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UNITED STATES BANKRUPTCY COURT

SOUTHERN DISTRICT OF NEW YORK

Case No. 11-15463(SHL)

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In the Matter of:

AMR CORPORATION,

Debtor.

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U.S. Bankruptcy Court

One Bowling Green

New York, New York

April 26, 2012

9:40 AM

B E F O R E :

HON SEAN H. LANE

U.S. BANKRUPTCY JUDGE

1 TRIAL RE: Doc. #2035 Motion to Reject - Motion of Debtors
2 for Entry of Order Pursuant to U.S.C. 1113 Authorizing
3 Debtors to Reject Collective Bargaining Agreements

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25 Transcribed by: Dawn South, Sherri L. Breach

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P R O C E E D I N G S

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THE CLERK: All rise.

THE COURT: Good morning, please be seated.

All right, any preliminary matters before we proceed with the next witness?

MR. POLLACK: Not from us.

THE COURT: All right. Call your next witness.

MR. POLLACK: Good morning, Judge, the debtors will call Alex Dichter.

THE CLERK: Please raise your right hand.

(Witness Sworn)

THE CLERK: Please state your name for the record.

THE WITNESS: Alexander Dichter.

DIRECT EXAMINATION

BY MR. POLLACK:

Q Good morning, Mr. Dichter.

MR. POLLACK: And for the record I'm Mark Pollack of Paul Hastings as debtor's counsel.

Judge, before we begin I wanted to advise you that union's counsel have raised some questions about this witness's expert qualifications, so I intend to spend a little more time than I did yesterday addressing that.

THE COURT: Fair enough. Thank you.

BY MR. POLLACK:

Q Mr. Dichter, have you ever testified before as an

1 expert witness?

2 A I have not.

3 Q Have you been asked to do so?

4 A Yes, on numerous occasions.

5 Q And why have you not previously?

6 A Up until about a year ago it was against McKinsey
7 policy to do so. Obviously if we were subpoenaed it would
8 be a different story, but we've recently made some policies
9 changes that allow us to do this in selected cases.

10 Q Okay. You mentioned McKinsey and I was going to ask
11 you next how are you currently employed?

12 A I'm a director at McKinsey & Company, that's the
13 equivalent of a senior partner. I also lead our global
14 airline practice and co-lead our global transportation
15 travel and logistics practice, and specific responsibility
16 in that context for Asia Pacific.

17 Q What is the general nature of McKinsey's business?

18 A McKinsey is a management consulting firm. We work with
19 companies, organizations, and governments around the world
20 to help them improve their performance on multiple
21 dimensions.

22 Q And how long have you worked with McKinsey?

23 A Approximately 14 years.

24 Q And over that period have -- have you had occasion to
25 work on other airline engagements?

1 A Yeah, I would say that over 14 years 90 percent of my
2 personal activity has been focused on the airline industry
3 specifically, the remaining 9. something percent focused on
4 things that have something to do with the airline industry,
5 so airline services companies, aircraft manufacturers in
6 some cases. Over the course of 14 years I've done precisely
7 two projects that had nothing to do with the airlines,
8 airplanes, or travel.

9 Q Okay. Now without divulging the identity of your
10 clients, I gather that information is confidential, can you
11 estimate for the Court over the course of your career how
12 many different airlines you provided service to?

13 A Sure. I've personally worked with somewhere between 23
14 and 25 airlines around the world over the course of the last
15 14 years. Of that 23 to 25, 10 of those would be among the
16 top 15 airlines in the world in terms of revenue and 10
17 would be in the top 15 airlines in the world in terms of
18 market cap or valuation.

19 Q Can you estimate how many separate projects you've been
20 asked to work on by those airlines?

21 A I would say over 200.

22 Q And of the engagements -- of the over 200 engagements
23 can you tell us approximately how many of those you lead the
24 engagement team at McKinsey?

25 A Sure. Probably a half to two-thirds, the remainder

1 would be me acting as a -- you know, an advisor on the side
2 where someone else is leading the engagement.

3 Q Again, without getting into any confidential client
4 information, can you generally describe the types of work
5 that you've done for the other airlines?

6 A Sure. Work breaks down into four broad categories, a
7 lot of my personal work has been on strategy topics such as
8 mergers and acquisitions, general trends in the industry,
9 responses to specific discontinuities like high fuel prices
10 or low cost carrier growth.

11 A large portion have been in operational
12 improvement areas, so that would range in productivity,
13 pilot productivity, flight attendant productively, reduction
14 in aircraft turnaround times, aircraft scheduling, baggage
15 transfer, on time performance, things of that nature.

16 A large portion would be on organizational topics,
17 and so that would range from organizational effectiveness,
18 capability building, organization design and restructuring,
19 and in some cases overhead reduction.

20 And then a large portion cuts across those themes
21 in what I would loosely call business planning, and so
22 that's bringing together a number of actions, comparing them
23 against exogenous forecasts to develop a plan over multiple
24 years, and some of those efforts have been for reasonably
25 healthy carriers that are looking to grow and do better, and

1 others have been for carriers that are in the process of
2 restructuring in some form.

3 Q Aside from your client work have you taught any courses
4 on the airline industry?

5 A Yeah, we keep a fairly non-public face at McKinsey, but
6 I have co-lead a case discussion on the airline industry at
7 the Tuck School of Business at Dartmouth several years ago.
8 I've been asked to speak at the MIT transportation club just
9 as examples, and I also teach annual course at McKinsey for
10 new associates on the airline industry.

11 Q Do you speak at industry conferences?

12 A Yes, occasionally. Again, we try to minimize our
13 public face a bit, but I've spoken at the Goldman Sachs Asia
14 Pacific analyst conference, at an industry association
15 conference in Washington, D.C., the Thai Airways 50th
16 anniversary conference in Bangkok in October of 2010, and
17 then coming this June I've been asked to sit on the CEO
18 panel, just the premier event at the International
19 Association of Transport Airlines, that's the -- essentially
20 the premier industry organization that -- to which virtually
21 all network carriers belong in Beijing this coming June.

22 Q Have you had occasion to author any published articles
23 or text on the airline industry?

24 A I have three published articles, one was actually a
25 chapter in a book. The first is a chapter in a book called

1 The Handbook of Airline Finance, which is a series of texts
2 published by McGraw-Hill I believe in 1999 or 2000. The
3 second I believe in 2001 an article in Airline Business on
4 airline merger management. And then the third an article on
5 airline turnarounds, the center of which was an interview
6 with one of our client's CEOs in the McKinsey Quarterly,
7 which is a journal that we publish.

8 Q Aside from your experience at McKinsey have you
9 actually worked within the airline industry?

10 A I have. I was a pilot and instructor at Continental
11 Airlines and before that at Continental Express between 1989
12 and 1997 -- sorry -- between 1989 -- yes, '97. Prior to
13 that I worked at a commuter airline in the Caribbean also as
14 a pilot, and if we really want to go back when I was 13 I
15 worked for a travel agency repricing tickets after school
16 taking advantage of some of the new fare rules that existed
17 post deregulation. At age 15 I did a market development
18 study for Ransome Airlines, they were looking at entering
19 the Bedford, Massachusetts market, which is a market that I
20 knew particularly well.

21 Q Okay. Finally can you briefly describe your
22 educational background?

23 A Sure. I have BS in professional aeronautics from
24 Embraer Aeronautical University where I graduated summa cum
25 laude, and I have an MBA from the Tuck School of Business at

1 Dartmouth College where I graduated with distinction.

2 MR. POLLACK: Your Honor, at this point we would
3 tender Mr. Dichter as an expert on the airline industry.

4 THE COURT: Any objections?

5 MS. PARCELLI: Yes, Your Honor, we object.

6 THE COURT: Basis?

7 MS. PARCELLI: Essentially -- should I just stay
8 here, Your Honor?

9 THE COURT: Wherever, I would just -- thank you,
10 that's -- you took the words right out of my mouth.

11 MS. PARCELLI: Doesn't seem to want to come
12 forward. Okay. I'm fine.

13 Essentially, Your Honor, we don't object to the
14 declaration coming in or we're not seeing to strike any
15 portions of it, we just don't believe it's an appropriately
16 considered expert report in this case.

17 The declaration in the main speaks to work that
18 McKinsey did on the business plan, it's really similar in
19 nature to elements of Ms. Goulet or Mr. Vahidi's
20 declaration, a fact witness, if you will, on kind of
21 information about that process.

22 Also in order to have material considered expert
23 there has to be an explanation of the methodology that has
24 been used in generating the expert report, and we think
25 that's really entirely lacking from the declaration.

1 Simply, you know, if you look at paragraph 6(c)
2 there's reference at the end of that paragraph:

3 "And McKinsey & Company to forecast the financial
4 outcome of the business plan and evaluate the key business
5 choices in the business plan are reasonable and consistent
6 with airline industry common practices and commonly held
7 views."

8 But we don't see any further explanation of the
9 actual sort of methodological analysis that underlies, you
10 know, just this kind of naked assertion of industry
11 practices and commonly held views.

12 Lastly, although Mr. --

13 THE COURT: Well, let me ask you a question. Are
14 you seeking to -- you said you don't have any objection to
15 this report or the direct, however we want to refer to it,
16 meaning his opinions coming in, so what is it that as a
17 practical matter we're talking about here? The weight you
18 want me to give it or is it -- are there particular by
19 virtue of highlighting paragraph (c) are you identifying
20 particular opinions that you have a problem with that you're
21 going seek to exclude?

22 I'm not -- I'm not quite sure where the rubber is
23 going to hit the road on this.

24 MS. PARCELLI: Others may have a different take on
25 it, Your Honor, but from our vantage we would like you to

1 just simply not treat it as an expert report.

2 As I say, it can come in as a declaration of a
3 fact witness, we're not challenging that, but --

4 THE COURT: Well, but here's the problem. If he
5 has an opinion such as the ones expressed -- and maybe what
6 we can do is this may be a longer conversation -- if you
7 want to just come down off the stand and maybe make yourself
8 comfortable somewhere unless somebody -- unless you had no
9 objection to him being present for all this colloquy back
10 and forth.

11 MS. PARCELLI: It's Your Honor's preference is
12 fine.

13 THE COURT: Right. Well, if you can survive
14 sitting there and just make yourself comfort.

15 (Laughter)

16 THE WITNESS: I get that it's not personal.

17 THE COURT: All right. If he has an opinion and
18 it is forward looking as opposed to merely historical events
19 then it would seem odd, given his qualifications, to treat
20 it as a layperson's opinion, which is permissible under the
21 Federal Rules of Evidence, but it doesn't really seem to be
22 a layperson opinion. I mean that's more how fast did you
23 think the car was going when it hit the other car? That's a
24 layperson opinion. I don't think that's what this is. I
25 think it's an opinion based on his qualifications.

1 Given that you don't object to the -- this coming
2 in in terms of its substance, perhaps we can table this and
3 if you want to pursue it in terms of being able to tell me
4 if there are any practical consequences to it, but I guess
5 if you don't have any objection to his testimony coming in
6 and what's going to be discussed today in terms of the
7 merits, it's obviously informed by his background regardless
8 of how he's considered.

9 But what I'll do right now is I'm not going to
10 rule on that since really there's nothing for me to exclude,
11 but if it -- if it turns out to have some practical
12 consequences I'll consider you to put in a place holder,
13 then we can discuss it more fully in the future.

14 MS. PARCELLI: I appreciate that, Your Honor, and
15 I'm very open to doing that. May I just ask for debtors to
16 make a clarification in terms of precisely what expertise
17 they are asserting for Mr. Dichter? That may help.

18 MR. POLLACK: Well, he's as an expert with respect
19 to the operations and strategic choices of the airline
20 industry, and we are going to be eliciting certain opinions
21 consistent with his experience, Judge.

22 THE COURT: Well, and that's where I'm -- I'm sort
23 of wondering about the practical consequences. If he was
24 hired because of his expertise to consult and offer opinions
25 and we're okay with all of that historically coming in I

1 don't know really where to draw the line if we're talking
2 about his expert opinion here, because it seems to be, as
3 you said, kind of the same thing.

4 So -- and again, I don't think it's lay opinion,
5 it seems to be informed by specialized expertise. I don't
6 have the relevant rules in front of me, but -- but again, I
7 think we can put a pin in it, if it has practical
8 consequences in the future we can discuss those at a later
9 time.

10 Anyone else want to be heard?

11 MS. KRIEGER: Yes, Your Honor, Kathy Krieger for
12 the Allied Pilots Association.

13 We too I think may have some concerns about some
14 of the opinions being expressed being beyond the scope of
15 any qualifications or aviation industry business expertise,
16 and as we understand it following the close of cross that's
17 when objections are being taken up when Mr. Pollack moves
18 the admission of the declaration, and there are some
19 paragraphs in the declaration that we may want to discuss
20 with Mr. Pollack objecting to, because the opinions
21 expressed there go beyond the scope of what he's being
22 presented as an expert in.

23 THE COURT: All right.

24 MS. KRIEGER: And I think that would be --

25 THE COURT: Well, that's a different problem --

1 MS. KRIEGER: Yes.

2 THE COURT: -- that's a scope problem.

3 MS. KRIEGER: And I just wanted to say, I am not
4 prepared to say right now that blanket we have no objection
5 to all the paragraphs in the declaration coming in --

6 THE COURT: That's fine.

7 MS. KRIEGER: -- but we will deal with them after
8 the cross.

9 Thank you.

10 THE COURT: All right. But I understand you don't
11 have a -- you don't have an objection to him being presented
12 and qualified as a witness, what you have a problem with is
13 you think there may be some topics that are beyond the scope
14 of his expertise, and you'll identify those at -- when we
15 get to that part of the program.

16 MS. KRIEGER: Correct, Your Honor.

17 THE COURT: All right.

18 MR. SHERWOOD: Your Honor, Jack Sherwood,
19 Lowenstein for the TWU. We also join in the objection, and
20 specifically --

21 THE COURT: All right, which one? Because there
22 are two different ones. The scope and the other is -- is
23 the notion of this witness as an expert as opposed to a fact
24 witness.

25 MR. SHERWOOD: Really both, Your Honor.

1 I think in terms of scope we are focused on the
2 parts of his opinion that talk about reduction in labor
3 costs, maintenance, fleet service, and the like, and we
4 don't think a foundation has been laid that he has expertise
5 in those areas.

6 And also with regard to methodology as to how he
7 arrived at the conclusions that --

8 THE COURT: Right.

9 MR. SHERWOOD: -- I think he's going to offer.

10 THE COURT: I think I'll have to hear a little bit
11 more before I decide on any of that.

12 But all right, what I'll ask is that once we get
13 through the direct parties can then identify if there's
14 anything specifically they wish to exclude, which I think
15 really is the operative question for purposes of today, and
16 I either may make a ruling on that or I may take it under
17 advisement, depending on the circumstances.

18 MS. PARCELLI: Thank you.

19 THE COURT: Proceed.

20 MR. POLLACK: Thank you, Judge.

21 THE COURT: And obviously given those objections I
22 think it's appropriate for you to address whatever topics
23 you wish to address in terms of the direct, because it puts
24 this witness in a -- you know, in a particular posture,
25 so --

1 MR. POLLACK: And I appreciate the comments of
2 counsel and I will speak to the methodological issues that
3 were raised.

4 I should say that the union's counsel, as is their
5 prerogative, made wholesale evidentiary objections virtually
6 to every paragraph of the declaration.

7 I don't think it's going to be an effective use of
8 the Court's time to go through every paragraph, and so my
9 preference, if it's acceptable to Your Honor, is to await
10 the specific cross-examination, see where they have issues
11 as to scope of opinions, and then I'll redirect on those
12 rather than trying just now --

13 THE COURT: That's fine. I'll leave it -- I'll
14 leave it to your wisdom, but I guess what I'm saying is I
15 certainly have been trying to move proceedings along, and --
16 but I recognize when there is an issue joined it changes --
17 it changes how things have to proceed, so I don't want to
18 cut anybody off, because obviously you're going to have to
19 address those topics that have been identified.

