

*REPORT*

to

*THE PRESIDENT*

by

*EMERGENCY BOARD*

*NO. 233*

*SUBMITTED PURSUANT TO EXECUTIVE ORDER NO. 13036  
DATED FEBRUARY 15, 1997  
AND SECTION 10 OF  
THE RAILWAY LABOR ACT, AS AMENDED*

*Investigation of a dispute between American Airlines, Inc. and its employees  
represented by the Allied Pilots Association.*

*(National Mediation Board Case No. 12806)*

*WASHINGTON, D.C.  
MARCH 19, 1997*

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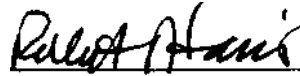
The President  
The White House  
Washington, D.C.

Dear Mr. President:

On February 15, 1997, you established this Emergency Board by Executive Order 13036, pursuant to Section 10 of the Railway Labor Act, as amended. We were authorized to investigate a dispute between American Airlines, Inc., and its pilots represented by the Allied Pilots Association.

The Board now has the honor to submit its Report and Recommendations to you concerning an appropriate resolution of the dispute between the above named parties.

Respectfully,



\_\_\_\_\_  
Robert O. Harris, Chairman



\_\_\_\_\_  
Helen M. Witt, Member

\_\_\_\_\_  
Anthony V. Sinicropi, Member

## TABLE OF CONTENTS

I. CREATION OF THE EMERGENCY BOARD .....	1
II. PARTIES TO THE DISPUTE .....	1
A. American Airlines .....	1
B. The Allied Pilots Association .....	1
III. ACTIVITIES OF THE EMERGENCY BOARD .....	2
IV. HISTORY OF THE DISPUTE .....	2
V. POSITIONS OF THE PARTIES .....	3
A. The Tentative Agreement .....	3
B. American Airlines .....	5
1. Compensation .....	6
2. "B" Scale .....	7
3. Rates for New Equipment .....	7
4. Regional Jets .....	7
C. Allied Pilots Association .....	8
1. Compensation .....	8
2. "B" Scale .....	9
3. Rates for New Equipment .....	9
4. Small or Regional Jets .....	10
VI. EMERGENCY BOARD RECOMMENDATIONS .....	11
A. Compensation .....	11
1. Introductory Remarks .....	11
2. Comparative Factors .....	12
3. Analysis of the Comparative Data Arguments .....	14
4. Compensation Recommendations .....	16
B. Regional Jets .....	17
1. Introductory Remarks .....	17
2. Regional Jets Recommendations .....	19
VII. CONCLUSION .....	21
Appendix "A" .....	A-1

## **I. CREATION OF THE EMERGENCY BOARD**

Emergency Board No. 233 (Board) was established by the President pursuant to Section 10 of the Railway Labor Act, as amended, 45 U.S.C. §160, and by Executive Order No. 13036. The Board was ordered to investigate and report its findings and recommendations regarding unadjusted disputes between American Airlines, Inc. (American or AA) and its Pilots represented by the Allied Pilots Association (APA). A copy of the Executive Order is attached as Appendix "A".

On February 15, 1997, the President appointed Robert O. Harris, an arbitrator from Washington, D.C. as Chairman of the Board, and Anthony V. Sinicropi an arbitrator from La Quinta, California and Helen M. Witt an arbitrator from Pittsburgh, Pennsylvania as Members. The National Mediation Board appointed Joyce M. Klein as Special Counsel to the Board.

## **H. PARTIES TO THE DISPUTE**

### **A. American Airlines**

American Airlines is one of the largest scheduled passenger airlines in the world. American provides scheduled jet service to over 160 destinations, primarily throughout North America, the Caribbean, Latin America, Europe and the Pacific. American's cargo division provides a full range of freight and mail services to shippers throughout the airline's system. American's fleet currently includes 642 jet aircraft.

American Airlines, as the trunk carrier, is the largest member of the airline group of AMR Corporation. In addition to American, AMR's airline group consists of AMR Eagle, Inc. and AMR Leasing Corporation. AMR Eagle is composed of four regional airlines which operate as "American Eagle." American Eagle carriers provide feeder and connecting service to and from high traffic cities serviced by American to smaller markets throughout the United States, Canada, the Bahamas and the Caribbean. AMR Leasing is a financing subsidiary which leases aircraft to subsidiaries of AMR Eagle.

American operates a "hub and spoke" system with four hubs: Dallas/Fort Worth, Chicago, O'Hare, Miami and San Juan, Puerto Rico. American Eagle provides connections to American at its hubs and at certain other major airports.

### **B. The Allied Pilots Association**

The Allied Pilots Association (APA) represents approximately 9,430 employees who fly aircraft for American Airlines as captains, first officers and second officers.

### III. ACTIVITIES OF THE EMERGENCY BOARD

On February 27, 28, and March 3, 4 and 5, 1997, the Board conducted closed hearings in Washington, D.C., at which the issues were addressed. The parties were given full and adequate opportunity to present oral testimony, documentary evidence and argument in support of their respective positions. Each party provided detailed testimony and rebuttal. A formal record was made of the proceedings.

After the close of the formal hearings, the Board met informally with representatives of the parties. Chairman Harris held further meetings with the parties to assist them in narrowing the issues. The Board met in executive session to prepare its Report and Recommendations. The entire record considered by the Board consists of 887 pages of transcripts and approximately 265 exhibits.

### IV. HISTORY OF THE DISPUTE

On June 30, and July 1, 1994, APA and American, in accordance with Section 6 of the Railway Labor Act, exchanged notices of their demands for changes in the provisions of the existing collective bargaining agreement. On January 16, 1996, APA applied to the National Mediation Board (NMB) for its mediation services. The application was docketed as NMB Case No. A-12806.

