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BEFORE THE

U.S. SENATE
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION
SUBCOMMITTEE ON AVIATION

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REGARDING

MERGERS, ACQUISITIONS, AND OTHER FINANCIAL TRANSACTIONS
IN THE AIRLINE INDUSTRY,
AND THEIR EFFECT ON AIRLINE EMPLOYEES

Thank you for the opportunity to appear before your subcommittee today to discuss the Department of Transportation's views on the imposition of labor protective provisions, or LPP's as they are commonly referred to, in cases involving section 408 of the Federal Aviation Act.

Congress has provided, through the Railway Labor Act, that disputes involving wages, seniority, and other conditions of the workplace in the airline industry be resolved through the collective bargaining process. This is consistent with the treatment of labor-management disputes in virtually all other sectors of our economy. Except where LPP's are warranted by special circumstances, such as the occurrence of a systemic disruption, airline management and employees should rely on collective bargaining, and not mandatory LPP's, as the means of resolving

labor disputes arising out of proposed mergers and acquisitions. The Department will not act in place of the National Mediation Board for the airline industry, nor insinuate itself into the collective bargaining process.

Before the enactment of the Airline Deregulation Act of 1978, the Civil Aeronautics Board routinely imposed LPP's as a condition to its approval of mergers and acquisitions under section 408 of the Federal Aviation Act, but less routinely as a condition to its approval of route transfers. The LPP's generally provide that employees whose jobs are lost, downgraded, or transferred as a result of an airline acquisition or merger are entitled to financial compensation from their employer. LPP's also require the carriers to integrate the seniority lists for the two carriers' employees on a fair and equitable basis.

The rationale for imposing LPP's was that, under a highly regulated system of air transportation with extremely limited and time consuming opportunities for additional route entry, measures needed to be taken to mitigate the prospect of disruption of the air transportation network due to labor strife arising from the implementation of an approved merger or acquisition. The focus of the Board's concern, however, was the stability of the nation's air transportation system, and not employee welfare.

With deregulation of the nation's airline industry, carriers gained the freedom to enter all domestic routes and many international routes based upon the relative demand for additional service in the market. Moreover, the United States' adoption of pro-competitive policies led to an increase in the number of U.S. and foreign carriers serving most limited entry markets. As a result of these changes, a labor dispute involving an individual carrier's operations no longer held such ominous implications for the overall national air transportation system. If one carrier cuts back service, another airline is easily able to enter the market.

The first case in which the CAB considered the issue of LPP's after enactment of the Airline Deregulation Act was the Texas International-National Acquisition Case. The Board announced in that decision that it would only impose LPP's where required by "special circumstances". Although it did impose LPP's in that instance because the labor parties did not have notice of the Board's new standards, the Board made clear that it would no longer routinely condition section 408 transactions with LPP's.

The CAB subsequently refined the standards that it used to evaluate the need to impose LPP's. The Board stated that it would generally limit LPP's to those circumstances where it believed they were necessary "to mitigate possible labor strife that would

adversely affect air transportation as a whole." This standard has been followed consistently in recent years by the CAB, and now, by the Department. It reflects the historic concern for the stability of the air transportation network that has always been present when considering the need to impose LPP's; it also recognizes the fact that any relationship between the stability of the system and a labor dispute at a particular carrier has become substantially attenuated as a result of deregulation.

It is consistent with the policies of deregulation, and with the treatment of other unregulated industries, to allow the private parties to a proposed transaction to come to agreement among themselves on the appropriate protections to be afforded employees in the event of a merger, acquisition, or route transfer. Labor interests are represented in this process through collective bargaining with carrier management. Where all sides have agreed to the LPP-type benefits as a condition to a proposed transaction, there is no need for intervention by the reviewing agency. However, where no prior agreement has been reached, regulatory intervention could serve to undermine the collective bargaining process by encouraging one side to achieve by government order what it could not accomplish at the bargaining table.