20 So however you think is most efficient to do that,
21 whether it's in the direct, whether it's in redirect I'm
22 certainly open to suggestions, and I'm sure -- I'm sure your
23 methodology sounds -- is a wise way to proceed.

24 MR. POLLACK: Thank you, Judge.

25 DIRECT EXAMINATION (Resumed)

1 BY MR. POLLACK:

2 Q Mr. Dichter, when was McKinsey retained by American in
3 connection with its bankruptcy proceeding?

4 A During the first half of December, 2011.

5 Q And what was the nature of the firm's engagement?

6 A We were asked to review the business plan.

7 Q Did you have a specific role with respect to the
8 revenue model that we've heard testimony about?

9 A We did. That was I would say the primary focus of our
10 engagement. We were asked to build a driver-based revenue
11 forecast model that would predict the revenue outcome of the
12 business choices in American's plan.

13 Q Okay. And what was your role with respect the
14 McKinsey's engagement?

15 A My primary role was to advise the McKinsey team that
16 was on the ground day-to-day, and specifically I designed
17 the architecture for this specific application of the model,
18 I pointed the team to the analysis that we would need to do
19 to be able to do this, the data sources that they ought to
20 use, and I had direct interface with several American
21 executives discussing this methodology and getting aligned
22 and getting comfortable that this was the right path
23 forward.

24 Q Who were the American executives that you principally
25 interacted with?

1 A Beverly Goulet, Candice Irvin, as well as three
2 executives from the commercial team, Virasb Vahidi, Don
3 Casey, and Chuck Schubert.

4 Q And by at the way, you were in court yesterday
5 listening to Mr. Vahidi's testimony?

6 A I caught the most part of it, not all of it.

7 Q Okay. Were there any other professionals outside of
8 McKinsey that assisted with the American engagement?

9 A Yes, Rothschild, several law firms, I believe a couple
10 of expert witnesses -- well, Kasper of course I've read his
11 declaration, and that was important in our process, perhaps
12 others.

13 Q What were the respective areas of focus between
14 McKinsey and Rothschild in working with American?

15 A Sure. Again, our primary focus was to develop the
16 revenue outcome of the plan. We also looked at alternatives
17 to the plan, both the network configuration and basic
18 business choices incorporated in the plan.

19 We looked also at costs. The bulk of that focus
20 was on non-labor costs, but we did a brief benchmarking
21 exercise on the labor costs as well.

22 Rothschild's focus as I understand it was to focus
23 on the financial metrics that would be required for American
24 as an entity to be successful post bankruptcy.

25 Q Did you prepare a written declaration summarizing your

1 testimony in the case?

2 A Yes, I did.

3 Q And you have a binder I believe on your witness stand.

4 If you can look at the first tab, which we've marked for
5 identification as American Exhibit 400. And just confirm
6 that that is your declaration?

7 A This is my declaration.

8 Q Do you adopt your declaration as your testimony in
9 court here today?

10 A I do.

11 Q If I can direct your attention to Appendix B, the very
12 last page of your declaration. You describe there the
13 various source materials that you considered in forming the
14 opinions and conclusions you've rendered in your
15 declaration.

16 A Yes.

17 Q And we're going to discuss those --

18 A Okay.

19 Q -- in some detail later on.

20 So you heard the colloquy earlier about the
21 architecture and methodology, and I do want to spend some
22 time understanding that.

23 A Sure.

24 Q When did your work begin in creating a revenue model
25 for American?

1 A Within hours after the confirmation of our engagement.
2 The date is the laid out in our engagement letter, and in my
3 declaration as well, I believe it was December 11th.

4 Q Now did American have a preexisting revenue plan or
5 model?

6 A Yes, they did. I'm not terribly familiar with the
7 workings of their model, our plan again was forward looking,
8 and an important principal of our process was that our
9 approach should be independent. American executives were
10 quite interested in making sure that the revenue forecast
11 that was developed was robust, driver-based, transparent.

12 But my understanding is that the model that
13 American used uses regression analysis and trend forecasting
14 to predict a revenue outcome from a given plan. And the
15 basic idea behind this is that it takes revenue production
16 in a given year, looks at what's different in the next year
17 or what we believe to be different in the next year, changes
18 in the economic environment, industry capacity, fuel prices,
19 and the overall change in production, available seat miles
20 that American is proposing, and based on historical
21 correlations predicts a revenue outcome associated with
22 those changes.

23 That is a fairly top-down methodology, and by the
24 way, perfectly sufficient for day-to-day business planning.

25 Q Did you use that methodology in your engagement?

1 A No, we didn't. Again, we started from scratch for the
2 most part using a different methodology.

3 It's our view that in bankruptcy proceeding the
4 level of transparency required around process is much higher
5 than it would be within a day-to-day corporate process.

6 Our model is designed to connect the underlying
7 observable drivers of revenue performance in specific market
8 areas to a revenue forecast.

9 Q Now, without getting into confidential details, I do
10 want you to describe how you went about building your model.

11 A Sure. Basically we divided the world into a number of
12 specific market flows, and these are at an aggregate level.

13 We looked at flows basically from specific
14 cornerstones to specific regions, and so for example, Los
15 Angeles to Asia, Los Angeles to southern Latin America, Los
16 Angeles to northern Latin America, for examples.

17 We also looked at cornerstone to cornerstone
18 markets individually inasmuch as that's a large portion of
19 American's business, so Los Angeles to New York, Los Angeles
20 to Miami.

21 Q And to be clear when you're referring to cornerstones
22 are you referring to the five --

23 A I'm referring to the five key cities in American
24 Airlines' network, that's correct.

25 In each one of those cells we then looked at three

1 exogenous drivers of revenue performance.

2 One is industry capacity growth. The other one is
3 industry demand growth. And then the third is nominal yield
4 inflation. And what I mean by that is all other things
5 being equal corrected for fuel price changes at what rate do
6 prices generally change?

7 The three of those by the way --

8 Q I want to go through each of those.

9 A Okay, sure.

10 Q So let's start with the assumptions around capacity
11 growth.

12 A Sure.

13 Q How did you go about constructing those?

14 A Different by period of time. For 2012 capacity is
15 reasonably known, and in fact into a portion of 2013 it's
16 known, but what I mean by that is airlines have published
17 their schedules, and while airlines don't always fly their
18 schedules precisely as flown we're within a rounding error.

19 For 2013 and 2014 the order pipeline, so in other
20 words the aircraft that are being built by manufacturers and
21 delivered to given airlines, is also reasonably known. If
22 we want to -- any individual airline wanted to significantly
23 change its order book in the next two years -- not to say
24 that that's impossible, but it's hard -- and the accuracy
25 level within that time frame is quite good.

1 Beyond 2014 order book information is not terribly
2 reliable, and so we made the assumption that industry
3 capacity continues to grow at the same gap to industry
4 demands. And so wherever we left off we just continue that
5 industry equilibrium, if you will.

6 Q Now let me stop you here.

7 A Yeah.

8 Q Is the approach that you just described for forecasting
9 future capacity growth consistent with what you've done for
10 other airlines and what experts in the field generally use?

11 A Well, it's consistent with what we do with other
12 airlines, it's also consistent with what airlines do on
13 their own.

14 So I've never seen an airline plan that doesn't
15 include a capacity forecast, and the basic principal is you
16 want to be as accurate as possible when that information is
17 reliable, and once you get beyond a certain period of time
18 you have to use assumptions about capacity growth.

19 Q Okay. Let -- if you can now turn to the demand
20 assumptions.

21 A Sure.

22 Q And the basis on which those were constructed.

23 THE COURT: Let me just ask a question about
24 capacity. You said I think you were doing this -- looking
25 at three factors for each cell?

1 THE WITNESS: Yes.

2 THE COURT: Could you --

3 THE WITNESS: Yes.

4 THE COURT: -- could you explain that term?

5 THE WITNESS: That's actually a very good
6 question, you're listening carefully.

7 (Laughter)

8 MR. POLLACK: Apparently better than I am.

9 (Laughter)

10 THE WITNESS: Obviously we can look at capacity on
11 an industry basis, but it's a big world and that's not how
12 competition plays out, and so we did assign that capacity to
13 these cells. And the basic by which we assigned this
14 capacity again in 2012 was based on actual schedule
15 information. So airlines have shown their cards for the
16 most part and let us know where they're planning to put
17 their capacity.

18 For years 2013 and beyond we assumed that airlines
19 added capacity roughly in line with their current network
20 footprint adjusted for industry growth rates. And so in
21 other words if United Airlines is at a certain level in San
22 Francisco and the industry between San Francisco and Asia is
23 growing at let's say eight percent, we assume that United
24 Airlines grows between San Francisco and Asia at eight
25 percent and that absorbs that portion of industry capacity.

1 THE COURT: Thank you.

2 MR. POLLACK: Thank you, Judge.

3 BY MR. POLLACK:

4 Q With respect to demand, how did you go about building
5 the assumptions on that metric?

6 A Sure. There are relatively well understood and
7 constant co-efficients between GDP growth and traffic
8 growth. Broadly traffic grows slightly in excess of GDP.
9 Those relationships are somewhat different by market, and so
10 we tend to see a higher multiple in emerging markets where
11 air travel is new than in mature markets where everybody is
12 used to traveling. Put differently, I don't really want to
13 travel anymore, and you know, I'm kind of done, but if
14 you're only traveling once every couple of years there's
15 lots of potential there.

16 We then took GDP growth forecast by global
17 insights for each region. And so if we're looking at Los
18 Angeles to southern Latin America, for instance, we took
19 U.S. GDP growth rates times the U.S. GDP to traffic
20 multiplier, we took southern Latin America GDP growth rates
21 as a composite times the southern Latin America GDP to
22 traffic multiplier, and then we weighted that based on the
23 percentage of traffic that's historically been sold by
24 either end in American's networks.

25 And so just to be clear about that point, when

1 American runs a flight between, you know, Dallas and Brazil,
2 for instance, it's not always the case that 50 percent of
3 that traffic would be sold in the U.S. and 50 percent of
4 that traffic would be sold in Brazil. Markets are not
5 balanced in that way.

6 Q And so how did you weight for -- just to use your
7 example, if 80 percent of the traffic originates in the
8 U.S., 20 percentage in Brazil, how did you then go --

9 A Sure.

10 Q -- apply the GDP assumptions?

11 A Eighty percent times the U.S. GDP growth rate times the
12 historical U.S. GDP to traffic multiplier, times 20 percent,
13 times the southern Latin America GDP growth rate, times the
14 historical southern Latin America GDP to traffic multiplier.

15 Q Okay. And you described the third element of the
16 methodology as an inflation adjustment.

17 A Yes.

18 Q Can you just briefly summarize --

19 A Sure.

20 Q -- the nature of that assumption?

21 A We looked at 30 years of industry yield. Yield is
22 essentially the average ticket price per mile paid by a
23 customer or per kilometer depending on where you sit. We
24 adjusted for fuel price. Fuel price has a significant
25 influence on yields. In a world of higher fuel prices

1 ticket prices are higher, and so you need to adjust for fuel
2 prices. And that got us to a nominal growth rate -- I'm not
3 sure if this is confidential or not -- but perhaps not
4 important, but --

5 Q Yeah, I'm not going to ask you to disclose --

6 A Okay, sure.

7 Q -- specific rates, just the process.

8 A Any way, it's a nominal growth rate that's consistent
9 with 30 years of industry history.

10 Q Okay. And if you could just take a moment just to flip
11 to Section 6 of your declaration, which begins at page 16.

12 MR. POLLACK: For the record paragraphs 21
13 through 25.

14 BY MR. POLLACK:

15 Q Do you summarize there the methodological assumptions
16 that you just elaborated on in your testimony today?

17 A I'm sorry, I'm not sure I understand the question.

18 Q In section 6 of your declaration, paragraphs 21
19 through 25.

20 A Yes.

21 Q My question simply is, did you attempt to summarize
22 there --

23 A Oh, yes, yes I did. Sorry, I thought you were asking
24 me to summarize again.

25 Q No, no.

1 A That would be repeating what I just said, but --

2 Q Okay. The driver-base model that you applied in this
3 engagement, was this the first time that McKinsey applied
4 that model to airline forecasting?

5 A No, it isn't.

6 Q Without disclosing particular airlines, have you
7 applied this -- well, let me ask it this way.

8 Have you had occasion to test the reliability of
9 this model on other engagements?

10 A Yes, we have.

11 Q Can you explain how you've done that?

12 A Sure. Shortly after we first developed the model we of
13 course wanted to test it, and so we had occasion to use the
14 model to essentially rebuild the P&L for a known year, and
15 so we took one of our airline clients and worked backwards
16 in time and took all of the assumptions that had been
17 present in the market a year prior, fed them into the model
18 based on the network plan that had existed at that time and
19 use the model to predict a revenue outcome, and in this case
20 a cost outcome as well for a year where the outcome was
21 known. We then compared that to the known result and were
22 literally within a rounding error.

23 Q Okay. Now you mentioned that McKinsey was engaged to
24 provide an independent perspective on the revenue model.

25 Did you interact with American Airlines personnel as you

1 developed the model?

2 A Yes, we certainly did. I mean on the one hand
3 everyone, including us, felt that it was important that we
4 be independent from an intellectual standpoint, meaning if
5 we fundamentally believed based on our industry knowledge
6 that market growth rates were going to be no more than X
7 that as long as we believed that that ought to be the
8 assumption used in the process.

9 That said, we had extensive back and forth with
10 American executives, and believed also that the output of
11 this should be something that was owned by them.

12 And so there were cases where American executives
13 had a different viewpoint than we had and we would debate
14 those viewpoints, and in some cases they convinced us, in
15 other cases we convinced them.

16 Q Were there strategic initiatives unique to American
17 Airlines that impacted your revenue model?

18 A Sure. So in addition to the three exogenous factors by
19 cell we looked at a number of business choice or strategic
20 overlays again by cell. These have been talked about I
21 think extensively both in my declaration and other testimony
22 today.

23 But those include, but are not limited to, market
24 share shifts within a cell, so all other things being equal,
25 airlines do better in markets where they have high market

1 share than when they have low market share.

2 We looked at the gauge changes proposed in the
3 plan and the impact that they would have on revenue
4 performance. We looked at the completion of the joint
5 business agreements. The expansion of domestic code share,
6 and also the impact of product upgrades, which were largely
7 the exception of a small amount, largely focused for
8 reversing a decline in revenue rather than necessarily
9 driving additional growth.

10 Q Okay. Mr. Dichter, I want to be sensitive to the
11 terminology that we use. You explained that you focused on
12 a particular cell, and earlier you explained to the Court
13 that that may have different meanings depending on its
14 application. How did you use it in your answer here?

15 A In a specific -- I mean a specific market flow, as I
16 described, Los Angeles to Latin America, Los Angeles to
17 Asia.

18 Q All right. Without getting into the specific numbers,
19 did you make assumptions relative to American's market share
20 across this network?

21 A Assumptions is probably the wrong word. We made
22 assumptions about where industry capacity went, as I
23 described to the judge earlier. American's network plan,
24 combined with the application of an assumption of where
25 industry capacity goes and overall market growth, yields a

1 market share as an output.

2 Q And again, I don't want to speak to the number --

3 A Sure.

4 Q -- but in relative terms what was that yield -- market
5 shared yield?

6 A Sure. So overall if you look across the network
7 American's capacity grows within a decimal point rounding
8 error within industry capacity. And so basically if you
9 look at the industry as a whole American is projected to
10 grow in line with its peers. And so you'd see very little
11 market share change on an aggregate level at all.