Mediator Harry D. Bickford began mediation between American and APA on February 12, 1996. Mediation continued through the summer of 1996, and in August of 1996, NMB Chairman Kenneth B. Hipp entered the mediation process. On September 2, 1996, the parties reached a tentative agreement. On January 8, 1997, APA notified American that its membership had failed to ratify the tentative agreement. The NMB, in accordance with Section 5, First, of the Railway Labor Act, offered American and APA the opportunity to submit their controversy to arbitration. On January 15, 1997, American rejected the proffer of arbitration. Accordingly, on that same day, the WEB notified the parties that it was terminating its mediatory services.

On February 10, 1997, NMB Chairman Hipp and Mediator Bickford commenced mediation in the public interest. Despite several days of intensive mediation, no settlement was reached. Negotiations concluded at midnight on February 14, 1997 and at 12:01 a.m. on February 15, APA went on strike. At that time, pursuant to Section 10 of the Railway Labor Act, the NMB advised the President of the United States that, in its judgment, the dispute threatened to substantially interrupt interstate commerce to a degree as to deprive sections of the country of essential transportation service.

The President, in his discretion, issued Executive Order No. 13036 on February 15, 1997, which, effective that day, created this Board to investigate and report concerning this dispute.

## V. POSITIONS OF THE PARTIES

### A. The Tentative Agreement

When the parties entered into a tentative agreement on September 2, 1996, they hoped to bring this round of collective bargaining to a close. While that has not been the case, the tentative agreement addresses many of the issues between the parties to their satisfaction and serves as a focal point for the unresolved issues. A summary of the terms of the tentative agreement (TA) follows:

Duration: \_\_\_\_\_ The agreement would become amendable on August 31, 2000.

Compensation: On the signing date, American would issue 3 million AMR stock options to pilots, priced at \$10 below the market on the date of grant. On August 31, 1998, American would issue 2.75 million AMR stock options to pilots at market price on the date of the grant. The TA also provided for the following pay scale increases:

August 31, 1997	3% increase to pay scales.
August 31, 1999	2% increase to pay scales.

Additionally, the tentative agreement established an hourly rate equal to 1/75 of the pilot's monthly salary for salaried first year pilots in order to provide a pay rate for hours in excess of 75 per month. The tentative agreement would have increased time away from base expenses by \$.05 domestic and \$.05 international.

The tentative agreement would modify the current profit sharing plan for pilots to account for the separation of SABRE from American Airlines. In the future, profit sharing would be based upon airline performance only. The tentative agreement also provided APA with an election regarding whether to change the measurement standard from return on investment (ROI) to a cash flow return on gross assets plan.

The tentative agreement would modify the pension plans to insure that changes in pension laws would not result in a diminution of pilots' pension benefits.

Scope (including Regional Jets): The tentative agreement included a variety of amendments to the scope clause. Those amendments included provisions which would limit expansion of AMR's commuter service, restrictions on comprehensive marketing agreements, restrictions on the use of regional jets (RJs) and a limitation on American's ability to furlough pilots. The no-furlough provision would, with minor exceptions, restrict American from furloughing any pilot on the AA seniority list as of the date of signing until a successor agreement is reached after the August 31, 2000 amendable date.

Provisions which would place limits on commuter service include:

- Commuters would be prohibited from flying any route where AA could perform the service and earn a return on investment (ROI) at least equal to AMR's weighted average cost of capital.
- Commuter flying would be limited to 5% of total AA available seat miles (ASM) (excluding certain new service).

Commuter flying would be limited to 40% of total AA block hours (excluding certain new service).

- Commuter flying would be frozen at actual levels of block hours and available seat miles, when AA pilots are on furlough.
- Commuters would be prohibited from flying non-stop between certain cities unless APA consents. If the number of departures scheduled by AA at any other airport exceeds an average of 70 per day over a 12 month period, AA and APA shall meet to discuss adding such airport to the list of cities.

Commuters would be prohibited from flying any aircraft type in AA's active or inactive fleets.

Commuters would be prohibited from operating any aircraft with a certificated maximum takeoff weight in excess of 75,000 pounds or in excess of 70 seats. The average passenger seating for all aircraft operated by commuter carriers cannot exceed 50 seats.

AA would be prohibited from transferring current aircraft (active or inactive), orders, or options to Commuters.

AA would be prohibited from entering into new codesharing or ownership arrangements with Commuters without prior discussions with APA.

- For Commuters deriving 50% or fewer Revenue Passenger Miles (RPMs) from passenger flying under AA code, such RPMs would not exceed 1.5% of AA's system RPMs. Such RPMs would be included in block hour, ASM and 50 seat average limitations.

The tentative agreement also included the following new restrictions on American's use of regional jets (RJs):

- If AA has 628 or fewer jets, then **RJs** would not exceed 9% of the combined AA/AMR jet fleet.

If AA has 629-700 jets, then AA would be required to add 3 jets to the AA fleet, before a Commuter may add one RJ.

- If AA has 701 or more jets, then AA would be required to add 2 jets to the AA fleet, before a Commuter may add one RJ.
- Notwithstanding the foregoing, there would be a fixed cap of 67 RJs until this agreement is amended.
- New restrictions on comprehensive marketing agreements included in the tentative agreement were:

AA would be prohibited from having comprehensive marketing agreements with domestic new entrant carriers, unless APA consents.

- AA would be prohibited from extending its AAdvantage agreements with Midway and Reno beyond April 30, 2001, unless APA consents.
- AA would be prohibited from expanding city pairs covered by AA/Midway AAdvantage agreement.
- AA would be prohibited from expanding city pairs and/or geographic region covered by AA/Reno AAdvantage agreement.

The TA included provisions strengthening successor and asset sale restrictions, restricting domestic and international (including Canadian) codesharing, and expediting arbitration before the System Board of Adjustment if APA believes that AA has violated the scope clause.

The TA also modified scheduling and work rules to provide for productivity increases. AA and APA agree that the productivity increases are equivalent to 811 jobs and save over \$200 million over the life of the agreement. In addition to scheduling and work rule changes, the TA also addressed several other issues which are not in dispute and which the parties agree will be included in their new agreement.

