individual faces and individual concerns and individual differences in their economic situations, their employment history with the company, et cetera, or even [a retiree organization] whatever it is… could possibly, within any reasonable time frame, marshal the facts and the evidence to present to this Court, to now, in effect, litigate, nit by nit and issue by issue, what has been painstakingly accomplished by two very accomplished, diligent committees and their numerous professionals.

* * *

What I'm saying is, I hope self-evident by now, the only way to resolve these complex social issues involving many, many people, with disparate interests, is, as Congress has done, to require to appointment of committees to represent a reasonably allied or similarly situated personnel, and have the committee be charged with the professional responsibility of representing the interest, as best they can see them, of all of those people. That was done here. The process has worked.

Transcript of Hearing, In re Delta Air Lines, case No. 17923, U.S. Bankruptcy Court S.D.N.Y., 10:30 a.m. October 19, 2006, 2:30 p.m. pages 73-79.

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In court remarks of Hon. Robert Drain, U.S. Bankruptcy Court, S.D.N.Y., in the Delphi Corporation bankruptcy case, where he appointed a Section 1114 committee only <u>after</u> approving termination of all salaried retiree health and welfare benefits, authorizing the committee to negotiate a settlement of the appeal of his order. Within weeks, the retiree committee resolved and settled the appeal and obtained $8.5 million in seed money to set up a hardship program and a Voluntary Employee Benefit Association, which has since rolled out a benefit to all the retirees ages 55-65 that is eligible for an 80% federal subsidy under the Health Coverage Tax Credit as recently signed into law, giving the otherwise devastated retirees potentially hundreds of millions of dollars in critical medical subsidies:

The settlement is clearly reasonable from the debtors' perspective in that it brings finality to this issue to the debtors. Normally, that's the only consideration that I would make under the Second Circuit case law. But given the concern Congress expressed for retirees over their benefits, I also want to note that I believe that the settlement reflects the very sophisticated participation by the retirees' committee and its counsel. And so, while normally I would never do this in connection with the settlement, again, since it's not my function to approve the fairness of the settlement to the other side, it appears to me, under all the circumstances, to be fair to both sides in light of all the issues and the debtors' condition and the issues raised by the retirees.

Transcript of Hearing, In re Delphi Corp., case No. 17923, U.S. Bankruptcy Court S.D.N.Y., 11:00 a.m. April 2, 2009.]

Specific Legislative Proposals Needed for Reform

The combination of the Retiree Benefits Protection Act of 1988, the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 and the American Recovery and Reinvestment Act of 2009 should have provided protection for retirees, but the law has not always been followed, and important loopholes have created dangerous gaps in the protections that Congress sought to provide. Several urgent changes are needed to protect these crucial benefits and fine-tune the existing statutory protections:

1. Bankruptcy Code Section 1114 should be clarified to protect *all* the defined retiree welfare benefits (medical, dental, life insurance, disability and survivorship benefits) during the bankruptcy case, not just those the company did not reserve the right to amend.

Bankruptcy Code Section 1114 (a) applies to the modification of "*any* plan, fund, or program" that provides the defined retiree medical and other welfare benefits. In addition, the statute expressly applies, through Bankruptcy Code Section 1114(*l*), to programs the debtor modified under non-bankruptcy law during the 180 days before the bankruptcy filing. Unfortunately, many bankruptcy courts have rejected the plain meaning and intent of the statute, and have refused to apply the statute to cases where the employer reserved rights to amend, modify, or terminate retiree benefits under applicable non-bankruptcy law. (As almost all employers have done.)

In a series of high profile recent cases, including the Delphi and General Motors bankruptcies, bankruptcy courts have ruled that the statute does not apply to any retiree benefit program that the debtor reserved a right to modify outside of bankruptcy. This strained interpretation is now being used by a large number of courts (or, as the Delphi court concluded, by the "majority" of published decisions on the issue) to deny millions of retirees the protection of the statute passed for their benefits.

Legislative clarification that Section 1114 applies to all retiree welfare benefits is critical, because, with the exception of provisions of some unexpired collective bargaining agreements, retiree welfare benefit plans provided by employers almost always include an employer's right to "amend, modify, or terminate" those plans. Without this clarification, judicial misinterpretation of the current statute can lead to absurd results. First, benefits protected by a collective bargaining agreement are covered by a different statutory section, Bankruptcy Code Section 1113, so under this interpretation, Section 1114 no longer has any independent meaning. Second, a benefit modified by the debtor during the 180 days before bankruptcy can be reinstated under Section 1114(*l*), but then immediately eliminated by the debtor under the rest of Section 1114 without judicial oversight during bankruptcy if the court agrees that a debtor's right to amend benefits outside bankruptcy preempts Section 1114.