12 Obviously in specific markets when you get down to
13 a specific origin and destination pair -- and specifically a
14 specific route -- if American is proposing to add a flight
15 on that route that obviously has an impact in market share,
16 but of course every single time any airline adds a flight
17 anywhere, or for that matter any company introduces a
18 product into a new market, it impacts market share.

19 Q We've heard testimony about unit rates measured in
20 terms variously of RASM and PRASM. Can you explain what
21 those terms refer to?

22 A Sure. Revenue (sic) is revenue per available seat
23 mile. So you take all the revenue that a company earns and
24 divide it by all of the available seat miles that the
25 network produces.

1 PRASM specifically focuses on passenger revenue
2 per available seat mile.

3 And the difference in the non-passenger revenue
4 you would include things like cargo, certain ancillary fees,
5 some of the revenue that you might get from selling services
6 to third parties, et cetera.

7 Q Okay. Over the course of the -- well, first let me ask
8 you.

9 What period of time did the model forecast
10 revenues for American?

11 A From 2012 to 2017.

12 Q And over that period what rate assumptions did the
13 model yield? Let me rephrase that question.

14 How does American's RASM compare over the course
15 of that period to the industry average?

16 A Sure. Again, I believe the specific number is
17 confidential --

18 Q It is.

19 A -- but American's PRASM growth and RASM growth for that
20 matter over that period are in line with historical trends,
21 net of a bit of a correction in the first few years. So
22 obviously the actions that are contemplated in the plan help
23 bring American back up to what we would consider to be its
24 rightful level based on its network footprint.

25 Q Presently how does American's RASM and PRASM compare to

1 its peers?

2 A American's RASM and PRASM has been declining over the
3 last few years. It's still up until around the first
4 quarter of 2011 been above the average of its peers, as I
5 believe Mr. Vahidi testified, since the first quarter of
6 2011 it's actually dropped below.

7 Q Okay. Now taking into account all of the variables
8 that you've summarized here, did the revenue model yield a
9 certain amount of incremental revenues beyond what would be
10 projected just from normal expected capacity growth?

11 A It did. So again, there's a reasonable growth
12 associated just with the capacity that American is proposing
13 to put online and industry yield growth, but basically by
14 2017 the actions that American has contemplated should yield
15 roughly -- and I believe this is now a public number --

16 Q It is.

17 A -- a billion dollars in incremental revenue above and
18 beyond normal growth rates.

19 Q And does that incremental increase in revenue occur
20 linearly over that six-year period?

21 A Depends a little bit by source. I can go through each
22 source if it's helpful.

23 Q If you would, yes.

24 A The joint business agreements are already partially
25 implemented and the model proposes that those continue to --

1 is that okay?

2 Q I just want to cautious you not to use numbers.

3 A No, I will not.

4 Q Thank you.

5 A Continue over the course of the next two to three
6 years. The increase in large regional jet flying starts in
7 2013 or so and is reasonably linear over the course of the
8 period. The product upgrades are concentrated in the 2012,
9 some of these are already under way by the way through
10 2015ish or so, and then linear beyond there.

11 Domestic code sharing, I actually think the date
12 might be confidential, but let's just say that it's -- the
13 beginning of the benefits from domestic code share are
14 consistent with the normal amount of time that you'd expect
15 an airline to engage with potential partners, complete those
16 negotiations, and implement those code shares from an
17 operational standpoint. And so it's neither by any means
18 immediate nor is it at the tail end of the period. I don't
19 think I've missed anything.

20 Q Was there a small amount of incremental revenues
21 associated with the product upgrades?

22 A There is. This is one that has two components. The
23 vast majority of the product upgrades are focused on what we
24 would consider catch ups to the industry.

25 So as has been pointed out by others, while

1 American's competitors have invested in fully flat seats in
2 business class, significant roll out of in-flight wireless
3 connectivity, in-flight entertainment, expanded overhead
4 bins, American has been a little bit behind its peers in
5 those upgrades.

6 And so it's our view that those particular
7 upgrades will not yield a revenue advantage for American,
8 those are partly responsible for the revenue decline that
9 we've seen.

10 And so we modeled that as part of the drivers of
11 bringing American back up to industry par, if you will.

12 There are some actions that may or may not be
13 confidential around a specific product plan in the --

14 Q I don't want to get into that.

15 A In a specific market, which we believe would be
16 incremental revenue on top of that, but it's a very small
17 portion of the total.

18 Q Okay. Based on your experience do you have an opinion
19 as to whether the incremental revenue enhancements that you
20 eluded to the million dollars annually by 2017 are
21 reasonable and attainable?

22 A Yes, I do. I think I specifically focus on the value
23 of those actions relative to American's revenue production.
24 I think the methodology that we use yields a fairly accurate
25 prediction of what the value of those levers will be. And

1 so we're quite confident that those are both feasible from
2 an execution standpoint as well as will yield benefits in
3 that range.

4 Q Okay. I want to step back for a moment and refer to
5 some of the other aspects of McKinsey's engagement.

6 You described at the outset that among the
7 elements of your engagement you were asked to look at other
8 alternatives that American --

9 A That's correct.

10 Q -- might deploy in its business plan.

11 A That's correct.

12 Q Can you explain what you did in that regard?

13 A Sure. First of all it's worth noting that -- and I
14 believe I said this in my declaration -- that the strategic
15 alternatives available to airlines are significantly limited
16 by the choices that their competitors have made, and so put
17 differently -- and I think I used this example in my
18 declaration -- you know, we didn't look at building a hub in
19 Atlanta, Delta has a large hub in Atlanta, that would be,
20 you know, something akin to industry suicide.

21 Neither did we really look at turning American
22 into a completely different kind of airline, turning
23 American into an LCC, for instance, that would have required
24 cost reductions well in excess of what are contemplated in
25 the plan.

1 We really looked at two dimensions. One was
2 operating from fewer key hub cities, or as have been
3 referred to, cornerstones. And two is shrinking the
4 airline.

5 We did not look at expanding the airline. And
6 again, the reason we didn't do that was, as has been pointed
7 out by several parties in these proceedings, growing well in
8 excess of industry growth rates can have a destructive
9 effect both of our own yields as well as on industry yields.

10 So as we looked at the possibility to reduce
11 cornerstones we thought about that in two ways.

12 One scenario was a scenario in which we removed a
13 cornerstone from the system and removed that capacity from
14 the system, so you ended up with a smaller airline.

15 The other scenario was a scenario in which you
16 removed a cornerstone and redeployed that capacity into the
17 remaining cornerstones.

18 Q Okay. What conclusions did you draw --

19 A Sure.

20 Q -- from those scenarios?

21 A The early outcome of that analysis yielded very, very
22 strong negative results for both of those scenarios. When I
23 say very strong -- can I share a number here or should I
24 share a number here? Let's say that at a level that would
25 result in American being well off even the range of EBITDAR

1 targets that were discussed by Rothschild.

2 Based on the strength of that analysis we stopped
3 that analysis. Meaning --

4 Q Let me stop you.

5 A Yeah.

6 Q Did you share that analysis with executives at
7 American?

8 A Yeah, we had conversations with several executives at
9 American about the output of that analysis, we discussed the
10 order of magnitude of the results, the methodology and the
11 process that we'd used, and we jointly decided to stop that
12 analysis as it was unlikely that any or perhaps even
13 impossible that any further level of granularity would
14 change the direction of those results.

15 Q You also explained that part of your task was to
16 benchmark certain cost elements at American Airlines.

17 Let me first ask you about what you were asked to
18 do and did do with respect to non-labor costs.

19 A Sure. With non-labor costs we were asked to look at
20 American's non-labor costs by category and do three things.

21 One, benchmark those costs against peers, see
22 whether or not they were in line.

23 Two, look at the initiatives that American had
24 launched over time to reduce those costs to see whether or
25 not those initiatives were consistent with initiatives that

1 other airlines have launched.

2 And third, quite frankly as an outcome of that
3 second piece was to see whether there were any material
4 levers that we believed American had overlooked.

5 Q Okay. And with respect to your historical look at the
6 initiatives what did you determine?

7 A That American had materially employed all of the same
8 cost reduction initiatives as had been employed by other
9 peers in the industry, and quite frankly beyond the industry
10 and other markets.

11 Q Generally speaking what type of initiatives did you
12 observe?

13 A These would be fuel cost reduction, productivity
14 improvements, the enhancement of self-service technology
15 that would allow passengers to check in on their own,
16 improvements in sales and distribution costs or negotiations
17 with suppliers, reduction in commission rates, reduction of
18 food content on board the aircraft, improvements in aircraft
19 utilization --

20 Q I'll just ask you to take a breath, the court reporter
21 is having trouble keeping up with you.

22 A Sorry.

23 Q I didn't want to --

24 A Sure, sorry.

25 Q -- prevent you from completing your answer, though.

1 A Anyway, that's a good cross section.

2 Q Okay. Did you find any additional opportunities for
3 non-labor cost reductions?

4 A We did. We pushed on a couple of areas, which I
5 believe are confidential. After discusses with American's
6 executives they decided to incorporate those opportunities
7 in the plan.

8 Q Lastly with respect to your benchmarking a labor cost
9 can you explain the process that you utilized?

10 A Sure. By the way, this was not part of our original
11 engagement letter, our focus was to generate a revenue
12 forecast, understand whether or not the non-labor costs were
13 reasonable, and if not adjust those, and as has been
14 described by others, the labor cost target came about
15 through a number of mechanisms.

16 We did -- we were asked to check to see that the
17 assumptions that American was making around labor cost
18 deferential, vis-à-vis, peers, seemed reasonable in our
19 view, and so we used Form 41 data, which I believe has been
20 described here before, it's a publicly available data
21 source.

22 Q Just quickly summarize what that contains.

23 A Sure. Form 41 is a data source that is collected and
24 maintained and published by the Department of Transportation
25 that all U.S. major airlines -- major airlines are defined

1 as airlines in excess of a billion in revenue I believe --
2 provide data into and it's published back out to the public,
3 and it gives you a reasonable sense by functional category.
4 And what I mean by that is pilot costs, maintenance costs,
5 flight attendant costs, on-board catering is a category,
6 airport and ground handling costs. And you can look at
7 those by a number of denominators. You can look at those on
8 an available seat mile basis or you can compare CASM to
9 CASM, you can look at those on a cost per block hour basis,
10 cost per departure basis, et cetera.

11 Q And did you review -- was there any stage length
12 adjustment deployed in your analysis of the data?

13 A Yeah. So we looked at those categories both on a CASM
14 basis and in some cases on a per block hour basis. The
15 analysis that looked at these categories on a CASM basis we
16 looked at both stage length adjusted and non-stage length
17 adjusted.

18 Q Okay. And why is it appropriate to adjust for stage
19 length?

20 A So airline cost structures combine a number of cost
21 categories that are fixed to the departure and a number of
22 cost categories that vary by the length of flight, and so
23 put differently, the amount of money that you spend on gate
24 agents and airport rent and tugs and commissions doesn't
25 really change for a two-hour flight versus a four-hour

1 flying, particularly with the same aircraft type. So those
2 costs by seat mile go down significantly with longer
3 flights. It's a benefit of scale or run rate as we might
4 say.

5 That said, fuel, a good portion, although not all
6 of aircraft maintenance costs and flight attendant and pilot
7 costs vary by hour, and so the longer you fly an airplane
8 the more fuel you spend.

9 And so an airline that flies aircraft on short
10 stage lengths will tend to have higher CASM than an airline
11 that has similar cost structure but flies its aircraft on
12 longer stage lengths.

13 And so stage length adjustment is an attempt to
14 compare airlines on an apples to apples basis as if they
15 were flying their aircraft on similar mission profiles.

16 Q And when you reviewed the stage length adjusted CASM
17 data for American versus its peers what did you see?

18 A That for virtually all categories Americans costs were
19 either at the top of the industry, meaning the most
20 expensive of industry peers or in the first two.

21 In cases where it was number two with one
22 methodology if you looked at it through another lens it
23 became number one or vice versa, and so in some cases on a
24 CASM basis it might have been number two, but on a block
25 hour basis it was number one, but in all cases in the top

1 two.

2 Q All right. I want to turn, Mr. Dichter, to a few of
3 the strategic initiatives that you reference in your
4 testimony and that have been the subject of considerable
5 testimony this week.

6 First I want to talk to you about the aspect of
7 American's business plan that assumes increased large
8 regional jet operations.

9 A Sure.

10 Q You heard Mr. Vahidi's testimony around that subject
11 yesterday?

12 A I did.

13 Q Did you review American's current utilization of
14 regional jets?

15 A We did.

16 Q And can you briefly describe what you observed?

17 A Yeah. American's use of regional jets is below its
18 peer set on both a relative basis and an absolute basis by a
19 reasonable margin.

20 Q And what assumptions relative to regional jet
21 utilization are embodied in American's business plan?

22 A The assumption is that American grows again somewhat
23 linearly, it's use of large regional jets over the course of
24 the six-year period. The assumptions are that those
25 aircraft are existing models over the course of that period,

1 although several of those models as they arrive in later
2 years would have significant performance upgrades as have
3 been promised by the manufacturers already, and that those
4 aircraft would be flown at cost structures that are
5 consistent with those that are offered by the regional
6 affiliates available in the market today.

7 Q Okay. And I believe you testified earlier that part of
8 your revenue model attempted to input the assumptions of
9 additional regional jet flying over the six-year period?

10 A Sure.

11 Q Okay. Now putting aside any contractual restrictions
12 that may or may not be in play -- I'm not going to ask you
13 about that -- from your experience do you have a view as to
14 from an operational perspective American's -- American can
15 feasibly implement the regional lift that's incorporated in
16 its business plan?

17 A I've seen an analysis that American performed that
18 looked at the number of aircraft needed by the network in
19 each year of the plan, and that a projection of the number
20 of aircraft available in the market -- that's a forecast of
21 course -- available meaning either in the existing fleet and
22 available for contract or production capacity that would be
23 available to buy directly from the manufacturers. Neither
24 of those numbers struck me as alarming in any way, shape, or
25 form, it looked consistent with the kinds of assumptions

1 I've seen elsewhere, although to be clear, we did not
2 analyze it.

3 Q Okay. Did you analyze the benefits that would accrue
4 under American's business plan from increased regional jet
5 utilization?

6 A We did.

7 Q What types of benefits did you identify?

8 A I can describe them qualitatively at first and then if
9 you'd like go into methodology. But --

10 Q I just want to refrain from specific quantitative
11 numbers, that's all.

12 A Sure, I understand.

13 Basically, as I believe has been described by
14 others, including Mr. Vahidi, regional jets allow you to fly
15 either a market at the same level of frequency that you're
16 flying with a larger aircraft at less capacity, and the
17 advantage of that is that if that if you have fewer seats in
18 a market you can be pickier in terms of the passengers that
19 you choose.

20 BY the way, that's an important benefit. If you're flying
21 an MD-80 between Dallas -- or between a given city in the
22 Midwest and Dallas and that's a market where the local
23 passenger flow is reasonably light you still need to fill
24 the airplane, and you often have options to fill the
25 airplane. For instance, at \$79 each way you can pretty much

1 take anyone to Orlando from anywhere, but that results in a
2 very low yield per seat on that segment. If you have fewer
3 seats you obviously need fewer of those low yield
4 passengers. And so that's one benefit.

5 The other benefit is in some cases you could fly
6 the same market with higher frequencies. And so if a market
7 has a total of 100 passengers a day and you're trying to do
8 that with an MD-80 you might be able to get away with one
9 frequency per day, with a 50-seat regional jet that could be
10 three, with a 70-seat regional jet that could be two.