## **B. American Airlines**

American asks this Board to recommend that the parties adopt the tentative agreement. According to AA, APA's current demands would cost the Company an additional \$426 million over the life of the agreement and an additional annual cost of \$203 million thereafter. American's specific proposals and rationale are described below.



## 1. Compensation

American proposes that the Board recommend the financial terms of the tentative agreement. According to American, its pilots are among the highest paid in the industry and the pay rates included in the tentative agreement would maintain pilots at the highest pay rates in the industry on most types of equipment. American asserts that the compensation provided to its pilots far exceeds the competitors' book rates for each type of aircraft. In addition to the hourly rate included on the pay scale, the pilot compensation package includes stock options, profit sharing and pension benefits.

Historically, pilot pay increases have not been tied to inflation, but, according to AA, have kept well ahead of the rate of inflation irrespective of its profitability. AA points out that its pilots have enjoyed substantial increases in earnings in addition to negotiated pay rates. According to AA, pilots receive periodic varying pay increases, in addition to rate increases and profit sharing, by virtue of their career progression. American also notes that its pilots would continue to have the "best" profit sharing and pension plans in the industry. Specifically, AA and APA negotiated changes to the pension plan in order to protect pension benefits from erosion as a result of changes in pension laws. AA notes that its pilots can look forward to pensions maintaining all of their final average earnings.

American opposes APA's current proposed compensation package because it would impose non-competitive costs on AA and would destroy the internal equity achieved among other groups of American employees.

The cyclical fluctuations in the industry have been obvious, particularly in the recent past, and these exaggerated swings should be expected in the future. American speculates that they may even intensify, and considering the vagaries of the economy and the industry which has been subjected to fiercely competitive challenges, that observation is a reasonable expectation.

American echoes APA's claim that it has been an efficiently run enterprise. However, it must maintain or increase its efficiency if it is to maintain its competitive edge. It expects increasing costs caused by rising labor costs, and the need to purchase new aircraft and equipment will require huge outlays of capital. American suggests that while the cost of the initial compensation payout for APA members may appear to be manageable, the compounding effects of such an initial payout, when considered in combination with future uncertainties, requires caution in assessing the potential impact of APA's proposal.

The work rule concessions and projected job shrinkage noted by the APA are acknowledged by AA. But American points out that the job losses will come about by normal attrition and no layoffs will result from such concessions. In this regard, American is willing to offer furlough protection for pilots employed at the time the agreement is put into effect. American also indicates these concessions will allow it more flexibility which, in turn, should lead to greater efficiency. The pilots will share in those benefits through profit sharing, American stresses.

Despite its relatively new fleet, 9 years average age, American contends it is revamping and changing the nature of the major aircraft fleet. It must do so because new aircraft are lighter and more efficient to operate and will allow American to continue to enjoy a competitive edge. Failure to update the fleet, despite its relatively young age, would leave American at a cost disadvantage in the near future, considering that its competitors will update their fleets with new cost-efficient aircraft.

## **2. "B" Scale**

The "B" scale is a lower pay scale for new pilots for their first five years of employment with American. American opposes the elimination of the "B" scale citing it as a needed financial incentive for it to acquire new equipment and to continue to grow.

## **3. Rates for New Equipment**

American is willing to negotiate rates for new equipment not yet in service. However, the carrier suggests that the Emergency Board should not recommend new rates, but should recommend a process of bargaining and interest arbitration to determine the rates.

## **4. Regional Jets**

American asserts that it can not fly RJs at competitive costs. American characterizes APA's proposal to fly RJs as a "job grab" which is not economically viable in light of the commuter operations at AA's major competitors. Since consumers prefer small jets to small turboprop aircraft, American's major competitors are, or soon will be, operating RJs through their commuter affiliates at commuter costs. In order to remain competitive, American asserts that it must maintain its commuter feed from the Eagle operation. According to AA, pilot labor costs are not the only cost element of a regional jet operation, and AA could not operate RJs at competitive costs compared to the Eagles' operations.

Instead, American proposes that the Board recommend adoption of the amendments to the scope clause included in the tentative agreement. According to American, the TA addresses APA's job security concerns while ensuring that American achieves a satisfactory return on investment. American cites its agreement to protect pilots from furlough and to cap the number of RJs at 67 during the life of the agreement as examples of its efforts to address APA's job security concerns. American thus proposes in summary form as follows on the RJ issue:

- a. that the TA, which does not contemplate having American pilots do all small jet flying, be adopted as the basis for the parties' agreement. But American stresses its willingness to negotiate with APA to develop the kind of safeguards the organization seeks to protect their job security. American remains committed to adopting the following additional proposals:

- (1) no furlough for any American pilot on the seniority list at the date of signing of the Agreement;
- (2) limitations on the number of small jets acquired in terms of aircraft mix, proportion of fleet, number of aircraft and commuter flying expressed as a percentage AMR flying;
- (3) limitations on stage length of commuter flights;
- (4) limitations on city pairs flown and development of routes;
- (5) where American can make a fair return on a route using the Weighted Average Cost of Capital method of valuation, it will retain the route itself instead of permitting the Eagles to fly it.

### **C. Allied Pilots Association**

According to APA, the tentative agreement was rejected by its members for two reasons: the economic package, including the "B-scale", and job security issues. In view of American's recent "record profits," APA seeks to improve the economic package offered to the pilots to get "value for value" for its work rule concessions, and to keep up with the cost of living over the life of the agreement. APA also seeks job security in light of AMR's plans to begin flying "small" 50 and 70 seat jets under the aegis of Eagle. With these goals in mind, APA presented the Board with the following proposals to resolve the dispute.