This clarification does not create permanent vesting of retiree benefits. Under the existing provisions of Bankruptcy Code Section 1129(a)(13), a debtor is not required to maintain benefits protected by Bankruptcy Code Section 1114 after confirmation of a bankruptcy plan, unless the debtor has committed to maintain those benefits for a specific amount of time. All this clarification does is provide short term and limited protections for these most critical benefits during the bankruptcy case, imposing a process so that retirees have a voice in the bankruptcy that will drastically affect their benefits, with a chance to negotiate for slightly less devastating changes—as Congress intended in 1988 and again in passing 2005 amendments.

Without this clarification, other provisions of the Bankruptcy Code and dynamics of the Chapter 11 process will force even debtors who don't want to cut retiree benefits to do so. Secured creditors have special rights to approve or oppose how cash is spent in a bankruptcy case (it is their "cash collateral" under Bankruptcy Code Section 363(c)), and if amendable retiree benefits can be cut without having to go through a process or meet a standard, these lenders will insist that those benefits be eliminated as a condition to the debtor's authorization to use cash for other operating expenses. As Congress recognized in passing the Retiree Benefits Protection Act of 1988 originally, retirees are otherwise vulnerable to losing everything before any other group has to lose anything: Having already made their contribution to the company, sometimes decades ago, "there is nothing that retirees have that the company needs." *Retiree Benefits Security Act of 1987: Hearings on S.548 Before the Subcommittee on Courts and Administrative Practice of the Senate Comm. on the Judiciary*, 100th Cong., 1st Sess. 16 (statement of Senator Heinz). As a result, their benefits are seen as the first cost that can be cut without endangering the debtor's ongoing business.

2. Bankruptcy Code Section 1114 should be amended to provide prompt appointment of retiree committees in large bankruptcy cases involving employers who provide retiree benefits.

Bankruptcy debtors routinely delay the appointment of a Section 1114 committee to represent retirees until it's too late to have a meaningful dialogue over benefit changes, and then use the short time available as an additional justification to avoid appointment of a committee to represent retirees.

Congress should include a provision similar to the following as an amendment to Bankruptcy Code Section 1114:

If the debtor provides retiree benefits to at least 2000 persons, then unless the debtor agrees to the retention of retiree benefits in place through the duration of the bankruptcy or otherwise establishes extraordinary cause for not doing so, the court shall authorize a Section 1114 retiree committee under Section 1114(d) during the first 60 days after the bankruptcy filing, unless the bankruptcy court finds that a liquidation or Chapter 11 confirmation is highly likely within no more than an additional 60 days.

Additionally, during the first 60 days of the case, the debtor shall provide the names, last known addresses and contact information for all retirees to any retiree committee appointed under Section 1114, and—if no such committee is yet appointed—to the organization or organizations representative of retirees seeking to represent their interests in the bankruptcy case.

3. Congress should amend the Bankruptcy Code to provide that in cases where a union refuses to represent its retirees, Section 1114 shall be expanded to provide representation of those retirees in proceedings that relate to the modification of any pension or welfare benefit plan that is subject to the collectively bargained agreement.

Current law gives unions the choice on whether or not to represent their retirees on benefits issues during the bankruptcy case. As a matter of policy, some unions routinely decline to represent the interests of their retirees and choose to represent only active workers' interests and benefits during the bankruptcy case. This creates a dangerous lack of protection for the retirees and their benefits, and it leads to potential abuses as compromises are made that sacrifice retirees' benefits, but the resulting bankruptcy claims or payments under the bankruptcy plan are awarded only to the active workers who have representation. For example, in recent airline bankruptcy cases, a pilots' union elected not to represent its retired members. The union negotiated significant compensation for active employees in return for granting approval to amend the collectively bargained agreement to allow termination of pension plans. In the United Airlines case, the active pilots were compensated $550 million in return for allowing the termination of the collectively bargained pension plan. In the Delta Air Lines bankruptcy case, active pilots were granted a claim in the amount of $2.1 billion (subsequently sold for $1.2 billion in cash) for contractual concessions and a note for $650 million in the event that the pension plan was terminated. In both cases, retired pilots were denied representation in the relevant proceedings and, in both cases, retired pilots did not share in the compensation provided to active pilots, even though the retired pilots lost the benefits. This is manifestly unfair, particularly in a bankruptcy case, which is before a court of equity under a statutory scheme intended to create a level playing field for creditors, not an arbitrary preference of some over others.[2]