11 The benefit of frequency is twofold. First of all
12 it's one of the most important choice drivers for business
13 travelers. I like to know that if I finish my meeting early
14 I can go to the airport and get on an earlier flight.
15 That's a significant driver of my --

16 Q We're working to that end.

17 A Okay. Second, particularly in the case of markets that
18 have currently only one or two frequencies a day that may
19 result in a significant number of missed connections. And
20 so there might be markets in the hub that you cannot connect
21 to in both directions because of the that.

22 Flights from Latin America to Dallas arrive in the
23 morning, they tend to depart in the evening. And so if you
24 don't have a morning flight out and an evening flight back
25 in you won't be able to make a round-trip connection for

1 Latin America. So it's a very important driver of an
2 airlines revenue plan.

3 Q Okay. Aside from frequency as you know from listening
4 to the testimony here the revenue plan is focused on
5 increasing of the fleet of large regional jets.

6 A That's correct.

7 Q And what's -- I want to make sure we have a definition
8 in mind. I'm speaking of regional jets in excess of 50
9 seats.

10 A Sure.

11 Q Do you have a view as the benefits of expanding the use
12 of regional jets of that dimension?

13 A I do.

14 The first element is cost. In a high fuel price
15 environment -- and when I say high fuel price that's called
16 somewhere in excess of 2 to \$2.50 a gallon, where we've been
17 for quite some time and will likely be for quite some time.
18 The difference in fuel burned per hour between a 50-seat
19 regional jet and a 70-seat regional jet is, you know, in the
20 neighborhood of 10 to 20 percent depending on the market
21 category. On the other hand the 70-seat regional jet has
22 somewhere in the neighborhood of 40 percent more seats. And
23 so the fuel cost per seat in a 70-seat aircraft is
24 significantly lower than it is in a 50-seat aircraft.

25 The fundamental trade off you're looking at when

1 you think about smaller airplanes to larger airplanes is the
2 benefit of lower trip costs, lower cost for the entire
3 flight versus the cost of higher per seat costs, and that's
4 a fairly fine line. In a high fuel price environment 70-
5 seat aircraft have a significant advantage over 50-seat, and
6 90-seat aircraft or 88-seat aircraft an advantage again over
7 a 70-seat.

8 The second is the ergonomics and economics of a
9 50-seat aircraft do not permit, at least not economically
10 and practically, the implementation of a first-class cabin,
11 expanded overhead bins, you know, in-flight Wi-Fi, things
12 like that, which isn't to say that no one has ever done it,
13 but those are benefits that are important to American's
14 customers or an important of insuring that we're creating a
15 seamless offering to our high value customers or to
16 American's high value customers.

17 Q Okay. And lastly with regard to this topic. You heard
18 testimony yesterday about the distinction between flying
19 these large regional jets at the mainline as opposed to
20 regional affiliate.

21 A Sure.

22 Q Do you have -- have you based on your experience as to
23 the economic benefits of flying these large regional jets at
24 one or the other options, mainline versus regional
25 affiliate?

1 A Sure. First of all it should be noted that virtually
2 all airlines fly large regional jets at their affiliates.
3 There is one exception, I believe US Airways flies Embraer
4 190 aircraft at its mainline.

5 There are two primary reasons why the industry has
6 evolved that way. One is obviously cost, and the biggest
7 cost category there is of course labor cost. And by the
8 way, when I say labor cost I don't just mean wage, I also
9 mean benefits, packages, pension costs, productivity. And
10 when I say labor I don't just mean pilots, I also mean
11 flight attendants, maintenance workers, aircraft cleaners,
12 airport staff, dispatchers, et cetera, and so there are a
13 number of groups.

14 Just to give you a sense of how sensitive that
15 issue is, and I'm going use round numbers and from publicly
16 available data so there's nothing confidential here, but
17 American Airlines narrow body cockpit costs per hour, so for
18 an MD-80 class aircraft would be in the neighborhood of \$700
19 a hour; that's everything. That's all of the cost of the
20 pilot force divided by all of the hours. There are 140
21 seats on that aircraft, that's \$4 per seat per hour. A 70-
22 seat aircraft flown by a regional affiliate would have
23 cockpit costs in the range of 250 to \$280 per block hour.
24 That's also \$4 per seat.

25 While I'm confident that if a regional aircraft

1 were to be flown by a mainline it wouldn't be at \$700 an
2 hour, it would be less than that. There's a big gap between
3 700 and 250, and to give you a sense of the sensitivity
4 here, obvious math, every \$70 of additional cockpit costs
5 per block hour is \$1 per seat.

6 The typical revenue per seat per hour in a
7 regional jet would be in the range of \$75 an hour, plus or
8 minus depending on the mission profile.

9 In a great year an airline would earn a five
10 percent profit margin, that's after everything. That's
11 \$3.75 per seat in profit.

12 And so \$1 per seat in pilot costs is more than a
13 quarter of your best case profit margin on that aircraft,
14 and that's just pilots.

15 In addition there are other cost categories that
16 are impacted by operating these aircraft at affiliates. The
17 work rules and scheduling flexibility associated with
18 affiliate labor contracts allow you to use aircraft more
19 productively.

20 I believe Mr. Vahidi was asked whether aircraft
21 ownership costs would change if these aircraft were operated
22 at affiliates. He described some possible lease structures,
23 I think that's correct.

24 In addition the scheduling flexibility you have
25 under typical affiliate work rules can allow you to operate

1 the aircraft more per day. Not in all cases, but certainly
2 in some. More hours per day means less aircraft costs per
3 hour. There's also a revenue benefit there of course.

4 And then last on the cost side, some of the
5 affiliates that have had lengthy histories operating these
6 kinds of aircraft have developed both significant scale and
7 significant expertise in maintaining these aircraft. That
8 has allowed them to customize maintenance programs, extent
9 the interval between which parts are removed from the
10 aircraft, in some cases actually even create alternative
11 suppliers that only they can use that provide additional
12 leverage with the aircraft manufacturers. And those are
13 actions consistent with the things that American would have
14 done on its MD-80 fleet over the years as one of the world's
15 largest operators of MD-80's.

16 Those are things that take a long time to develop.
17 And I'm not saying that American couldn't develop those
18 capabilities, but it would take time. The regional
19 affiliates, particularly the larger ones have them
20 immediately.

21 The second benefit is flexibility.

22 Q So we're moving beyond costs now --

23 A Yeah.

24 Q -- and non-cost benefits.

25 A Sure. The big benefit here, the plan contemplates not

1 just that these aircraft would be flown by an affiliate, it
2 contemplates that these aircraft would be flown by multiple
3 affiliates. That's consistent with industry practices where
4 a number of aircraft would be divided up across a number of
5 suppliers.

6 This both gives you access to the infrastructure
7 of all of those suppliers, so multiple maintenance bases for
8 instance, but it also gives you a significant risk
9 mitigation benefit.

10 If there are labor difficulties at one supplier
11 for instance you can move capacity to another. If you quite
12 frankly just need fewer aircraft, depending on the ownership
13 structure of those aircraft, you've got some ability to
14 reject contracts and reduce the size of the fleet in a
15 shorter period of time than would typically be possible if
16 you operated those aircraft at mainline.

17 Q Okay. And are you familiar with how the other large
18 network carriers deploy their regional jets in terms of
19 whether it's at their mainline or regional affiliate?

20 A I am.

21 Q And can you quickly and briefly describe how they do
22 so, their use of affiliates, and where -- how American
23 compares?

24 A Yeah. Delta, United, US Airways all use multiple
25 affiliate providers to provide their regional lift. In the

1 case of US Airways they do operate E-190, Embraer 190, it a
2 roughly 90-seat aircraft at the mainline.

3 Q And how does American's utilization of affiliates
4 compare to those that you just described?

5 A Again, both fuel regional jets overall and of course
6 dramatically fewer affiliates with the vast majority, if not
7 all of that, capacity being flown by Eagle -- American
8 Eagle.

9 Q I want to turn lastly now to domestic code sharing, a
10 topic that has received much attention here this week.

11 Did you examine American's existing domestic code
12 share relationships?

13 A We did.

14 Q How has domestic code sharing been utilized by the
15 large domestic carriers over the course of the past decade?

16 A It's a good question.

17 Q Thank you.

18 A Prior to the merger of Delta Northwest and United and
19 Continental, the mergers of domestic code sharing was a
20 frequent tool to expand network breadth and improve customer
21 offering in the industry. United and Delta had an extensive
22 code sharing relationship, subsequently Continental and
23 Northwest, and then for a time Continental, Delta, and
24 Northwest, in addition to many others.

25 The mergers of Delta and Northwest and United and

1 Continental have rendered domestic code shares somewhat less
2 necessary for them than for others, although they still do
3 it.

4 But case in point, US Airways, which is a smaller
5 carrier across the big four, makes extensive use of domestic
6 code shares through its star lines relationship with United.

7 Q And how does American's current utilization of domestic
8 code sharing compare to the others you referenced?

9 A It is below all of those.

10 Q What assumptions does American make in its business
11 plan relative to its future use of domestic code sharing?

12 A There's an assumption that existing code share
13 relationships continue to grow in line with the overall
14 industry growth rate. There's also contemplation of
15 expanded code share relationships in the New York area.

16 Q Okay. And I don't want to get into any confidential
17 information around that relationship.

18 Do you have a view as to the viability of
19 American's ability to enter into a domestic code sharing
20 relationship in the New York area?

21 A Well, I guess you could answer that on two dimensions.

22 One would be the likelihood that a partner would
23 want to engage in such code sharing relationships, and I
24 guess two would be the operational viability of those
25 agreements.

1 On the first point our general experience has been
2 that non-overlapping code share agreements, which is what is
3 contemplated in this plan, so in other words you would not
4 code share with a counter-party on a route that you both
5 serve. Non-overlapping code share agreements tend to be
6 accretive to both parties. Meaning they're really only
7 pluses, relatively few, in any, minuses.

8 Q And in that connection have you reviewed historical
9 examples?

10 A Yes, we have.

11 Q And did you find those to be accretive?

12 A Yes, we have.

13 Q I'm sorry.

14 A Emphasis on non-overlapping code share agreements.

15 And so in the context of an agreement that's
16 accretive to both sides and the incentives are there for
17 both sides to engage in that agreement, over time a large
18 portion of those attempts across the industry have been
19 successful while we absolutely could not guarantee that.

20 If I were advising JetBlue I would certainly
21 advise them to consider such a proposal seriously. Sorry
22 about that.

23 Q We'll take that.

24 A Yeah, it's been done before.

25 On the point of operational viability just say the

1 challenges associate on the operations front whether it be
2 different airplane terminals, different IT systems, our
3 experience has been that airlines work these issues out over
4 time.

5 Q You heard Mr. Vahidi's testimony yesterday that as part
6 of the relief requested in this court American is seeking
7 additional flexibility to enter into future domestic code
8 sharing arrangements.

9 Why do you regard additional flexibility as
10 particularly important with respect to this topic?

11 A Sure. While I don't have a point of view on the
12 specific contract language that would be required, my
13 experience has been that these kinds of negotiations are
14 fast paced and real-time, particularly by the way if there
15 were a third party involved, and you need the ability to
16 commit at the negotiating table.

17 I was in the last two years involved in a code
18 share negotiation where literally you had airlines locked in
19 two conference rooms, you know, in the same hotel going
20 backward and forward on proposals.

21 While I understand and I don't understand the full
22 details, I understand the current contract language involves
23 a 30-day discussion period of some kind with the APA.
24 Having to leave the negotiation table each time and say I'm
25 going need to get back to you in 30 days to confirm whether

1 or not we can do this can be a significant barrier to
2 closing a deal in any business context.

3 Q I want to show you what was introduced yesterday as
4 APFA Exhibit 8. Do you have a copy?

5 A Yes, I do.

6 MR. POLLACK: Your Honor, may I approach?

7 THE COURT: Yes.

8 BY MR. POLLACK:

9 Q This is the news article that Mr. Vahidi was asked
10 about. And you see the first line about current plans?

11 A I do.

12 Q Okay. Are you familiar with verbiage to that effect?

13 A Yeah, I believe what Mr. Barger (ph), while not
14 directly quoted as saying, but what the article says is that
15 there were no plans to refocus its marketing pact with
16 American Airlines. I don't know Mr. Barger well --

17 Q And I'm not going to ask you to interpret --

18 A Yeah.

19 Q -- his --

20 A So I don't -- I can't interpret his meaning.

21 What I can say is that the term "we have no plans
22 to," is used frequently in multiple industries to say we
23 have no further comment.

24 Case in point, the CEO of Delta Airlines was
25 quoted in April or so of I believe 2007 of saying, we have

1 no plans to merge with Northwest Airlines, they merged with
2 Northwest Airlines about 11 months later.

3 MR. POLLACK: Nothing further, Judge.

4 THE COURT: All right. Cross-examination?

5 MS. PARCELLI: May we have a five-minute break?

6 THE COURT: Sure.

7 MS. PARCELLI: Thank you.

8 THE CLERK: All rise.

9 (Recess at 11:07 a.m.)

10 THE COURT: Please be seated.

11 All right, before we proceed with cross I did have
12 a question for this witness about something that keeps
13 coming up that I may have missed a more fulsome explanation.

14 But could you explain to me when you're talking
15 about use of regional jets what it -- how that arrangement
16 works, vis-à-vis, affiliates?

17 Because I think what I've -- what I've heard is
18 that American has some use of regional jets with American
19 Eagle, but I'm not quite sure what the term affiliate
20 encompasses in this context, and also what the business
21 arrangement is if American is buying the aircraft.

22 THE WITNESS: Sure. I think we've probably used
23 the term "affiliate" somewhat loosely, but what we intended
24 was a broad description of the other companies to which
25 American would contract regional jet flying, which would

1 include by the way American Eagle, and why that's part of
2 the AMR group it's an entity in its own right.

3 And so just to give you specific examples of other
4 providers in the market those would include Mesa, Republic
5 Airways, Sky West, you know, for example.

6 The relationships vary considerably. First off
7 there a cases where the mainline carrier buys the aircraft,
8 keeps the aircraft on its books and subcontracts those
9 aircraft to the affiliate. In that case obviously if the
10 relationship were terminated the mainline airline is stuck
11 with the airplanes.

12 There are cases where the mainline airline buys
13 the aircraft and then effectively sells them or transfers
14 them to the affiliate and they're on the affiliate's books,
15 and in those cases there is more contractual freedom to
16 separate.

17 BY the way, there's litigation in the market today on
18 exactly that subject, and so, you know, it's not completely
19 black and white.

20 And then there are cases where the regional buys
21 aircraft speculatively and looks for airlines to place those
22 aircraft with.

23 In cases where, as the result of the second
24 category, in other words it had airplanes, it lost a
25 contract, you know, it now has excess airplanes, it's

1 looking for additional contracts to fill.

2 THE COURT: All right, thank you.

3 THE WITNESS: You're welcome.

4 THE COURT: Proceed.

5 MS. PARCELLI: Good morning, Your Honor.

6 THE COURT: Good morning.

7 MS. PARCELLI: Carmen Parcelli for the APFA.

8 CROSS-EXAMINATION

9 BY MS. PARCELLI:

10 Q Good morning, Mr. Dichter.

11 A Good morning. Good to see you again.

12 Q Nice to see you.

13 Mr. Dichter, I believe you testified on direct
14 that McKinsey was retained in this case on December the 11th
15 of 2012. Could it be the December 12th of --

16 A It's whatever I said in my --

17 Q -- or 2011?

18 A -- whatever I said in my written declaration and was in
19 the engagement letter.

20 Q Fair enough.

21 A My calendar is a complicated thing.

22 Q Okay. I think your declaration reflects the 12th.

23 A Okay. Good enough.

24 Q Now when did your work on the business plan begin?

25 A As I said earlier on direct, literally within hours.

1 Q Okay. And then the business plan though was first
2 presented to the various stakeholders in the bankruptcy on
3 February the 1st; is that correct?