#### **1. Compensation**

APA contends that AMR and American have been and continue to be highly efficient organizations and there is every expectation the AMR family will continue to be an industry leader in the future. As such, American enjoys a cost advantage over its competitors. The airline industry is cyclical and cyclicity is expected to continue into the future. However, APA contends that such fluctuations should moderate, and given overall projected growth in the industry, American, as an industry leader, should expect to benefit from the expected growth trend.

Work rule accommodations previously conceded by the APA will contribute to American's ability to maintain its comparative cost advantage. In this regard, American and APA agree that, in part as a result of these work rule concessions, American Airline pilot jobs will shrink by 811. The APA seeks "value for value" for these work rule concessions which the Company estimates will produce \$212 million in savings.

American enjoys another competitive cost advantage because its fleet is the newest in the industry. American's competitors will be required to expend enormous sums to update their aging

fleets at a faster and greater rate than will American, and as a result the competitive edge the Company enjoys in this area should be increased.

American's route structure (longer routes, bigger planes, larger markets) significantly contributes to and will continue to contribute to its relatively low operational costs.

APA seeks 7.25 million in stock options at \$10 below the market rate in exchange for a pay freeze from the amendable date of August 31, 1993 through August 31, 1997 and proposes the following pay scale increases:

August 31, 1997	3 percent
August 31, 1998	3 percent
August 31, 1999	3 percent
August 31, 2000	2 percent.

## **2. "B" Scale**

APA proposes a phased-in elimination of the "B" scale. The "B" scale presently provides for a five year merger of rates for new hires. The tentative agreement left the "B" scale unchanged. APA seeks to reduce the "B" scale from five years to one year over the life of the agreement. APA suggests that now is the time to eliminate the "B" scale. Since hiring at American during the contract term is likely to be minimal, elimination of the "B" scale would effect chiefly those pilots who have been called back from furlough recently. Thus, it would have a relatively low cost to American. APA's proposed implementation schedule follows:

August 31, 1997	Change 5th year First Officer percentage to 62% Change 5th year Flight Officer percentage to 53%
August 31, 1998	Change 4th year First Officer percentage to 61% Change 4th year Flight Officer percentage to 52.2%
August 31, 1999	Change 3rd year First Officer percentage to 60% Change 3rd year Flight Officer percentage to 51.3%
August 31, 2000	Change 2nd year First Officer percentage to 50% Change 2nd year Flight Officer percentage to 43.5%

## **3. Rates for New Equipment**

APA proposes the negotiation of pay rates for new aircraft announced after the TA (Boeing 737 and 777).

#### 4. Small or Regional Jets

APA proposes that American pilots fly all jets operated by American or the Eagles. To maintain American's competitive position, APA proposes to negotiate a "Small Jet Supplement" to the agreement that will permit American pilots to fly regional jets at competitive costs. APA characterizes its "Small Jet Supplement" as a crucial job security issue for AA pilots. American pilots will ultimately lose jobs, according to APA, if its members do not perform all RJ flying. According to APA, **RJs** are main line aircraft that can and will be used in service other than in commuter feeder operations. Therefore, APA seeks to protect its membership from losing work as main line routes are siphoned off to American Eagle carriers. According to APA, the supplement would embody the following principles: (1) the Supplement would be "competitive, implementable and affordable;" (2) the compensation and work rules would produce a competitive result; (3) **RJs** would be limited to 20 percent of American's jet fleet; (4) the Supplement together with a wage and work rule adjustment mechanism would lock in wages and work rules for more than ten years, and (5) an interest arbitration mechanism would be implemented to facilitate the extended duration. The specific terms of the "Small Jet Supplement" include:

##### Preferential Hiring

APA proposes the following preferential hiring guarantee be extended to American Eagle pilots:

For every two pilot job openings, American Airlines will offer at least one of the openings to a pilot who is employed by any of the American Eagle carriers, and who otherwise meets all of the competitive hiring standards for employment by American Airlines as a pilot. This preferential hiring obligation shall apply only to the extent that American Eagle pilots meeting both of the foregoing criteria are available.

##### Work Rules

APA proposes the adoption of work rules that are cost neutral under the current Comair/ALPA agreement. APA specifically proposes adopting the work rules in that agreement which cover the minimum monthly guarantee, deadheading, miscellaneous flying, training (schedule portion only), hours of service, and scheduling. If American identifies any other work rule in the agreement that is not cost neutral with respect to the Comair Agreement, APA will enter discussions with American to find a cost neutral work rule.

##### Career Progression

APA proposes that the current provisions regarding entry level positions and career progression at American be modified to reflect that the position of First Officer on a **RJ-50/RJ-70** or comparable aircraft shall be the new entry-level position at American. A pilot holding any position on a small jet may bid directly into any available position on a large jet on the basis of seniority, and

this shall not be considered a down-bid. A pilot who attains any position on a large jet shall not be required for the purposes of qualifying in turn to bid or be assigned to any small jet position.

APA proposes that in the event of a furlough that would allow a senior pilot on a large jet to displace a junior pilot on a small jet, that senior pilot shall have the right to elect a furlough in lieu of displacement, under the stand-in-stead principle that has been agreed to and implemented at American and that was incorporated into the TA.

#### Duration and Interest Arbitration

Under APA's proposal, the parties would meet and attempt to negotiate the first successor agreement governing the "Small Jet Supplement". If no agreement were reached within four months following the first amendable date, the unresolved pay and work rule issues would be submitted to interest arbitration. The arbitrator would establish pay rates and work rules comparable to those in effect at certain named operators of small jets, using the current Small Jet Supplement as an absolute floor. The arbitrator's decision would be rendered no later than six months following the first amendable date of the supplement, and would be effective back to the first amendable date. The duration of the Small Jet Successor Agreement would be 42 months. At the next amendable date, the parties would follow the same process with the second Small Jet Successor Agreement becoming effective on the amendable date of the first Small Jet Successor Agreement and extending for 42 months.