A slight modification of existing law would allow a retiree committee appointed under Bankruptcy Code Section 1114 to protect the other legitimate interests of bargaining unit retirees whose unions elect not to represent their interests in the bankruptcy case. The proposed legislative change is to expand Section 1114 to include modification of the collectively bargained benefits of retirees, including the plans that govern those benefits, in bankruptcy cases where a union elects not to represent retirees. In such cases, a committee should be authorized under Section 1114 to represent the interests of retirees relating to their collectively bargained benefits. This is particularly important where the company cuts deals with the active employee representatives to take money out of funds set aside for retirees, survivors, and the disabled to make up the difference between bargaining positions.[3]

The following additional language should be added to the end of Bankruptcy Code Section 1114(d):

"In the event that the labor organization does not represent or refuses to represent the interests of its retirees with respect to modifications of its collective bargaining agreement, including but not limited to proceedings under Section 1113 of this Title, or if the court finds separate representation appropriate, then the court shall also authorize the committee appointed under this section (or a separate committee of retirees) to represent the interests of retirees with respect to other benefits under the collective bargaining agreement, including pension and welfare benefit plans that provide retiree benefits, that are subject to modification under Section 1113 of this Title."

This legislative change will not disturb the ability of the debtor to pursue modification of collectively bargained agreements under Section 1113 or other negotiations, but will provide for

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[2] As the attorney for the PBGC noted, in unsuccessfully objecting to the unfair agreement between Delta Air Lines and the ALPA leaving retirees uncompensated for their losses, "we are required by statute to share a portion of our recovery on our exclusive plan with all of the plan participants, not just the active pilots; the retirees, the people who no longer work there, they are all entitled by statute to share in our recoveries…And what Delta and ALPA are doing here is turning the statute on its head by letting money go directly to the active pilots only, and compensating them to the tune of at least $650 million, if not more, for that same claim." (Transcript, May 31, 2006 oral argument before the Second Circuit Court of Appeal, p. 67, *In re Delta Air Lines.*) Retirees have earned their contractual benefits by working until retirement, and those benefits should not be waived simply because their union chooses to no longer represent their interests. As the Sixth Circuit Court of Appeals noted, "it is unlikely that [life and health insurance benefits], which are typically understood as a form of delayed compensation (continued on page 13) or reward for past services, would be left to the contingencies of future negotiations." *UAW v. Yard-Man, Inc.,* 716 F.2d 1476, 1482 (6th Cir. 1983). Thus, "retiree benefits are in a sense 'status' benefits which, as such, carry with them an inference that…the parties likely intended those benefits to continue as long as the beneficiary remains a retiree." *Id.*, 716 F.2d at 1482.

[3] For example, in the bankruptcy of Delta Air Lines, ALPA elected not to represent the interests of its retirees, survivors, and disabled in the bankruptcy. When a $60 million gap needed to be closed in benefit and compensation modification negotiations between the ALPA and Delta during the bankruptcy, Delta and the ALPA agreed to take $60 million out of the previously fully funded disability and survivorship trust for the benefit of survivors of deceased pilots and disabled pilots, targeting those least able to bear the cuts who were not represented in the negotiations..

fair and equitable treatment of the collectively bargained benefits of retirees that are subject to modification in cases where a union chooses not to represent those retirees.

4. Bankruptcy Code Section 1114 should be revised to provide flexibility for including the determination of claims for loss of retiree's non-qualified pension benefits.

Section 1114 of the Bankruptcy Code applies only to retiree medical, prescription drug, disability, survivorship and death benefits. Retiree pension benefits currently do not fall under the purview of Section 1114, but a need for the protection of certain retiree pension benefits has been highlighted in recent bankruptcy cases.

When a debtor seeks distress termination of a qualified defined benefit pension plan, the Pension Benefit Guaranty Corporation (PBGC) is involved in negotiations relating to the termination of the qualified pension plan, and in cases where a pension plan is subject to a collectively bargained agreement, a union also may participate in negotiations relating to the pension plan. But many millions of retirees and workers have non-qualified pension benefits not under a collective bargaining agreement, and there is no one representing their interest in the bankruptcy case—not the PBGC, not any union, and not the Section 1114 retiree committee, which is limited to dealing with non-pension benefits. That leads to a risk of serious abuses, particularly when it comes to allowing (or disputing the allowed amount) of individual claims for loss of non-qualified pension benefits. The calculation of the net present value of future pension payments is complex and can vary significantly depending upon actuarial assumptions relating to longevity and discount rates. Most cases would benefit from centralized authority to negotiate over the determination of these claims, and a Section 1114 retiree committee is the logical body for that role.