4 A That's correct.

5 Q Okay. And when did you begin -- or McKinsey begin its
6 work on the revenue model?

7 A Within hours after we started.

8 Q Okay.

9 A Yeah.

10 Q And I believe you testified on direct that American did
11 have an existing revenue model, correct?

12 A Correct.

13 Q And did you spend time reviewing that model?

14 A We really didn't. We were really focused on creating a
15 business plan looking forward. We're under a tight timeline
16 and so weren't all that intellectually interested quite
17 frankly in reverse engineering history.

18 And as I said before, you know, an important
19 principal of our engagement was to maintain a degree of
20 independence on the methodology used in that forecast.

21 And so I had a brief description of that model
22 given to me by a few people, but beyond that I didn't get
23 into the mechanics of it, and I've actually never laid eyes
24 on the screen or any of the code in it.

25 Q All right. And when did you complete work then on the

1 revenue model?

2 A As I believe I said in our -- in my deposition,
3 somewhere in the last couple of weeks of January.

4 The architecture of the model was complete
5 relatively quickly, there's then a process of calibrating it
6 and making sure that all the links are functioning properly,
7 that the code is as you expect, and this of course is a
8 normal process in writing, you know, any piece of software
9 or any model.

10 The model was stabilized, I think I used that word
11 in deposition, within the last two weeks of January.

12 Q And did you ever compare the output of your new revenue
13 model to the output of American's existing revenue model?

14 A We did.

15 Q Okay. And what did that comparison show?

16 A Yeah, it showed a gap of -- I'm going to get -- can I
17 talk about numbers? Yeah.

18 Well, let's say in the few hundreds of millions of
19 dollars, and just to be specific American's revenue model
20 projected a revenue outcome that was a few hundreds of
21 millions of dollars higher in 2017 than our model did.

22 Q Okay. Can I just get a clarification?

23 A Yeah.

24 Q Are you saying few hundreds of millions of dollars in
25 order not to give a specific --

1 A Yes.

2 Q -- amount? Is that --

3 MS. PARCELLI: How do you feel about that,
4 counsel?

5 MR. POLLACK: Well --

6 MS. PARCELLI: Let me ask.

7 MR. POLLACK: -- the overall revenue number I
8 think is confidential and is protected.

9 MS. PARCELLI: Yeah. But we're talking about
10 the --

11 THE COURT: I think he was trying to give you a --

12 MS. PARCELLI: -- spread.

13 THE COURT: -- degree of magnitude.

14 MS. PARCELLI: I know. I'd like to get a more
15 precise number in the record if we're permitted.

16 THE COURT: Well, that -- that's subject to the
17 confidentiality issues.

18 MS. PARCELLI: So we're talking about --

19 THE COURT: I mean, I think it's in the record per
20 se, but I don't know -- I don't think it's in the public
21 record.

22 MS. PARCELLI: I don't think it's in any of the
23 materials that were submitted.

24 MR. POLLACK: Yeah. I think we're comfortable,
25 Judge, with -- let me just confer with the client.

1 MS. PARCELLI: Sorry.

2 THE COURT: Well, the other thing we can do is --
3 is maybe something that you agree upon. In other words, you
4 don't necessarily need this witness unless you have a series
5 of questions you want to ask about that number.

6 MS. PARCELLI: No, it just -- it came out in
7 deposition and I'd like to get it in the record if we can.

8 THE COURT: Well, the reason why I say that is
9 what I'd like to do is, do what we can do with this witness
10 and then I think you can chat about it and we can figure it
11 out, but -- unless you have a series of questions that you
12 need that number for let's just move along with the witness
13 because I know there's some time pressure.

14 MS. PARCELLI: Thank you, Judge.

15 MS. PARCELLI: Okay.

16 THE WITNESS: Thank you.

17 MS. PARCELLI: That's fine.

18 THE COURT: But let's not forget to deal with that
19 over lunch and chat and let me know how you want to work it
20 out.

21 MS. PARCELLI: No, that'll work fine. Thank you.

22 BY MS. PARCELLI:

23 Q Now I believe you also testified on direct that part of
24 your assignment was to look at alternative business
25 strategies. Now how long did that process take you?

1 A You know, it was kind of happening in parallel. You
2 know, we had a real number of people working on the team,
3 but I would say there was three weeks out of the six or so
4 that elapsed between middle of December and end of January
5 that were focused on those alternatives.

6 Q Okay.

7 A A lot of that in discussion as opposed to, you know,
8 specific analysis.

9 Q And you already provided testimony as to what those
10 alternatives were?

11 A Yes, I did.

12 Q Okay. Now did you consider merger or consolidation
13 among those alternatives?

14 A No, we really didn't.

15 Q Okay. And is it correct to say that you did not
16 consider merger or consolidation because it was not part of
17 your mandate from American Airlines to look at that?

18 A Yes, partly. As I believe I've said also in
19 deposition, certainly we have a professional obligation to
20 raise anything to our clients that we believe that they
21 ought to be looking at that they're not, and we typically do
22 even if we're not asked to.

23 So yes, it was not part of our scope, but in
24 addition we believe strongly as has been testified by others
25 that it's very important to have a viable stand-alone plan

1 before you consider such alternatives, and not just on paper
2 but actually in actuality.

3 Q When you say in actuality you mean implemented?

4 A Well, at least locked in through -- through a contract.

5 I guess the point I'm trying to make is two
6 things. One the -- a huge amount of the value in any merger
7 to stakeholders comes from the outcome of negotiations with
8 the counterparty, not just the total synergies that are
9 created. So it's not always the case that two parties get
10 together and say we'll split them down the middle, there's
11 usually a significant back and forth on equity stakes and
12 number of board seats and things like that, and your power
13 in the negotiating table in any M&A deal is very much linked
14 to what you're bringing to the table in terms of ongoing
15 business results.

16 And so your ability to walk into those
17 negotiations saying we have a business plan that we can
18 count on, meaning we have the contracts in place, we know
19 that these will be our costs, we have a reasonable revenue
20 model, is directly linked to your power in those
21 negotiations.

22 Second, while there are significant synergies in
23 airline mergers one of the most common dissynergies is the
24 upward migration of labor costs. Meaning when you merge two
25 airlines together all other things being equal you tend to

1 end up at a labor cost level and working condition level
2 equal to the higher of the two.

3 And so any airline with higher labor costs talking
4 to an airline with lower labor costs that's going to reduce
5 the total number of synergies, and in some cases may limit
6 the number of counterparties that you can reasonably talk
7 to.

8 And our view is that if you're going to engage in
9 M&A you want to be able to look at all possible options and
10 you want to be able to do that from both the strongest
11 negotiating position and with the maximum possible pool of
12 synergies.

13 Q Okay. Mr. Dichter, do you have any past experience in
14 Section 1113 bankruptcy matters?

15 A No, I don't.

16 Q Okay. So the experience that you're drawing from then
17 to give your answer and explanation doesn't have anything to
18 do with the Section 1113 bankruptcy context; is that fair?

19 A No, it has to do with many M&A negotiation support
20 engagements.

21 Q Okay. Now was it also your understanding that American
22 was not looking at merger scenarios because its CEO, Tom
23 Horton, believed that that should only be considered after
24 emerging from bankruptcy?

25 A I have heard him say that in the press, yes.

1 Q Okay. So that was your understanding?

2 A Yes, it is.

3 Q Okay. Now, Mr. Dichter, let's see if I can set the
4 stage for this.

5 Would you agree that there are four primary
6 elements in the business plan? And let me list them.

7 One is the revenue model, so revenue forecast,
8 okay?

9 Second would be the EBITDAR target, okay?

10 Third, non-labor cost target.

11 And fourth labor cost target.

12 Are there any other sort of key components that I
13 haven't hit on?

14 A I think that's basically right. I may rephrase it
15 slightly for the record if that's okay.

16 Q Sure.

17 A And that's I would think of the revenue forecast as an
18 outcome. If I think about the elements of a strategic plan
19 it comprises of a number of business choices that you make
20 first and foremost, and so where do you deploy your assets,
21 how many assets do you deploy, of what nature, what
22 investments do you make in technology and product, et
23 cetera, the nature of the network, and those of course drive
24 a significant portion of the revenue plan, but they also
25 have implications on costs as well.

1 Second would be a cost structure, right, and so
2 that's the nature of your labor contracts, the agreements
3 you have with suppliers, et cetera.

4 Third is obviously a balance sheet, and so --
5 again, we didn't spend any time on that, Rothschild did.

6 Q Uh-huh.

7 A So the level of debt to equity that you have overall
8 that sort of speaks to the flexibility that you have in the
9 plan.

10 And then several of the other dimensions that you
11 talked to are kind of outputs, right, so --

12 Q Uh-huh.

13 A -- and/or targets.

14 So in the case of EBITDAR yes, you will often
15 begin with a specific EBITDAR target and then iterate across
16 those others to figure out what combination of business
17 choices, cost structure, and balance sheet configuration
18 will yield the results that you're looking for.

19 Q Okay. But these are important features of the business
20 plan, right?

21 A Yes, these are business features of the plan and those
22 are all, you know, key ingredients to getting at that
23 outcome, you're right.

24 Q Okay. So in terms of the process of creating the
25 business plan as it went out to stakeholders, February 1st,

1 is it fair to say that you and your work, you began with the
2 revenue forecast?

3 A That's correct.

4 Q Okay. And then is it also correct that American worked
5 with Rothschild to develop the EBITDAR target, right?

6 A That is correct.

7 Q Okay. So that happened then next, right?

8 A Yeah, and I'm not entirely clear on the sequence.

9 Q Okay.

10 A Rothschild was engaged before we were so they may have
11 been working on that for some time.

12 Q And then the in-house team at American that you were
13 working with, they came up with the non-labor cost target;
14 is that correct?

15 A Yes, as a starting point, and so they had both a
16 historical set of actions, a current starting point, as well
17 as additional initiatives in place that yielded a non-labor
18 cost target.

19 And just to clarify too because I think the words
20 have been used somewhat interchangeably, there's a bucket in
21 the plan that is referred to as restructuring savings --

22 Q Uh-huh.

23 A -- and these are in point of fact non-labor costs
24 because they are costs that don't affect labor, but they're
25 specific to renegotiations with suppliers and debt holders

1 and things like that, and we did not look at that category,
2 that was I believe a Rothschild responsibility.

3 Q Okay. And so the in-house team then, they were
4 involved both in forecasting the future growth that the
5 airline was projected to experience in costs, right?

6 A Yes, that's correct.

7 Q And then offsetting that with any of American's
8 initiatives to cut its non-labor costs; is that fair to say?

9 A Yes. So they had a forecast for natural progression of
10 labor costs, non-labor costs, all cost categories absent any
11 action, if you will, and then layered actions on top of
12 those to --

13 Q Okay.

14 A -- get at an overall cost forecast.

15 Q So -- so once you had values for those three items, the
16 revenue, the EBITDAR, and the non-labor cost target, was
17 then a final labor cost target set?

18 A Yeah. I mean the labor cost target was first of all
19 multiple parties working on that and so we had some
20 responsibility and American had some responsibility and
21 there may have been others. There are really three
22 dimensions to that.

23 So one dimension has been unflatteringly referred
24 to in these proceedings as a "plug," right, meaning, you
25 know, if you're only going to achieve revenue of X level and

1 you need an EBITDAR target -- sorry, I'm using my hand
2 again, I know you can't do that --

3 Q Yeah.

4 A -- but if you're going to -- if you have a certain
5 EBITDAR target and you know that your revenue forecast is
6 going to be X and your non-labor cost target is going to be
7 Y then obviously the remaining element in that math is your
8 labor costs. And so there is a -- sort of a fall out effect
9 of that process.

10 Q And that's just mathematics?

11 A That is just mathematics.

12 Now that said there are two other inputs to that.

13 One input is, is that result commensurate with
14 your peers? And that's important for two reasons.

15 One reason is even if that labor target -- and
16 this is not the case here -- but even if that labor cost
17 target got you to your EBITDAR level, our view is that if
18 your labor costs were still significantly higher than your
19 peers you have a long-term problem, and you have a long-term
20 problem because this is a competitive industry where revenue
21 production in a similar network footprint tends to be
22 relatively even across peers. When you go on Expedia you
23 don't tend to see Delta charging a higher price in the same
24 market than American or than United. And if you have labor
25 costs higher than your peers for a long period of time your

1 peers will have higher margins, and if they have higher
2 margins they'll have more money to spend on new equipment,
3 more money to invest in new products, they'll have more
4 money to weather industry shocks, and that's competitively
5 dangerous over the long term.

6 So -- and then second if you looked at that labor
7 cost target and it said it was significantly below your
8 peers, you know, you'd have another problem, which is you'd
9 have difficulty recruiting, you know, people in the labor
10 force.

11 The third component, which we had no involvement
12 in but American worked on, was the question of as you think
13 about how you get to that labor cost target do you see a set
14 of actions which appear feasible, loosely described?
15 Meaning can you see changes in work rule and benefit
16 constructs that get you to that number without -- you know,
17 I'm using an extreme example -- you know, paying pilots \$5
18 an hour? Which I think everybody would say is, you know,
19 not feasible on multiple dimensions.

20 Q Okay. That was a lot there.

21 A Sorry.

22 Q Let's go back and --

23 A Yeah.

24 Q -- unpack a few things here.

25 So all right, the -- so we talked about the

1 plug --

2 A Yeah.

3 Q -- where it's just mathematics, right?

4 Now then you talked about you would look and
5 compare it to peers. And you said if American was higher
6 than its peers then in your view that might call for an
7 adjustment; is that correct? So even if at that higher
8 level of employee costs American was still hitting the
9 desired EBITDAR target you're saying still there would be an
10 adjustment down in your view?

11 A Well, look that's up for the -- that would be up for
12 the courts to decide from a pure business planning
13 standpoint.

14 Q No, I'm asking what --

15 A Yeah, from a strategic --

16 Q -- in developing the model you were doing.

17 A From a strategic standpoint -- there's a modeling
18 effort here, but there's also strategic advice.

19 As a business planning professional I believe it
20 is imprudent to embark on a five-year plan with any major
21 cost category significantly higher than your peers. It just
22 opens up the opportunity for your peers to have higher
23 margins than you do, and as I said, invest in places that
24 could be dangerous to your business if you didn't counter
25 those investments, and of course with a lower margin you

1 might not be able to.

2 Q So was the overall labor cost target number adjusted
3 downward even below what it needed to be to hit the EBITDAR
4 target?

5 A I actually don't know where it was before, what I do
6 know is that the target that came out of our joint exercise
7 with American put American's costs in line with peers, point
8 one.

9 And then point two, it's our understanding that
10 American believed it had a set of actions to reach that
11 number, which you know, it believed were -- again, loosely
12 described -- feasible.

13 Q Now when you talked about the -- sort of the third --

14 A Yeah.

15 Q -- element or input I think you used the word, that was
16 -- I'm just trying to make sure I understand it correctly
17 what you were conveying -- that was American's in-house
18 personnel figuring out what contract changes would be
19 necessary to make to equal the value that had been set for
20 the labor reduction target; am I correct?

21 A That's correct.

22 Q Okay. Now when did you first see any labor target
23 number for American?

24 A I guess personally somewhere in the middle of January
25 as we went through this iterative process. I --

1 Q Not right at the beginning of your engagement?

2 A I saw previous documents that led up to the final
3 versions that are referenced in Exhibit B of my declaration.
4 I cannot honestly remember whether or not there was a labor
5 cost target in there. I certainly would imagine that if
6 there was and it was materially different from the one that
7 we ended up with I would remember it, but --

8 Q Okay. And that -- but what you did see was a number
9 that came from American at that point in time; is that
10 correct?