## VI. EMERGENCY BOARD RECOMMENDATIONS

### A. Compensation

#### **1. Introductory Remarks**

Essentially, there are two major arguments advanced by the parties dealing with the economic and compensation questions in dispute. The first is directed towards cost factors and American's ability to meet the compensation goals of the APA while continuing to remain competitive. The second deals with comparability factors that justify the most appropriate compensation due the pilots.

In considering the first question, there are several factors advanced by the parties and the major and most important of those arguments are listed below. A word of caution is in order, however. These detailed listings highlight the parties' most important arguments but do not represent all of their respective arguments, nor does this exposition attempt to explain in lengthy detail the major arguments. To do so would serve no useful purpose and would require an extensive and exhaustive treatment that, in this Board's view, is unnecessary.

The APA's concern about "value for value," i.e., compensation considerations for work rule concessions and job shrinkage, requires serious attention. Both parties agree that the job losses will

occur by attrition. The pilots are of the view that the savings American will realize as a result of these concessions and job losses, should accrue to the pilots. American contends these circumstances are essential to allow it the flexibility/efficiency matrix to keep its competitive edge. These arguments reflect the classic productivity sharing arguments made by labor and management over the years. What is being debated is who should get what share of the savings.

This Board has concluded that the pilots indeed will share in the proceeds of the work rule concessions. No convincing arguments have been made that payment is due for job loss because the job losses, if they in fact occur, will be only by attrition. Second, there is no evidence that anything other than de minimus increases in work hours will occur. Monthly minimums will have been advanced by two hours. Moreover, it can not be conclusively determined that more flying hours may be required above the new 80-hour monthly requirement. When or if such may be required, additional compensation at premium rates will be paid. In effect, greater efficiency and productivity should occur and no appreciable diminution of lifestyle and/or increase in work effort on the pilots' part has been demonstrated. Moreover, if productivity and efficiency increase, the result will be manifested in greater profit sharing rewards. The Board has taken the pilots' "value for value" theme into account in its consideration of the decision regarding the total compensation recommendations and it is of the view the entire compensation package already reflects that consideration.

With regard to all of the arguments the parties made on the effects of costs, the Board recognizes that both parties offered excellent, well prepared and meritorious arguments. However, these arguments are not compelling when determining the appropriate compensation package. While cost is not an unimportant factor, it is not a controlling or determinative factor in this matter. But cost is not the only constraining factor in this dispute. Thus, it is appropriate to review internal and external compensation comparisons as factors for determining compensation. Because "ability or inability to pay" has not been the major argument or defense, that axis of consideration may be the determinative factor in the outcome of this dispute only if the comparative facts require the Board to revisit the cost criteria arguments.

## **2. Comparative Factors**

The APA makes the following arguments:

a. From 1991 to the present, the pilots have not realized any "real" compensation increases. The only increase received during that time period was the 1990 retroactive pay from those negotiations and that was paid in 1991. That payment inflates the Company's assessment of wage increases received by APA members during the relevant time period. Other increases such as movement from "B" scale, profit sharing and seat advancement, are the kind of increases employees in all occupations expect by virtue of promotions, job move-ups and longevity of employment. The failure to achieve any general salary increase during this time period is a critical factor. Moreover, many pilots who were at the top of their job progression did not receive some of those increases. As for profit-sharing payment, that was the result of work effort expended by the pilots who were properly rewarded and it should not be considered as a real compensation improvement. The APA

asserts that the Company characterization of the compensation received by its pilots during this time period is inflated and misleading.

b. The cost of living as measured by the (Consumer Price Index) CPI-U during the relevant time period has increased. When the CPI is taken into consideration, pilot compensation has decreased over the time period in question.

c. The increase sought by the APA if distributed over the six year period covering the negotiations and the length of the new contract, amounts to a little over 1.2% per year. In addition, since no retroactivity is being sought, the real CPI deflated earnings realized in the past three years can not be recovered.

d. The "B" scale pilots have not only been penalized by low compensation levels, in that their fringe benefits, most notably pension, are geared to salary, they have suffered an unrecoverable and a more serious future loss.

e. When making comparisons with pilots at United, Northwest and Delta, American pilots do not fare as well as AA purports. While conceding that American pilots have been near the top of their peer comparison group, APA claims their future standing will not be as well situated if the APA position is rejected in favor of American's position. In this regard the APA makes reference to the stock bonus grants made at United, Northwest and Delta. The stock plan as proposed by American is more restrictive and less attractive. In this instance, American's offer was to allow pilots the right to exercise non-tradeable stock options at \$10.00 below the market price of AMR stock at the time of purchase of the stock. This situation requires the use of a non-tradeable option and the outlay of dollars to buy the stock. No such requirement existed at the other airlines. The stock in those instances was an outright grant. The APA contends American's offer must be considered to be of less value and is less attractive than the carrier represents it to be.

f. The APA rejects the notion that salary increases should be restricted to percentage increases obtained by other employee groups because of "me too" contract strictures between American and other unions. Such a notion is tantamount to acknowledging that the APA has no independent bargaining power or authority. The APA asserts that its salary and compensation goals should be accepted is justified and needed.