Specifically, Bankruptcy Code Section 1114 should be modified as follows:

The following language should be added at the end of Section 1114(d):

"If the court determines it is appropriate or efficient, the court may authorize a committee appointed under this section, or Section 1114(c)(2) above, to represent the interests of retirees with respect to non-qualified pension and compensation plans or any other benefits other than a qualified plan (where payments are guaranteed by the Pension Benefit Guaranty Corporation) including with respect to the determination of any claims of retirees arising from modifications to those benefits."

These changes would not necessarily impact the process of terminating a non-qualified pension plan, but would give bankruptcy courts additional flexibility in providing for representation of retirees on critical issues and an efficient way of resolving group claims for loss of non-qualified pension benefits.

Congress might appropriately be concerned about whether such a provision would be misused to protect the special benefits granted to a few top executives. That is not the case, however, because Bankruptcy Code Section 1114(m) already includes an income limitation, specifying that except in unusual cases where replacement insurance is unavailable, none of the provisions of Bankruptcy Code Section 1114 protect the benefits of those who earned over $250,000 in the twelve months before the bankruptcy filing.

5. Congress should amend the Bankruptcy Code to require the termination of senior executive pension and deferred compensation plans as a precondition to the termination of the more broadly available pension plans of other employees.

The termination of a pension plan should be the remedy of last resort during a bankruptcy case—necessary for the debtor's reorganization and survival—not the first cost to cut. Current law gives debtors broad latitude to make business decisions on what obligations to reject and which ones to assume. Unfortunately, the top executives making those decisions have a conflict of interest in evaluating their own rich retirement compensation programs.

It is blatantly inequitable for the executives of bankruptcy debtors to propose the termination of employee pension plans while maintaining their own much richer pension and deferred compensation plans. In the interest of fair and equitable treatment and in order to ensure that the termination of any pension plan absolutely is essential to emerging from bankruptcy, language similar to the following should be incorporated into the Bankruptcy Code:

The termination and rejection of the pension and deferred compensation plans of the senior executives of the debtor, including without limitation any "insider" or former "insider" and the five top executives and five most highly compensated individuals shall be a pre-requisite to the court's approval of the termination or rejection of any broadly available pension plan or broadly available pension or survivor benefit of employees or retirees generally. Further, in connection with the disclosure requirements for confirmation of a Chapter 11 bankruptcy plan under Section 1129(a)(5) the court shall require that for five years after confirmation of the plan, any replacement pension or deferred compensation plan for the most senior executives of the debtor or reorganized debtor, including any "insider" and including the five top executives and the five most highly compensated individuals, generally shall be no more favorable than replacement plans of the employees or retirees whose pension plans were terminated, when the replacement plans are compared to the respective pension plans that were terminated.

6. Congress should amend the Bankruptcy Code to require payment of minimum funding of defined benefit pension plans during Chapter 11 bankruptcy cases and to establish as administrative claims against the debtor for failure to pay those minimum funding obligations until the defined benefit pension plan is terminated.

Defined benefit pension plans, which are guaranteed in part by the Pension Benefit Guaranty Corporation, often become even more underfunded as bankruptcy cases drag on and the employers use the protections of bankruptcy law to stop making otherwise required minimum contributions during the case. Simultaneously, employers often drain these same plans at an accelerated rate by raiding them to pay severance allowances as they downsize. The combined result is a heightened risk that pension plan sponsors or the PBGC will seek termination of pension plans and that retirees will suffer greater losses of pension benefits.

Congress should add language to the Bankruptcy Code similar to the following:

Within 60 days after entry of the order for relief in a Chapter 11 case, unless the bankruptcy court finds that (A) a liquidation or Chapter 11 confirmation is highly likely within no more than an additional 60 days, or (B) such funding would both create a liquidity crisis for the estate and lead to the likely termination of the pension plan, the bankruptcy court shall order timely payment by the debtor to any defined benefit pension plan maintained by the debtor of at least the cost of benefits earned during the bankruptcy case, and if there are sufficient available funds, timely payment of any additional required minimum contributions as calculated under applicable non-bankruptcy law.

Additionally, any defined benefit pension plan shall have an allowed administrative claim equal to (i) the cost of benefits earned during the bankruptcy proceeding, to the extent not paid into the defined benefit plan during the case but required to be paid as minimum contributions under applicable non-bankruptcy law; (ii) any additional required minimum contributions that were not made during the case, as calculated under applicable non-bankruptcy law; and (iii) interest on those contributions not made during the case at a rate equal to AA rated corporate bonds with a payment schedule roughly equivalent to the predicted schedule of benefit payments under the applicable defined benefit pension plan. The trustee of such pension plan shall not waive, compromise, or agree to different payment of that administrative claim other than in cash on the effective date of Chapter 11 plan confirmation without prior notice to the Pension Benefit Guaranty Corporation and to the affected retirees and any affected collective bargaining unit, with an opportunity for any or all of them to object and to be heard on the issue.