11 A Again, I can't remember whether or not there was a
12 labor cost target in the earlier versions of that document.
13 There certainly were in the final versions.

14 Again, our task wasn't to compare the labor cost
15 target to American's, our task was to compare the revenue
16 target to American's and develop a joint point of view on
17 the revenue production coming from the plan and focus mostly
18 on the non-labor cost pieces of the plan.

19 Q But you don't recall as you sit here today a draft
20 labor number at the beginning of the process based on
21 American's own projections for revenue?

22 A No, I do not.

23 (Pause)

24 Q So I'm sorry, again, when do you think now that you
25 first saw a labor target number?

1 A I think it would have been in the last two weeks of
2 January when again the model started to stabilize and we
3 started providing both input and back and forth discussions
4 with American executives for the final numbers that led up
5 to the February 1 and subsequent presentations that you saw.

6 Q Okay.

7 THE COURT: Could I just clarify? I think your
8 witness made a reference to prior version of an exhibit.

9 THE WITNESS: Yeah.

10 THE COURT: Did he say Exhibit B?

11 THE WITNESS: Yeah.

12 THE COURT: Of which document? I just want to
13 make sure I'm looking at the right thing in the folder.

14 BY MS. PARCELLI:

15 Q Are you talking about your report?

16 A Sorry. Yes, I'm talking about -- if you look at my
17 declaration, I believe it's called Exhibit B. Yeah, it's --
18 it is -- it's right -- Appendix B. Sorry.

19 THE COURT: I just want to make sure --

20 THE WITNESS: Yes. In Appendix B there are a
21 number of documents that I relied on in the preparation of
22 the declaration.

23 As is often the case documents have an
24 evolutionary life and so, you know, the first version of a
25 document will often have nothing more than chapter headings

1 in it, for instance, and you start to built in frameworks
2 for the way you want to present information and the types of
3 topics that you want to look at, and those documents get
4 populated with numbers over time.

5 THE COURT: Thank you.

6 BY MS. PARCELLI:

7 Q And do you recall the labor number that you first saw?

8 A I do not.

9 Q Okay.

10 A No.

11 Q And the final labor number as of February one was
12 1.5 billion. That's not --

13 A Yeah, there's a couple ways to look at that number, but
14 -- but yes.

15 Q Okay.

16 A That is one way to look at that number.

17 Q Okay. So I know you said you can't recall --

18 A Yeah.

19 Q -- the specific number, but was it different from the
20 1.25 billion?

21 A Well, again, anything that I might have seen at the
22 beginning of the process I --

23 Q Yeah.

24 A -- I honestly do not --

25 Q Mr. Dichter --

1 A Yeah.

2 Q -- the question was a lot more straightforward --

3 A Yeah.

4 Q -- than that. Was it a different number than the one
5 you first saw, the 1. --

6 A I'm saying I can't even --

7 Q -- is 1.25 different --

8 A -- remember whether I saw a number, and --

9 Q Okay.

10 A -- and I have a reasonable view on my memory works, and
11 if I see something unusual I typically remember it, and
12 so --

13 Q Okay.

14 A Yeah.

15 Q But -- I mean, Mr. Dichter, you were deposed in this
16 case on Friday, April 20th of 2012, correct?

17 A That's correct.

18 Q And I'm looking now at page -- where am I looking --
19 the very bottom of page 156.

20 MR. POLLACK: Excuse me, I don't know if the
21 witness has access to this transcript.

22 THE COURT: Yeah.

23 MS. PARCELLI: Yeah, I can get him a copy.

24 MR. POLLACK: Thank you.

25 THE COURT: Yeah. Whenever we're going to ask a

1 witness about his deposition testimony we need to start
2 handing those things out.

3 THE WITNESS: Yeah.

4 MS. PARCELLI: Okay.

5 THE COURT: Thank you.

6 MS. PARCELLI: Sorry about that.

7 THE COURT: That's all right. It just speeds
8 things along.

9 MS. PARCELLI: Yeah.

10 THE WITNESS: 156 you said?

11 BY MS. PARCELLI:

12 Q Yeah.

13 A Sorry. Or 56?

14 Q And you have to -- there's four pages reproduced on
15 each page, so you have to --

16 A Ah, yes, I understand.

17 Q -- look at the little number inside -- yeah.

18 A Is this an environmentally correct deposition?

19 Q No, when you have to carry a lot of stuff --

20 A Yeah.

21 Q -- from Washington, D.C., it's also got other uses.

22 A Okay.

23 Q So page 156.

24 A Yeah.

25 Q And if I could direct your attention --

1 A Yeah.

2 Q -- let's see here, line 21.

3 A Yeah.

4 Q Question, "Okay. So at what point in time in between
5 December 12 -- so at what point in time in between
6 December 12 and February 1" --

7 A Yeah.

8 Q -- "was there this labor number" --

9 A Yeah.

10 Q -- was it arrived at?"

11 Answer, "There was a draft number at the beginning
12 of that process based on American's own projections for
13 revenue."

14 A Yes.

15 Q Question, "When you first came on board?"

16 Answer, "When we first came on board."

17 A Yes.

18 Q "That" -- continued answer -- "That number evolved over
19 the course of that period of time as the revenue forecast
20 became more robust and refined."

21 A Yes.

22 Q Okay. Does that --

23 MR. POLLACK: Excuse me, I would ask that the
24 witness --

25 THE WITNESS: No --

1 THE COURT: You got to read the rest of it because
2 there's relevant testimony.

3 MS. PARCELLI: Okay.

4 THE COURT: So I don't want to have to go back
5 through this again.

6 MS. PARCELLI: Okay. I'm sorry. I'm happy to
7 read more.

8 THE COURT: Just -- just the next question and
9 answer.

10 MS. PARCELLI: Sure.

11 THE WITNESS: Sure.

12 MS. PARCELLI: Sure.

13 MS. PARCELLI: Okay.

14 THE COURT: It's the next two actually.

15 BY MS. PARCELLI:

16 Q Okay. Next question.

17 "Okay. How did the number evolve? Do you
18 remember what the number was when you first saw it?"

19 Answer, "I do not. As I testified earlier, the
20 revenue number came down slightly and there were some
21 offsets by increases in non-labor costs. I can't remember
22 exactly whether the number grew or shrunk."

23 Question, "Oh, you don't remember whether the
24 labor number grew or shrunk in this time period we've been
25 discussing?"

1 Answer, "No, I do not, and largely because there's
2 a third bucket that we weren't involved" -- I believe that
3 should be in -- "which are the restructuring costs, and I
4 don't know whether there were changes in that bucket over
5 the course of that period either."

6 I think that's it is relevant portion.

7 THE COURT: I think there's one more.

8 MS. PARCELLI: Okay.

9 BY MS. PARCELLI:

10 Q Question, "Do you remember what the number was when you
11 initially saw it?"

12 Answer, "I do not."

13 Okay? But my point here was to the testimony that
14 speaks to seeing a draft labor number at the beginning of
15 that process based on American's own projection's
16 (indiscernible - 11:35:21).

17 A So I honestly don't mean to be pedantic here, but you
18 asked me earlier whether I'd seen it, and I haven't, or at
19 least I do not remember if I did. I am 100 percent
20 confident that there was a number, and --

21 Q Okay.

22 A -- that's how I understood the question in my
23 deposition.

24 Q Okay.

25 A So the question was asked --

1 Q Well then --

2 A -- was there a number and I said, yes, there was a
3 draft number.

4 Q Okay. So you knew there was a draft number?

5 A Oh, absolutely.

6 Q You just hadn't seen the actual number?

7 A That's correct.

8 Q Okay. And even not having -- even just being aware of
9 the draft number as you testified in your deposition you
10 weren't aware of what the number actually was?

11 A No, I was not.

12 Q But you just knew that that number existed?

13 A I knew that there was a number.

14 Q Okay.

15 (Pause)

16 THE COURT: And just -- counsel, for future
17 reference, whether it's the debtor's or the union's, if
18 there's deposition for impeachment purposes and there's
19 testimony that's arguably relevant, I know I went back and
20 forth on how I was going to do this, but my view is we'll
21 read everything that's relevant and it'll probably shorten
22 any redirects or recrosses just so we can get it all out at
23 one point.

24 So that's any purpose in doing that, not to
25 interrupt your questioning.

1 MS. PARCELLI: Oh.

2 BY MS. PARCELLI:

3 Q Mr. Dichter, you testified on direct that McKinsey had
4 done some labor benchmarking analysis; you recall that?

5 A I do.

6 Q Okay. When in the time period that we've been
7 discussing --

8 A Yeah.

9 Q -- was that analysis done?

10 A I honestly don't know exactly. As I said earlier, this
11 was not part of our original scope. My team was asked at
12 some point during the process to do this, I assume by some
13 combination of Bev Goulet and Candice Irvin, but I don't
14 exactly know, but it would have been, you know, somewhere in
15 the latter half of December or the early part of January I
16 would guess.

17 Q Okay. And do you know why it wasn't in your original
18 retention and then was later added by American?

19 A I don't know why it wasn't in the original engagement
20 letter. I would presume that it's because American felt it
21 had a reasonably clear point of view on where its labor
22 costs were, vis-à-vis, competitors, but at some point in the
23 process we were asked to confirm or test American's views if
24 we had a different view.

25 Q Okay. Did you have any understanding of why you were

1 being asked to do that?

2 A Beyond that -- beyond the general helpfulness of
3 helping clients get, you know, even clearer on views that
4 they have or test those views with alternate views, no.

5 Q Okay.

6 A Yeah.

7 Q And when you say test --

8 A Yeah.

9 Q -- so were you taking something that had already been
10 done by American and --

11 A No, we did our own benchmarking through methodology
12 that we would normally use to do this and came up with
13 results that were at least to my understanding consistent
14 with American's views.

15 Q Okay. And I'm sorry if you said this, who was it? Do
16 you know who was it that decided that you --

17 A I actually do not know --

18 Q -- should do the analysis?

19 A -- precisely.

20 Q Okay.

21 A Given the daily interactions I would assume that it was
22 Candice Irvin or Bev Goulet.

23 Q Okay. And is this type of analysis something that
24 McKinley (sic) commonly -- McKinsey -- I said that at his
25 deposition -- McKinsey commonly --

1 A We've been called worse things.

2 Q I don't know what it is in my brain about your name.
3 Let's go back.

4 Is this type of analysis something that McKinsey
5 commonly undertakes?

6 A Yes.

7 Q And to the extent that this benchmarking analysis is
8 reflected in your declaration -- and at the risk of this not
9 being a very -- being an unwieldy question I'll try it.

10 If you can refer to paragraph 13 that begins on
11 page 7 in your declaration?

12 A Yes.

13 Q Is the information contained in paragraph 13 sort of a
14 product of this benchmarking work that you did, and the
15 chart that you see there?

16 A The chart is certainly a product of that work, and
17 again, as I believe we discussed in deposition, that chart
18 was -- the chart as you see here was a joint product, we did
19 our own analysis and then aligned with American on the
20 output, and I'm not sure who actually produced the chart in
21 terms of putting ink on paper.

22 Q Okay.

23 A The comment about -- let me just read it.

24 "As -- first as American's key competitors reduced
25 aircraft labor and debt serving costs -- debt services costs

1 through Chapter 11 reorganizations American's structure
2 became uncompetitive relative to its peers."

3 That obviously suggests some trend analysis, and
4 we were really focused just on where American's costs are.
5 The fact that American's competitors were able to reduce
6 their costs during bankruptcy reorganizations in the past is
7 certainly well known to me and I think reasonably well
8 understood in the industry, and so that's my general
9 industry knowledge behind the -- you know, sort of tread
10 implication at that point.

11 Q Sort of back looking.

12 A Yeah.

13 Q Okay. Okay. But other than this one paragraph in your
14 declaration is this benchmarking work that you were doing
15 reflected, do you know? I don't want you to have to flip
16 through it.

17 A No, I do not believe in my declaration that we -- that
18 I discussed the category by category cost differences.

19 Q Okay.

20 A Again, I think from a strategic and business planning
21 standpoint the key issue is labor costs overall.

22 Q Okay. So is it fair to say though you did more work
23 than what is reflected now in your declaration?

24 A Yes. Yes, we did.

25 (Pause)

1 Q Now you did work beyond the revenue model, right?

2 A We did.

3 Q Okay. And was part of that work to analyze the
4 sensitivity of the business model?

5 A Again, that was not a specific end product so to speak.
6 We certainly -- the team -- I should be specific -- looked
7 at sensitivity to insure that the model was behaving in a
8 way consistent with our expectations. In other words, this
9 sort of a back of the envelope check that if revenue rises
10 by X percent what should happen to results, if capacity
11 changes by X percent who should happen to results? And so
12 we did that for make sure that the model was yielding
13 changes that were consistent with our expectations, and that
14 was the case certainly.

15 Q And perhaps for clarity if you would, if you could
16 briefly explain what it is to sort of analyze for
17 sensitivity?

18 A Sure. Sensitivity analysis is a process by which upon
19 having set a number of assumptions that combined with
20 mathematical formula yield a certain result you then move
21 those assumptions. And say for a given movement in
22 assumption X how much does the result change?

23 Q So, you know, correct me if I'm not fairly
24 characterizing it. So you did some of this.

25 A Uh-huh.

1 Q But it sounds like it wasn't necessarily kind of done
2 in a systematic way to do this with absolutely every
3 assumption that's in the business model?

4 A Again, it was done to -- fairly systematically to make
5 sure that the model was working properly and behaving
6 properly.

7 Again, this is an industry where we have, you
8 know, at least 30 years of relevant history and lots of
9 historical and empirical sensitivity data in terms of, look,
10 if capacity moves by X what happens to results, and the
11 correlations are quite tight. And so we want to make sure
12 that our model is yielding similar sensitivity.

13 I think if what you're getting at was did we spend
14 a lot of time focusing on, you know, if we're wrong by this
15 amount what happens and what are the implications of that?
16 No, we didn't. I guess if only because those sensitivities
17 are well understood by us and by management.

18 Meaning the airline business is a very sensitive
19 business, and you know, if industry capacity grows in excess
20 of demand for any period of time by even a small amount
21 that's a big deal. If fuel prices, you know, increase by 20
22 or 30 percent that's a big deal.

23 These are all big deals, and unfortunately that's
24 one of the reasons why this industry is certainly not among
25 the most profitable in the world.

1 Q But the model allowed you to make these sensitivity
2 adjustments --

3 A Yes, it did.

4 Q -- that you did? Right. Okay.

5 And then -- and correct me if I'm wrong, it sounds
6 like you didn't really run like I think what hopefully we'd
7 agree would be referred to as like a downside scenario for
8 the model overall?

9 A No, we did. You mean -- sorry, maybe I need to make
10 sure I understand your question.

11 Q Yeah.

12 A We run a smaller airline scenario, we did not run a
13 business downturn scenario, at least not holistically,
14 meaning you know, combination of fuel price changes, GDP
15 changes, you know, demand and growth changes, et cetera, et
16 cetera.

17 Q Yeah, I appreciate that --

18 A Yeah.

19 Q -- description, that was what I was trying to --

20 A Yes.

21 Q -- to get at --

22 A No, we did not.

23 Q -- talking about downside scenario.

24 A Yeah.

25 Q And just for completeness, so is it fair to say then

1 that you didn't run sort of this kind of comprehensive
2 upside scenario? You know, the sun is shining and we're
3 very, very happy.