American makes the following arguments:

a. Since 1991, American pilots have enjoyed substantial compensation increases on an annual basis. While these increases have resulted from a retroactive payment in 1991 for 1990, a salary schedule increase, profit sharing rewards, and "B" scale and seat move-ups, these increases have been real in-pocket increases for most pilots. Nearly all have realized one or more of the combination of the above rewards during the relevant time period.



b. American compares CPI-U increases from 1991 to the present to the compensation increases the pilots received over the same time period and argues that the real compensation increases have outstripped increases in the CPI-U.

c. American contends that the original TA achieved in September of 1996, will accord its pilots a viable and competitive comparative compensation advantage over their peers at other companies. Profit sharing has been excellent the past two years and the carrier expects it to continue to be rewarding. To maintain its integrity, the carrier has adjusted and indexed the profit sharing plan to account for its partial sell off of SABRE and the resulting loss of its income contribution to AMR. American points out that its profit sharing plan is among the industry's best and over the past six years it has paid the average pilot about \$15,000.00 in profit-sharing rewards.

d. By either measure, hourly rates or the annual salary on most aircraft types, American pilots now receive more than their counterparts at United, Northwest or Delta. The carrier contends that its compensation offer at the time of the tentative agreement would continue to keep its pilots in the lead in compensation, and if anything, their differential over their competitive peers will increase in the future. Even with salary snap back expectations at United and Northwest, American claims its predominant position should remain intact.

e. Internal compensation equity is one of the cornerstones of good compensation policy. American argues that if it were not consistent in its administration of internal compensation programs, it would not only defy good compensation practice, but it would negatively affect employee morale. American implies that if the percentage pilot compensation increases exceed those negotiated with other employee groups, it might well have to make adjustments for the other employees -- thus adding to its overall labor costs.

The options purchase plan and the stock offering proposed by American when compared to United, Delta and Northwest, is comparable in several respects. According to American, the valuation of this offer should be made consistently, and if done in such a manner, this offer when added to the rest of its compensation offer, provides American pilots with an excellent compensation package.

### **3. Analysis of the Comparative Data Arguments**

In assessing these arguments, the Board will rely on a standard of what it considers to be fair and reasonable under the circumstances reflected in the record.

The "real" in-pocket compensation benefits realized by American pilots from 1991 to 1997, are more closely related to American's position, than APA's for the following reasons:

a. While seat advancements, "B" scale move up, profit sharing pay and retroactive pay are not salary scale advances, they nevertheless are real in-pocket monetary rewards. They constitute disposable income that can be spent or saved. In

addition, most, if not all of such income has fringe benefits (including pensions) attached to it. Moreover, "automatic" longevity increases and/or promotions must be considered as monetary rewards.

b. Reliance on the CPI-U as a cost of living indicator for this group of employees is misplaced. The CPI, even by the Bureau of Labor Statistics (BLS) definition, is not a measure of cost of living. At best, it measures the dollar increase in consumption patterns of an urban family of four, earning between \$40,000.00 and \$50,000.00 per year. The group of employees involved in this dispute does not fall within that definition, even if the CPI were relied upon. The CPI-U also has been under attack as an inflated index that overstates increases in prices. The following example highlights this point. The CPI has several sub indices, each of which is weighted. Among those sub indices is one dealing with medical costs and medical insurance. If that sub index reports increases in the medical cost area and concurrently reports increases in the medical insurance area, it is improperly inflating medical costs because it double counts these increases. In addition, if the employees are covered by medical insurance for which they pay no increase in premium, the index significantly over represents the increases. It is not necessary to belabor the point but the CPI is not an appropriate measure to rely upon to prove inflation for this group of employees. However, even if the CPI were taken into account as a cost of living factor, the "real in-pocket" increases in compensation realized by the pilots during the relevant time period exceeded CPI increases.

c. At Delta, Northwest and United, pilots took salary and salary scale reductions of sizeable amounts - up to 15 1/2 percent. While such cuts did not include major fringe benefits reduction, they indeed were real in-pocket monetary reductions. To be sure, stock was offered in exchange for these cuts, but the salient point is that those pilots received real pay cuts for three or more years and had restrictions on trading of stock during that time and perhaps beyond. This point is important for a variety of reasons. First, American pilots did not experience an across the board pay decrease and consequently their total compensation over the relevant time period was greater than their counterparts' elsewhere. Second, American should be recognized now for not asking its employees to share its profit shortcomings or losses by taking pay cuts. If employees are expected to take pay cuts in periods of the carrier's losses, they should expect to share greater benefits in periods of the carrier's prosperity. When no pay cuts are requested in non-profit years, a different result may be justified.

d. An analysis of the comparability data shows that American's data is more convincing than APA's in that American pilots' relative compensation status will remain substantially above their competitors' in the future. In addition, when the entire compensation package is considered, American's pilots' relative comparative standing does not seem to be in danger of being eroded or altered in the future. In fact their status may be heightened.

e. Internal compensation consistency is one measure of compensation policy. While "lock step" procedures or "me too" agreements should not and do not have an influence on this Board, if the compensation levels arrived at independently are fundamentally sound, then internal consistency should not be disturbed.

f. The \$10.00 below market price for exercising a stock option indeed holds great promise for the pilots. Most analyses of American stock, which is now trading in the mid \$80.00 range, reveals that a \$120.00 price is more representative of its real market value. The price differential (between a mid \$70.00 purchase price range under the stock option offer and a \$120.00 value) is in fact equal to the \$50.00 value placed on the options by the expert witnesses of both parties. Thus, while projections are always made with a certain degree of risk, the assumptions underlying the value of this offer are relatively sound.

In summary, the Board believes that the compensation elements in the tentative agreement are more representative of a fair and equitable settlement than is the last position advanced by the APA. However, the Board concludes that some enhancements of the tentative agreement compensation package can be a basis for a very fair and reasonable settlement. Accordingly the following recommendations are made.

#### **4. Compensation Recommendations**

- a. Effective on the date of signing, five (5) million AMR stock options priced at \$10.00 below market price at the date option is exercised.
- b. The following increases to pilot pay scales are recommended:
  - o August 31, 1997 - 3% increase in the pay scale.
  - o August 31, 1998 - 2% increase in the pay scale.
  - o August 31, 1999 - 1.5% increase in the pay scale.
- c. The Agreement should be amendable on August 31, 2000. At APA's option, the amendable date may be extended to March 1, 2001, in exchange for 1,000,000 (one million) stock options priced at market value.
- d. All pilots on furlough between January 1, 1993, and March 15, 1997, will receive seniority credit for pay purposes only, in the amount of one (1) day for each two (2) days on furlough.
  - o such credit will be prospective and will not extend seniority for pay purposes beyond step 6.
  - o such credit will not impact any other matter including probationary status.

e. There will be a phased-in elimination of the B-scale. This addresses APA's economic concerns in terms of both salary and pensions and is regarded as fair and reasonable by this Board.

f. APA and American should continue their negotiation over pay rates for new equipment. If they can not reach an agreement by the time the new aircraft has been in service for 60 days, then the pay rates should be arbitrated. If the pay rates must be arbitrated, the arbitrator should be restricted to a rate between one and three percent above that used at other main line carriers.