7. The Bankruptcy Code should be revised to provide, similar to the provision preserving representation for small business creditors, that a retiree representative may be included as a member of the unsecured creditors committee.

In bankruptcy cases, retirees often lose as much or more than other unsecured creditors, and the aggregate value of the benefits owed to them is often the largest liability on the company's balance sheet--yet retirees rarely are provided *any* representation on unsecured creditors' committees that act in a key role in the case. The lack of recognition of retirees is a result of the initial selection of creditors from those with the largest individual claims—although the retirees as a group often have the largest aggregate claim in the bankruptcy, it is divided among thousands of individual retirees, none of whom is individually one of the company's largest creditors.

Recognizing a similar problem that led to the systematic exclusion of small business creditors from creditors committees (particularly since small vendors can be devastated by a large customer bankruptcy), Congress added Bankruptcy Code Section 1102 (a)(4) providing a means for adding a small business creditor to the creditors' committee in cases where small businesses as a group (but not individually) represent a large portion of the debt.

The need for protection of retirees is even more critical. Most creditors spread their investment risk among many different business customers (or in the case of bondholders, make a risk based investment decision, often buying their bonds at a deep discount) but retirees often have invested 100 percent of their careers at one company, sometimes decades in the past. The loss of retiree benefits normally has a disproportionate impact on retirees when compared to the losses of other creditors. Consistent with the provision that small businesses receive special consideration for appointment to the unsecured creditors committee under Section 1102 (a) (4) of the Bankruptcy Code, the appointment of a retiree representative to the unsecured creditors committee would ensure more equitable representation of the interests of retirees.

The proposed change to bankruptcy law is to add the following to the end of Section 1102 (a) (4): "The court may also order the U.S. Trustee to increase the number of members of a committee to include a creditor that is a retiree or an authorized representative of retirees, if the court determines that the aggregate claims of retirees or aggregate value of retiree benefits that may be lost, is substantial in proportion to the other claims of creditors who are members of the committee."

8. Congress should amend the American Recovery and Reinvestment Act to clarify that even after December 31, 2010 "qualifying coverage" for the Health Coverage Tax Credit includes any plan provided by a Voluntary Employee Benefit Association authorized by a bankruptcy court order or a Section 1114 retiree committee, in a bankruptcy case pending on or before December 31, 2010. Congress should also consider extending the current 80% subsidy beyond 2010.

Although the new provisions extending Health Coverage Tax Credit eligibility to certain programs authorized by bankruptcy judges or Section 1114 committees representing retirees are very helpful in simplifying access, an ambiguity in the statute makes it unclear whether benefit programs set up under the statute will still constitute "qualifying coverage" for the Health Coverage Tax Credit after December 31, 2010. That ambiguity makes it difficult to obtain commitments from vendors capable of providing health or prescription drug plans to these newly-formed VEBAs.

The American Recovery and Reinvestment Act ("ARRA") made it substantially easier for retirees to set up benefit plans when their employers collapse in bankruptcy and have those plans be eligible as "qualifying coverage" for the Health Coverage Tax Credit (as COBRA continuation coverage would be or the qualified state plans in about 39 states.) Unfortunately, COBRA continuation coverage often ceases when the employer disappears at the end of a bankruptcy, and many retirees are in states where there is no qualifying plan or the qualifying plan is for minimal coverage of last resort at high premiums.

Conclusion

Bankruptcy is a devastating process, and there are few happy faces in bankruptcy court. But the other key constituencies in a bankruptcy case—employees, management, lenders, suppliers—can live to fight another day and profit as the reorganized company emerges and succeeds in the future. The retirees cannot. Once their benefits are lost, those benefits are lost forever. Five years in the future, the new shareholders of the reorganized company are not going to authorize reinstatement of a benefit for workers who retired decades before the reorganization. Those other key constituencies also have a choice—they can chose to deal with a troubled company, or not, as bankruptcy looms. But for retirees who are often decades past their working age, that choice is unavailable, and nothing they or Congress or the courts can do can give them back their four decades of service for a company, which began half a century earlier.

Bankruptcy is supposed to be a level playing field where the results are fair. Unfortunately, for retirees, recent experience has made it look more like a game of 3-card Monte: Difficult to understand, but completely predictable: They lose every time. These modest changes to existing law will reinstate fairness to the process, level the playing field, and create a different predictability: Millions of retirees will have some chance to negotiate to preserve some of the most critical benefits they already worked decades to earn.