4 A Yeah, we kept fantasy to a minimum, you know, put
5 differently.

6 No, we did not. And a couple of -- on the
7 downside scenario partly we were constrained by time, six
8 weeks or so is a fast-paced effort. We certainly understand
9 that a business downturn is a possible event over the course
10 of the forecast period.

11 It's worth noting that airlines don't typically
12 include business downturns in their plans, it's just too
13 hard to gauge. Certainly if we had more time we would look
14 at that. It's fair to say that that would yield a worse
15 result, it's fair to say that that would probably increase
16 the degree of cost savings required across the board.

17 An upside scenario, to be frank, I think is
18 imprudent. I've seen lots of upside scenarios and
19 relatively few of them materialize.

20 I'm going to use a statistical term here which may
21 or may not be familiar, but airline results tend to have a
22 bit of what we'd call a plasonlike (ph) distribution to
23 plan. Meaning you rarely exceed plan. You can undershoot
24 plan by a little a lot of the time and occasionally
25 undershoot the plan by a lot.

1 Q Okay. I accept your explanation --

2 A Yeah.

3 Q -- but you just -- you didn't do that analysis?

4 A No, no, we didn't. Yeah, sorry.

5 Q All right. And you know, had you ever had in your
6 experience at McKinsey to deliver sort of a project of this
7 size and magnitude in the time that was allotted and
8 required?

9 A Certainly not in weeks.

10 Q Yeah.

11 A In man hours, yes. As I believe I said in deposition,
12 you know, we had a large team of people working, somewhere
13 in the neighborhood of 100 hours a week.

14 Q Yeah. But you would agreed --

15 A Yes.

16 Q -- it was as greatly compressed time schedule?

17 A Absolutely.

18 Q Now returning to your direct, and correct me if I'm
19 wrong, but when you were discussing code sharing I believe
20 you made a statement regarding sort of when the benefits of
21 that would begin to materialize --

22 A Yeah.

23 Q -- and in your view there was a normal amount of time
24 for that to take place.

25 So what is that normal amount of time, can you

1 tell us?

2 A Yeah. From the initiation of negotiations, depending
3 on the level of interest of the counterparty and the
4 complexities involved, you know, we've seen ranges of
5 anywhere from 6 to 18 months, maybe on the outside 24 months
6 to, you know, complete those negotiations and implement
7 deals.

8 Q Okay. And I think this was sort of in your response,
9 but the basis for your understanding or your --

10 A Having been involved in those negotiations before, not
11 directly, but as providing analytical support.

12 Q Okay. And then similarly when you testified regarding
13 product upgrade I think you there also spoke of sort of a
14 normal amount of time for that to materialize; is that fair?

15 A Yeah.

16 Q And again, can you identify what you mean by a normal
17 amount of time --

18 A Yeah.

19 Q -- in that context?

20 A Here the big driver is you don't get any benefit from
21 product upgrades until they are physically in place, and so
22 there are constraints in terms of how fast you can retrofit
23 aircraft, how fast you can, you know, get the technology on
24 board, et cetera, et cetera, and so we made assumptions,
25 worked with -- together with American executives over the

1 time line by which these changes would be rolled out across
2 the fleet.

3 Q Okay. Can you give me a sense of what the timeline --
4 I mean I understand it may vary product to product.

5 A Yeah. I'm -- again, I believe the bulk of those
6 changes were spread out somewhat linearly in the 2012 to
7 2014 or '15 time frame with most in place by 2015, with the
8 exception of those associated with aircraft that are going
9 to be believed between 2015 and 2017.

10 Q Okay. And again, the basis of your sort of assigning a
11 time period for these things?

12 A Was the roll out plan provided to us by American, which
13 again looked to us to be a reasonable starting point. You
14 can do it faster, you can do it longer, the big variable
15 here is how much aircraft down time you're willing to
16 absorb.

17 And just for -- Your Honor, that's -- to make
18 these upgrades can take anywhere from a week to two weeks of
19 maintenance time, and so depending on whether or not you do
20 those aligned with a scheduled maintenance event that can
21 involve you pulling an aircraft out of revenue service,
22 which is certainly a choice that some airline choose to
23 make, but that's the big driver. You can do these things
24 quite quickly or you can spread them out over time.

25 BY MS. PARCELLI:

1 Q So it can vary quite a bit?

2 A Yeah.

3 Q Okay.

4 MS. PARCELLI: Thank you, I have nothing further.

5 THE WITNESS: Okay.

6 THE COURT: All right.

7 UNIDENTIFIED SPEAKER: Could we have just two
8 minutes?

9 THE COURT: Sure.

10 UNIDENTIFIED SPEAKER: Thanks.

11 THE COURT: Rather than go out and come back I'm
12 just going to linger if we're really talking about two
13 minutes.

14 UNIDENTIFIED SPEAKER: Okay.

15 (Pause)

16 THE WITNESS: I probably have the best perspective
17 on that if you want.

18 (Laughter)

19 THE COURT: In an ideal world what time are you
20 trying to get out of here?

21 THE WITNESS: Look, I think we might have passed
22 that point. I mean if I was to get out of here at 12:45 I
23 would make this flight, on the other hand while my personal
24 obligations are important, there is much more at stake here
25 for all parties --

1 THE COURT: Right.

2 THE WITNESS: -- and I'll go as long as is
3 necessary.

4 THE COURT: I appreciate your flexibility.

5 All right. So we'll see how it -- how it goes.

6 CROSS-EXAMINATION

7 BY MS. KRIEGER:

8 Q Good morning.

9 A Good morning. Good to see you again.

10 Q It's still morning, Mr. Dichter.

11 A Yeah. For a minute.

12 Q I got it under the wire. Good to see you again.

13 Let me ask you, you testified that the reason that
14 American brought McKinsey in to build an independent revenue
15 model is that they wanted something -- or you provided
16 something that gave greater transparency for purposes of
17 Chapter 11?

18 A Uh-huh.

19 Q Can you describe for us in what ways the revenue model
20 that you've built for American Airlines and that they're
21 using now in the plan for success is more transparent than
22 the previous revenue model?

23 A Sure. Really it's around the ability to take the
24 drivers of revenue performance, which I outlined before,
25 those three exogenous factors and the strategic levers that

1 are outlined in the plan, assign them to the individual
2 market flows and to be able to see the relationship between
3 those drivers and the revenue outcome.

4 And maybe just to illustrate the point, I wasn't
5 present, but my team and American executives had a multi-
6 hour session with the UCC where they walked through the
7 model cell by cell to explain the methodology and walk
8 through how the assumptions linked to the output. That
9 would be something that really wouldn't be possible using a
10 typical regression-based forecasting model, it's just a bit
11 too -- pardon the colloquial term -- but black boxy, you
12 know, a bunch of stuff comes in and a bunch of stuff goes
13 out and there's some scientists that could explain what
14 happened in the middle, but to a layperson I think we'd all
15 be lost.

16 Q And so the transparency, to clarify, it's both
17 transparency to the executives at American who are working
18 with it determine actions to be based on this model?

19 A Yes, I think that's fair to say.

20 Q As well as to stakeholders in the Chapter 11?

21 A Yeah. And by the way, it's our belief that this is a
22 better way of planning in any context, and you know, we've
23 been trying to help airlines see that around the world over
24 the last few years, so.

25 Q And just again to your knowledge --

1 A Yeah.

2 Q -- I know you said that you didn't focus very much on
3 American's specific revenue model that existed when you came
4 on board, but do you have any understanding of what they
5 were doing with their revenue model in the way of driving
6 action prior to your coming on the scene?

7 A Again, this is my understanding, as I said before, I
8 didn't spend much time looking at it or talking about it for
9 that matter, but it's my understanding that the model was
10 more used to forecast a result of a set of actions than
11 necessarily to define actions.

12 Now there's always an iterative process in
13 planning, meaning if you don't get at result that you like
14 you go back to the drawing board and you come up with
15 different actions and see whether those actions yield a
16 better result.

17 Q Okay. And did -- were you aware of that iterative
18 process having taken place prior to your coming on the
19 scene?

20 A Not specifically, but I'd be very surprised if it
21 didn't happen.

22 Q Okay. And just to clarify as well, do you know -- had
23 American ever had a driver-based forecasting model?

24 A Not like the one that we built with them, no.

25 Q Okay. Anything close to it?

1 A The model that was described to me is again quite
2 robust and complicated. I think it does link to drivers on
3 the cost side, but the revenue side of the model at least as
4 I understand it is more trend and regression-based than
5 driver-based.

6 Q Okay. Now can I ask -- the starting point for the
7 revenue improvement -- excuse me -- the overall earnings
8 improvement target by the end of the business plan is
9 American's current gross revenue?

10 A I'm sorry, I'm not sure I understand. You mean the --
11 our six-year forecast --

12 Q Right.

13 A -- starts with American's 2012 plan, which of course is
14 partly executed --

15 Q Right.

16 A -- and partly forecast and continues through 2017.

17 Q Okay. And the total revenue starting point is what in
18 that model?

19 A Well, again, I think this is public and I'm not going
20 to remember the decimal points in any event, but it's --

21 MR. POLLACK: Your Honor, excuse me, I don't
22 believe --

23 THE WITNESS: Oh, okay, sorry. Yeah. Over the
24 last few years or over the last -- American's --

25 BY MS. KRIEGER:

1 Q The publicly reported earnings, yeah.

2 A The publicly reported number has put American's revenue
3 in the vicinity of \$20 billion.

4 Q Twenty billion, okay.

5 And so as I also understand it the targeted
6 revenue improvements that are built into the business plan
7 that's been presented to us are incremental revenue above
8 and beyond what's forecast as the natural growth?

9 A That's correct.

10 Q Okay. And the -- that natural growth is derived
11 according to the -- the growth factor that you described in
12 your direct testimony?

13 A Yes, that's correct.

14 Q And one other question for clarification.

15 I know that you've probably seen the break down of
16 the total -- the total 3.1 billion --

17 A Yeah.

18 Q -- targeted improvement by the end of 2017 breaks down
19 into the buckets of --

20 A Yeah.

21 Q -- targeted revenue improvement, targeted non-labor
22 cost reductions, and targeted labor cost reductions.

23 The number for the targeted labor cost reductions
24 as presented in the written business plan presentation has
25 been shown as 1.5 billion, but for purposes of discussions

1 here today and in some other testimony we've also heard a
2 number 1.25 billion.

3 And so I just want to clarify that when --

4 A Sure.

5 Q -- you're speaking to the number of 1.25 billion that
6 represents the annual average of --

7 A Yes, my understand --

8 Q -- of 1.5 billion.

9 A -- 1.5 is the 2017 end point, and --

10 Q Study state exit?

11 A Exactly.

12 Q Yes.

13 A Yeah.

14 Q Okay.

15 A And 1.25 is the average over the period.

16 Q So I just want to make sure we're talking about -- that
17 people understand --

18 A Yes.

19 Q -- from the transcript we're talking about the same
20 number in it.

21 A Yeah.

22 Q Now as I understand --

23 THE COURT: Let me just clarify. We're talking
24 about the same analysis, just different measures that come
25 out of that analysis.

1 MS. KRIEGER: Right.

2 THE COURT: One's an average, one's an end point.

3 THE WITNESS: Yes.

4 BY MS. KRIEGER:

5 Q Exactly. And we're talking about the same target.

6 Okay.

7 And also for clarification sometimes it's been
8 referred to as labor cost as opposed to labor cost
9 reduction, but when those references are being talked about
10 you mean the targeted reduction in labor costs --

11 A That's correct.

12 Q -- from where they are now, and also referred to as the
13 labor ask --

14 A Yes.

15 Q -- in the aggregate.

16 And so when -- sometimes when people say lower
17 labor cost or -- it gets confusing as to whether they're
18 talking about a lesser amount of labor concessions or --

19 A No.

20 Q -- a greater amount, so I'll try to be --

21 A Yeah, is --

22 Q -- clear.

23 A -- more better or worse.

24 Q Yes. Now you mentioned that when you did your labor
25 benchmarking exercise, as I understand it, it was -- the

1 starting point was reflected in exhibit -- American Airlines
2 Exhibit 103.

3 A Yes.

4 Q That's part of your declaration. And is the end point
5 of that -- or review shown in Exhibit 133 at page 27 of your
6 declaration?

7 A It's certainly the supporting evidence for the
8 statement that I make at the end of paragraph 13.

9 Q Is that -- but is that part of the benchmarking
10 exercise --

11 A Yes, it's --

12 Q -- that you --

13 A Yes.

14 Q -- as you've referred to?

15 A Yes, it was.

16 Q So it's saying that the end result of the labor cost
17 reductions that have been targeted would yield that --

18 A No, what this exhibit specifically shows where
19 American's labor costs per ASMR in 2011 are -- were in
20 2011 --

21 Q That's 103 I'm talking about.

22 A Yes, exactly.

23 Q But then when you look at 133 --

24 A Oh, 133, I'm sorry.

25 Q -- yes, at page 27 of the declaration.

1 A Yeah, this is a -- as I believe I mentioned in
2 deposition, this is something of an illustrative analysis.
3 It's basically saying where would American's costs be today
4 if it had the benefits of the labor cost reductions that the
5 company has asked for. And I say illustrative because
6 obviously it's nearly impossible to implement those kinds of
7 changes over night.

8 And second point hopefully obviously is -- 2011 is
9 in the past. And so --

10 Q Okay. And does that expect that the labor cost at the
11 other airlines are going to remain as is now?

12 A It doesn't expect one way or the other. It simply says
13 -- I mean the purpose of this is, as I think I mentioned
14 before, was one triangulation on the labor cost target or
15 the labor cost asked, as it's been variably referred, is to
16 understand does that put American's labor costs in line with
17 its peers, you know, plus or minus?

18 And I think the output of this analysis showed
19 that the new American, as we describe it, so American with
20 the labor cost targets equalize for 2011 would in fact put
21 American in line with its peers. Slightly above US Airways,
22 you know, match neck and neck for -- to Delta, and slightly
23 below United.

24 So we made no assumptions over time about
25 increases in other airline labor costs.

1 Q Okay. And -- but then just to be clear the 1.5 billion
2 total aggregate labor cost reduction that's been sought, is
3 it that end state cost reduction that has been used to then
4 show where American arrives at if on this chart 133?

5 A Yeah, good question.

6 Again, I -- my focus on the team was describing
7 the analysis that should be done and checking the output to
8 make sure that it made sense. I would have guided them to
9 have adjusted that for 2011 norms.

10 And so it should be that it's not the full 1.5,
11 but you know, something less than that based on the size of
12 the airline in 2011.

13 So the 1.5 is based on an airline of X size at
14 2017, the 2011 airline is smaller than that, and so you'd
15 scale that number down.

16 Q All right.

17 A But I can't honestly say that I checked that.

18 Q Okay. And then just again for clarity.

19 A Yeah.

20 Q If you were wanting to model where American would end
21 up had it achieved its goals or should it achieve its goals
22 at the end of 2017 and show its competitive labor cost
23 exfuel position, that the point, vis-à-vis, the other
24 airlines, you would change those bars as well, you would
25 project them out?

1 A Yeah, you would. I mean let me describe to you what
2 you do.

3 In the case of Delta at least several of their
4 labor groups, pilots in particular, have a current contract
5 that has escalation rates built into it, and so some of that
6 is known or knowable.

7 In the case of United they're currently in
8 contract negotiations.

9 US Airways is currently in extended contract
10 negotiations as they try to merge the two pilot groups
11 there.

12 We don't know the outcome of those negotiations,
13 but -- and by the way, I'm not a labor bargaining expert by
14 any means -- but certainly as has been reported by others
15 there is something of a pattern bargaining -- pattern of
16 conduct in this industry.

17 And so if we did that we would, you know, assume
18 that the labor rates in those airlines end up somewhere in
19 the peer set, and obviously where American's costs would be
20 at the end of that outcome would influence that peer set.