## **B. Regional Jets**

AMR Corporation, parent of American Airlines, also owns and operates the four commuter airlines known collectively as American Eagle or "the Eagles". These small air carriers operate turboprop airplanes to feed passengers to cities where American has established "hubs". A hub is the center point of the "hub and spoke" system developed by air carriers after deregulation of the airline industry in 1978. It was designed to provide air transportation to local geographic areas which, because of population size or geography, cannot support the efficient use of large jet aircraft. Smaller turboprop airplanes such as the Shorts are used as feeders to the hubs or connectors with hub flights. Stage lengths commonly average no more than 250 miles at American Eagle.

The Eagles were purchased by AMR in 1987 after the Allied Pilots Association agreed to "Supplement S", a special provision authorizing American to create, buy or contract with a commuter air carrier for the purpose of providing passenger and cargo feed to American flights and/or "to enhance the Company's overall market presence." The Supplement also provided limitations or "wraps" intended to limit Eagle flying to the parameters established for its existence.

In 1991, APA petitioned the National Mediation Board alleging the existence of a dispute with respect to representation on the four Eagle carriers. After a lengthy proceeding, the **NMB** found that there was a single system for representation purposes. In the election that followed, the Air Line Pilots Association won the right to represent all pilots flying the Eagles. Pilots at American Airlines, of course, are represented by the Allied Pilots Association, the organization which is a party to the dispute here.

### **1. Introductory Remarks**

At the core of the dispute before this Emergency Board is APA's concern that the job security of American pilots is at risk because of AMR's stated intention of purchasing small jets. It is viewed by APA leadership as "...the first and foremost, the high priority issue." APA sees a potential for AMR to replace AA's F-100's and MD-80's now in use with new 50- or 70-passenger small jets which then can be flown instead in the Eagle system by Eagle pilots at commuter pay rates rather than the main line rates paid to AA pilots. These aircraft are not regarded simply as replacements for shorthaul commuter turboprops but rather, because they have cruising ranges of up to 2000 nautical miles, as an efficient and profitable commuter alternative for such main line purposes as accessing new markets and providing hub capacity relief. AMR intends to replace aging Eagle turboprops with RJs

in order to maintain market share, develop new routes and strengthen the feeder and connector systems already in place. But RJs capable of carrying more passengers faster, farther and more efficiently than turboprops, could threaten the job security of AA pilots if used for the development of routes by the Eagles which otherwise would be American routes. There could be a resulting loss of AA pilot positions, and the shrinkage of American Airlines.

Commuter airline feeders are essential to a hub and spoke system. Moreover, it is critical to have a feeder that shares American's code so that passengers can be ticketed on American for the entire trip rather than on an airline partner of a non-code sharing commuter airline.

Passengers are known to prefer jet aircraft to turboprops and will choose a jet commuter flight over a turboprop commuter flight if given the option. That is one reason why American concluded it is essential to gradually replace its commuter fleet with small jets. A second reason is that small jets are faster, lighter, capable of traveling longer distances and, because of their smaller capacity, have the potential to take advantage of new opportunities in longer, thinner markets. In sum, small jets are more efficient and promise a better earnings potential than the aircraft now in use on American Eagle.

The issue of regional jets gained momentum within pilot ranks after the TA was negotiated when the Chairman of AMR wrote a letter to a Miami pilot which, to the pilots, seemed to imply that neither the Chairman nor American's chief negotiator cared who flew the small jets so long as the costs were Eagle-equivalent costs, not American costs. Pilots at the top of the seniority list on an Eagle carrier earn about \$64,000 per year. The pilots concluded from the letter that an exclusive right to fly the small jets was obtainable in bargaining if APA pressed hard enough. The team that had negotiated the TA received a vote of "no confidence" and was replaced.

American insists that it has no intention of substituting Eagle flying for AA flying, arguing that it seeks only to strengthen the feeder system and establish new markets to enhance American's presence. But it recognizes the job security issue raised by the pilots and remains willing to adopt appropriate limitations or "wraps" on the use of RJs by commuter carriers.

The proposal made by the pilots to fly RJs at special rates, as entry level positions on American, although made in good faith, is non-competitive, because the proposed rates far exceed cabin costs, including flight attendant costs, on the commuters and the proposal makes no provision at all for other costs. Moreover, APA's proposal acknowledges that there is little likelihood that American pilots currently flying as Captains or First Officers on F-100's or MD-80's would be willing to bid to the **RJs** at lower rates of pay.

American's major competitors already have purchased or have options on up to 300 small jet aircraft demonstrating their commitments to operate RJs at their commuter partners. American, to compete effectively, can do no less.

In addition to pilot costs, there are other costs which differ between the Eagles and American. Even if the pilots agreed to a Small Jet Supplement which provided for reduced rates for American pilots flying RJs for commuter-type flying, there is no means to reduce in a corresponding way the

costs associated with other employee groups.

The RJs do not threaten to supplant the large aircraft American flies on its main lines because of the unit cost advantage of large aircraft and the revenue advantages of amenities like first class cabins. And inasmuch as American represents more than three quarters of AMR, it would be counterproductive for American to give way to the Eagles.