At the Department of Transportation, we first considered the question of LPP's in the context of two airline acquisition cases,

the Midway-Air Florida Acquisition Show Cause Proceeding and the Southwest Airlines-Muse Air Acquisition Show Cause Proceeding. In both cases the Department clearly stated that it would continue to assess the need for LPP's based upon the potential for labor unrest which might disrupt the national air transportation system. However no party, in either case, sought to demonstrate that this potential existed if the transactions were approved without mandatory LPP's. Therefore, the Department found no basis to condition its approval on the imposition of LPP's. The rationale for these decisions is consistent with precedent that we have inherited from the CAB, as well as with the policies and principles of deregulation which seek to reduce governmental interference in the allocation of economic resources.

Although the standards for the imposition of LPP's were not met by the Labor parties participating in either of these cases, the Department also noted that imposing LPP's would be unlikely to benefit any of the affected employees, and might even place them in a more disadvantageous position.

The Midway-Air Florida case concerned Midway's proposed acquisition of Air Florida's assets. Air Florida had filed for bankruptcy in the summer of 1984 and suspended all operations. It was able to resume operations later that year only because Midway had provided financial assistance under a joint operating agreement. Midway also agreed to purchase all of Air Florida's assets, subject to the Department's approval under section 408.

However, Midway stated that it would not go forward with the purchase if the Department were to impose LPP's, thereby ending any possibility of Air Florida employees retaining their current jobs. Based upon these circumstances, the Department concluded that the imposition of LPP's would not benefit the Air Florida employees.

In the Southwest-Muse case the Department also found that requiring LPP's might reduce the job opportunities of workers at the acquired carrier. Muse was experiencing serious financial difficulties, and its ability to continue operating, absent the acquisition by Southwest, was doubtful. Southwest repeatedly stated that it would not acquire Muse if the Department imposed LPP's. As a result, the Department determined that the "imposition of LPP's could cause the employees of Muse to lose their jobs, an outcome that would clearly be inconsistent with their welfare."

The Department also considered the issue of LPP's in the Pacific Division Transfer Case, which involved the transfer of Pan American's Pacific route authority to United Airlines. Relying on the policy applied in CAB precedent, as well as in the Department's recent decisions in the acquisition cases which I have just discussed, the Secretary found that the proponents of LPP's had not demonstrated that the air transportation system was, as a whole, likely to experience disruption due to any potential labor unrest resulting from the implementation of the route

transfer, and had not shown any reason why the past LPP policy should not be applied. The Secretary recognized that a strike might cause some passenger inconvenience on routes served by United and Pan American, but that no threat to the overall air transportation system was likely. As the Secretary pointed out, both Pan American and United experienced major system-wide labor strikes earlier this year without any destabilization of the nation's air transportation system.

As the Secretary noted in the Pacific Division case, were the government to impose the kinds of conditions requested by the labor parties, it would place the airline industry in an entirely different position from enterprises in other sectors of our economy. Such a result would be inconsistent with both the policies and principles of airline deregulation.

Deregulation has brought air travelers a significant improvement in the choice of available services and fares in most markets. It has also allowed the airline industry the freedom to respond to market demands with a minimum of regulatory intrusion. However, with this freedom to compete comes the challenge of developing an efficient cost structure. Before deregulation, when fares were set by the CAB, the costs of doing business, including employee salaries, were automatically passed on to passengers in an environment largely devoid of meaningful competition.

Today, however, carriers whose work rules, employment levels, and wage structures were developed during the era of regulation must compete in an open market with low-cost airlines that began service after deregulation. As carriers continue to align their cost structures with the needs of a competitive environment, it will remain necessary for carrier management and employees to sit down together and reach agreement on a program that best meets the needs of both sides.

One thing is certain, however. Neither carrier management nor employees should continue to look to the government to assist in the determination of employment and wage policies. Except where the stability of the national air transportation system is jeopardized, or in other special circumstances, the role of the government must be to remain neutral. To do otherwise could inhibit the collective bargaining process and undermine the development of the competitive environment that Congress sought to promote when it passed the Airline Deregulation Act.

This concludes my prepared testimony. I will be happy to answer any questions that the committee might have.