## **2. Regional Jets Recommendations**

Cognizant that the regional jet issue is fraught with emotional and technical issues beyond the capacity of this Board to resolve in the limited time available, the PEB recommends the following broad guidelines, anticipating that representatives of the parties with the necessary technical expertise will flesh out the proposals into practical contract language.

a. The Emergency Board does not recommend APA's proposal that all RJ flying be flown by American pilots. In 1987, APA agreed to Supplement "S" which allowed the Commuter Air Carriers to operate jet-powered aircraft and we are not inclined to revisit that agreement. Ultimately that option could and most probably would lead to the extinction of American Eagle as a feeder/connector airline thereby weakening the hub and spoke system to the detriment of American's competitiveness. The data do not support a conclusion that a cost-effective small jet supplement is reasonably attainable.

b. The restrictions or wraps set forth with respect to regional jets that appear in the TA should be used as the basis for the parties' agreement with the following additional provisions:

(1) AA Fleet Floor

In the event that the AA fleet count falls below 628 aircraft, then the Commuter Air Carriers operating pursuant to Section 1.D shall remove from service one RJ for every two AA aircraft below 628. This provision shall not apply if the reduction in aircraft below 628 is caused by conditions beyond the Company's control, such as, but not limited to the following: (1) an act of God, (2) a strike by any other Company employee group or by the employees of a Commuter Air Carrier operating pursuant to Section 1.D., (3) a national emergency, (4) involuntary revocation of the Company's operating certificate(s), (5) grounding of a substantial number of the Company's aircraft, (6) a reduction in the Company's operation resulting from a decrease in available fuel supply caused by either governmental action or by commercial suppliers being unable to meet the Company's demands, (7) the unavailability of aircraft scheduled for delivery.

(2) Pilot Floor

i. If the number of pilots falls below 7,300, the commuter exception contained in Section 1.D. terminates. The Company shall have reasonable

time to complete disposition of such operations.

ii. Between 7,300 AA pilots and 8342 AA pilots (the number of AA pilots on the seniority list on 3/3/97 minus 811), the number of aircraft operated pursuant to Section 1.D. is frozen (i.e., neither the number of turboprops nor the number of RJs may be increased).

(3) Block Hour Limitation

i. Eliminate "new flying" exception for block hours.

ii. In the event of a furlough:

(a) The total block hours for all Commuter Air Carriers as of the date of the furlough cannot be increased, pending recall of the furloughed pilots, and

(b) The block hours percentage may not exceed the block hour limits set out in the TA as a result of a reduction in AA block hours.

(4) Stage Length Limitation

Eighty-five percent of all RJ departures must be limited to stage lengths of not more than 1000 nautical miles.

(5) Deployment in Hubs/Major Airports

85% of all RJ departures must be into or out of the following hubs/major airports: DFW, ORD, SJU, SFO, LAX, LGA, and JFK. RJ departures utilizing commuter slots at slot controlled airports other than those listed above (e.g., DCA), and departures from airports limited to commuter departures by other governmental or aircraft operational restrictions (e.g., SAF), shall not be covered by this provision.

(6) Methodology

The methodology for counting departures shall be consistent with the methodology contained in the previous tentative agreement between the parties for counting RJs, block hours, ASM's, aircraft, and seats.

(7) Remedies

i. Add language to Section 1.L. of the Scope Clause which allows APA to enforce an arbitration award in court by the use of injunctive relief.

- ii. AA, AMR and APA shall enter into a side letter wherein AMR acknowledges that it is an affiliate of American within the meaning of Section 1 and that AMR is bound by Section 1 in the same manner as American.

The Board makes no other recommendations with respect to the issue of regional jets.

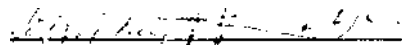
## VII. CONCLUSION

This Report is submitted by the Emergency Board in the hope that it will be viewed by the parties as a fair and reasonable basis for resolution of all issues remaining in dispute.

Respectfully,

  
\_\_\_\_\_  
Robert O. Harris, Chairman

Helen M. Witt, Member \_\_\_\_\_

  
\_\_\_\_\_  
Anthony V. Sinicropi, Member



EXECUTIVE ORDER

-- 13036 --

ESTABLISHING AN EMERGENCY BOARD TO INVESTIGATE A DISPUTE  
BETWEEN AMERICAN AIRLINES AND ITS EMPLOYEES REPRESENTED  
BY THE ALLIED PILOTS ASSOCIATION

WHEREAS, a dispute exists between American Airlines and its employees represented by the Allied Pilots Association; and

WHEREAS, the dispute has not heretofore been adjusted under the provisions of the Railway Labor Act, as amended (45 U.S.C. 151-188) (the "Act"); and

WHEREAS, in the judgment of the National Mediation Board, this dispute threatens substantially to interrupt interstate commerce to a degree that would deprive sections of the country of essential transportation service,

NOW, THEREFORE, by the authority vested in me as President by the Constitution and the laws of the United States, including sections 10 and 201 of the Act, 45 U.S.C. 160 and 181, it is hereby ordered as follows:

Section 1. Establishment of Emergency Board ("Board"). There is established, effective February 15, 1997, a Board of three members to be appointed by the President to investigate this dispute. No member shall be pecuniarily or otherwise interested in any organization of airline employees or any air carrier. The Board shall perform its functions subject to the availability of funds.

Sec. 2. Report. The Board shall report to the President with respect to the dispute within 30 days of its creation.

Sec. 3. Maintaining Conditions. As provided by section 10 of the Act, from the date of the creation of the Board and for 30 days after the Board has submitted its report to the President, no change in the conditions out of which the dispute arose shall be made by the parties to the controversy, except by agreement of the parties.

Sec. 4. Records Maintenance. The records and files of the Board are records of the Office of the President and upon the Board's termination shall be maintained in the physical custody of the National Mediation Board.

Sec. 5. Expiration. The Board shall terminate upon the submission of the report provided for in sections 2 and 3 of this order.

William J. Clinton

THE WHITE HOUSE,

February 15, 1997.