21 Q Okay. And just finally on the charts 103 --

22 A Uh-huh.

23 Q -- in Exhibit 103 and 133 the set of comparators that
24 you are using for purposes of your labor cost benchmarking,
25 those are all the large network carriers --

1 A They are --

2 Q -- as I understand it?

3 A -- the large network carriers. And just to be clear,
4 that's United now refers to the combination of Continental
5 and United, Delta and US Airways. I believe in deposition I
6 suggested that it might include a couple of the larger low
7 cost carriers. We sometimes do that, in this case it did
8 not.

9 Q And just confirm for us this is American's and
10 McKinsey's consensus on what's the appropriate benchmarking
11 comparator set?

12 A Yes. Yeah, I mean there are various reasons to look at
13 low cost carriers, mostly -- for the most part low cost
14 carriers will show lower labor rights, not all -- in all
15 cases, but certainly there are specific areas where the
16 productivity targets that low cost carriers have achieved
17 are available to mainline carriers, and we sometimes look at
18 that, but in this case we focused on the large network
19 carriers.

20 Q Okay, thank you.

21 So as I understand now the benchmarking dealt only
22 with the aggregate of total labor costs and does not purport
23 -- you did not purport to do any benchmarking of, for
24 example, pilot labor costs?

25 A No, we did. We looked at -- again, this was not part

1 of our original engagement scope -- but at American's
2 request we did use Form 41 data to look at pilot costs per
3 ASM, pilot costs per block hour, maintenance costs per ASM,
4 I believe maintenance cost per block hour, flight attendant
5 costs per block hour, flight attendant costs per ASM, and
6 airport and ground handling costs per block hour, and
7 airport and ground handling costs per ASM.

8 Q Okay. And did you reflect those in any documents or --

9 A I believe there were documents, but as -- we did not
10 discuss this in the declaration and I did not rely on those
11 documents for the declaration.

12 Q Okay. And your opinion does not --

13 A No.

14 Q -- address it at that granule level --

15 A No, it does not.

16 Q -- the pronouncing on the appropriateness of any
17 particular labor cost reduction?

18 A No, again, from a strategic standpoint what in our view
19 really matters is overall labor costs.

20 Q And so just so we're clear, you are not expressing an
21 opinion about the apportionment of the total 3.1 billion in
22 improvements -- in financial improvements that's built into
23 the plan between the various buckets as you've termed them,
24 the revenue, the labor, and the non-labor cost?

25 A Certainly we express an opinion about the revenue

1 target. Certainly we expressed opinion about the non-labor
2 target. And we expressed an opinion about the
3 reasonableness of the labor target as a whole, vis-à-vis,
4 the question of whether or not that would be in line with
5 peers. But beyond that in terms of how the labor target
6 would be apportioned across labor groups, no, we did not.

7 Q Okay. And now when you give your benchmarking -- or
8 when you discuss benchmarking with American at what point
9 did you present the results of your analysis and to whom?

10 A I'm not entirely sure. A good number of the meetings
11 we had -- in fact I would suggest probably somewhere in the
12 neighborhood of 75 percent of the meeting that we had with
13 American executives were between my colleagues and those
14 executives. I, as perhaps as been on the record, live in
15 Tokyo, Dallas is a long way away and I came through with
16 frequency, but could not be there all the time.

17 Q Okay. And --

18 A But I was not present in that meeting.

19 Q Okay.

20 A I guess is a more direct way of answering the question.

21 Q Well, what I'm trying to focus in on is your opinion
22 that it would be imprudent you said as a planning
23 professional to emerge with a business plan that met all the
24 financial targets but where the labor costs were still
25 higher than American's legacy peers?

1 A Yeah. And again, as I stated before, that's my
2 opinion. And --

3 Q And is that an opinion that you were requested to give
4 to --

5 A No, that --

6 Q -- American?

7 A -- opinion I was not requested to give.

8 Q Okay. And that is not part of your declaration?

9 A It is not part of my declaration.

10 Q Okay. And was there any iterative process that you're
11 aware of in the building of the final plan in which McKinsey
12 implemented that discipline, if you will, on American?

13 For example, a plan was proposed, a set of buckets
14 and numbers were presented that provided a suitable
15 financial profile within the range of reasonable EBITDAR as
16 Mr. Resnick has testified.

17 A Yeah.

18 Q And McKinsey advised, now you need to go back and
19 increase the labor cost reduction because your labor costs
20 are not comparable to the peers?

21 A No, we did not.

22 Again, in the last two weeks of January as the
23 revenue number finalized and as I testified during -- or I'm
24 not sure whether you call it testimony -- but discussed
25 during deposition there were also some increases to the non-

1 labor cost targets based on the non-labor cost benchmarking
2 that we did, and so that combined with the work that
3 American was doing moved the labor cost target around a
4 little bit I presume in those last two weeks. But where it
5 ended up was in line with industry peers.

6 And so based on the comment that I made before I
7 wouldn't have had a chance to express that opinion because
8 there was none.

9 Q It just happened to --

10 A Yeah, there wasn't an outcome that was higher than
11 industry peers --

12 Q Okay.

13 A -- let's put it that way, at least not that I saw.

14 Q Okay. And then just for the sake of clarity, so you
15 didn't say you need to --

16 A No.

17 Q -- reduce your labor cost by 20 percent across the
18 board in order to reach this benchmarking target?

19 A No, we did not.

20 Q Okay. That was a target selected by American?

21 A Yes, through the process that I described.

22 Q Okay.

23 (Pause)

24 Q Now you mentioned that in this particular case you did
25 not run alternate scenarios or changes in the business model

1 comparisons through the revenue model and the business
2 modeling apparatus to see different outcomes, for example,
3 for a downside scenario?

4 A Well, again, just to be clear we did look at
5 alternative network configurations --

6 Q Right.

7 A -- as I described earlier, we did not --

8 Q Okay.

9 A -- look at a comprehensive downside scenario.

10 Q Okay. And once the plan became stabilized in the
11 footprint that we see it, as I understand it, it would -- it
12 would be possible to run an alternative with different
13 numbers, for example, different revenue assumptions,
14 different non-labor cost assumptions --

15 A Yes, absolutely.

16 Q -- just from targeted labor cost reduction assumptions?

17 A Yes.

18 Q Okay. And what would be involved in doing that? How
19 long would it take to do that?

20 A Well, it depends on exactly what you were doing. If
21 you simply wanted to test what would the outcome be if
22 industry capacity grew at X versus Y for instance --

23 Q Uh-huh.

24 A -- and was apportioned in exactly the same way that the
25 model logic assumes today, that could be done very quickly.

1 And again, the team did some of that to test that the model
2 was working.

3 The main reason that we didn't produce that as an
4 output is I think everybody well understands the
5 relationship between those big drivers and results. The
6 question of modeling a downturn scenario is a more complex
7 effort.

8 Q Okay.

9 A Yes.

10 Q But I'm not asking about --

11 A Yeah.

12 Q -- a downturn scenario now, I'm just asking what if the
13 allocation between labor cost savings and non-labor cost
14 savings were different? Instead of 1.5 billion that we're
15 1.4 billion on the labor side and that excess was added to a
16 different bucket.

17 A Yeah. That particular issue is complicated also, and
18 it's complicated -- and I believe Mr. Resnick discussed this
19 -- but it's complicated because if labor costs -- well,
20 sorry -- the -- you're asking about the total cost remains
21 the same and the apportion between two --

22 Q Yes.

23 A -- are different -- ah, okay.

24 Q It doesn't change the 3.1 billion --

25 A Yeah.

1 Q -- but there's a difference.

2 A It's still complicated --

3 Q Okay.

4 A -- for a slightly different reason.

5 But in the labor cost ask are -- and again, I
6 don't know the full details, I have headlines, if you will
7 -- but there are a number of productively-related elements,
8 and those productively-related elements affect the
9 scheduling of aircraft and the markets that you can serve.

10 And so --

11 Q And then the model has the capability to --

12 A No, it does not. And so if -- if you were to -- say
13 let's take the labor ask down from, you know, 1.25 on
14 average --

15 Q Uh-huh.

16 A -- down to a billion, you'd first need to know through
17 what means. Meaning which specific work rule changes or
18 benefits changes would you be suggesting that would make
19 that change?

20 Q So suppose -- let's suppose --

21 A Yeah.

22 Q -- you decide what means it's going to be.

23 A Okay.

24 Q Picking one.

25 A If those means affect the scheduling of aircraft in any

1 way or particularly affect the operating cost of aircraft as
2 opposed to the fixed cost base they will have an impact on
3 which markets you can viably serve --

4 Q Right.

5 A -- and so you would then need to generate another
6 network plan --

7 Q Right. Which is done through a model?

8 A Which is done through a model.

9 Q Uh-huh.

10 A And then feed that into the revenue model --

11 Q Right.

12 A -- and look at that output.

13 Q Exactly how long would that take?

14 A A few weeks.

15 Q Okay, a few weeks.

16 A Two to three maybe.

17 Q Okay. And the same -- is it in the same ballpark for
18 example if you got -- if you changed the amount of total
19 labor ask in some other way, whether you ascribed it to
20 wages or benefits or some other feature of -- that goes into
21 labor cost?

22 A Yes, it does. And again, the issue here is the
23 viability of an individual flight is very linked to the
24 operating cost and the schedulability of that flight

25 according to specific labor terms, supplier terms, and work

1 rules in that context.

2 Q Okay. So the -- the components of the modeling
3 system --

4 A Yeah.

5 Q -- are robust enough to be able to one, using these
6 different assumptions as inputs?

7 A Yes. But again, it sort of changed the dynamics of the
8 labor ask, check with operators as to how that affects --

9 Q Right.

10 A -- scheduling flexibility --

11 Q Uh-huh.

12 A -- feed that back into root specific economics --

13 Q Uh-huh.

14 A -- make choices about where you send your airplanes,
15 feed that network plan back into the model. So there's
16 certainly no toggle in the model --

17 Q No.

18 A -- where I can say, you know, change rest requirements
19 from --

20 Q Right.

21 A -- you know, 12 hours to 10 hours and see what happens.
22 If that were the case I'd --

23 Q Right.

24 A -- be a very wealthy person.

25 Q But if you -- and we haven't got there yet --

1 A Yeah.

2 Q -- it would be a great negotiating tool, but --

3 A Yeah.

4 Q -- what we have now in negotiations if you're
5 exchanging proposals --

6 A Yeah.

7 Q -- and counter-proposals and a counter-proposal comes
8 across the table and say do it this way rather than that way
9 then in order to figure out -- is this -- you know, can we
10 live with this --

11 A Yeah.

12 Q -- what's the impact on revenue, and the -- you would
13 do that, right?

14 A You would do it. And again, the time frame -- I know
15 what our part of it would be, you know, so --

16 Q Uh-huh.

17 A -- feeding in the new network plan, you know, probably
18 takes us a week and a half or so, I really don't know how
19 long it would take --

20 Q Okay.

21 A -- American or any other airline to iterate, you know,
22 it's network plan and go through the process that I
23 described.

24 Q Okay. And prior to McKinsey coming on the scene though
25 presumably they had a way to figure out costing out of

1 proposals and so on and then impact on their network plan?

2 A Yeah, I'm sure you can discuss that with Mr. Brundage,
3 but I would assume that to be the case.

4 Q Okay.

5 A Yeah.

6 Q I mean that's a normal thing to do --

7 A Yes, that is a very normal thing to do.

8 Q Okay. And -- but as I understand it this particular
9 business plan model that became stabilized was built not
10 just around a particular gross number of labor cost
11 reductions but a particular configuration of how those labor
12 cost reductions were made up, correct? Or that was the
13 input that went into this?

14 A No, no, you're getting at something important here.

15 Q Okay.

16 A Nowhere in the model is the labor ask.

17 So in other words, we don't go to the model and
18 say, well, what happens if it's a billion or a billion five?
19 There's a cost structure in the model, and the cost
20 structure reflects fixed costs, GNA, station costs,
21 maintenance cost per block hour, pilot cost per block hour,
22 et cetera, et cetera, and the labor ask was translated by
23 American executives into specific changes in those inputs
24 that we then glanced at certainly, did these look out of
25 line in any way? No, they didn't, they make sense. We did

1 not check that analysis, that wasn't part of our scope. Fed
2 that in the model to reflect the cost structure.

3 And then by the way, as an output of the model we
4 would then say does the labor costs, you know, overall look
5 in the range of 1.25 to 1.5 billion less than it was before?
6 You know, and yes.

7 But it's not an input to the model, it's an
8 exogenous input into the cost structure that is incorporated
9 into the model.

10 Q Okay. And again so I'm clear, the model is capable of
11 being able to model variations in those inputs?

12 A Certainly. If you made a proposal to the company that
13 changed pilot costs per block hour, you know, we could go
14 back in and change pilot costs per block hour and look at
15 the output of that.

16 Q Okay. And you could see the sensitivity of the output,
17 like within what range it would come out on the final profit
18 and loss, the financial --

19 A Yes, you could.

20 Q -- profile?

21 A There is some tie up between our model and American's
22 model --

23 Q Uh-huh.

24 A -- around how you merge costs and revenues, but yes.

25 Q Okay. And for my understanding as well, now is this a

1 model that's still solely in McKinsey's custody, so if they
2 need to do that they have to go to you to do it, or is it
3 within their control?

4 A That would be a neat revenue trick for us, but no, it
5 is in American's custody.

6 Q American owns it and they know how to run it?

7 A I believe they know how to run it, if not we'll
8 continue the process of making sure that they do.

9 Q And they know how to do the things you described?

10 A Yeah.

11 Q Okay. And then again, so getting back to the more
12 complex full downsize scenario just as a marker. About how
13 long would it take to run that kind of a scenario?

14 A Again, a single input change like that should be
15 relatively straightforward. The more input changes that
16 you're talking about, again, the more that triggers a new
17 network plan.

18 And so again, it's been said over and over again,
19 but I think it's an important point, the relationship
20 between individual cost drivers and P&L tends to be non-
21 linear because you across certain lines and you end up
22 producing different amounts of revenue, and you need to
23 understand that relationship, and that's that multi-step
24 process that I described.

25 Q Okay. Can you give us a ballpark time frame using this

1 model? Is it less than 30 days or --

2 A Again, I'd be testifying --

3 THE COURT: Wait.

4 THE WITNESS: -- to something I don't know the
5 answer --

6 THE COURT: Hold on a second.

7 THE WITNESS: -- to.

8 THE COURT: Hold on a second.

9 THE WITNESS: Yeah.

10 THE COURT: We've spent a lot of time on this and
11 I sort of let it go --

12 MS. KRIEGER: Okay. I just --

13 THE COURT: -- but ultimately I'm not -- I'm not
14 sure how much additional added value for purposes of 1113 --

15 MS. KRIEGER: Okay.

16 THE COURT: -- decisions. There may be
17 discussions you want to have offline --

18 MS. KRIEGER: No, I --

19 THE COURT: -- about various things, but I kind of
20 get the picture here.

21 MS. KRIEGER: Okay.

22 THE COURT: But just so we can move this long.

23 MS. KRIEGER: I'll close this subject.

24 THE WITNESS: Okay.

25 BY MS. KRIEGER:

1 Q Are you aware that union side financial advisors had
2 requested alternative scenarios be run through the model
3 from -- from the company?

4 A I'm not aware, no.

5 Q Okay. And you're not aware that they were told it
6 would take four to six weeks to do that?

7 A I'm not aware. But again, the piece that I can't
8 testify about is how long would it take American to build
9 the new network plan that would feed into that model --

10 Q Okay.

11 A -- and so our piece of that as I said is, you know, a
12 matter of brief weeks, and if American says four to six
13 weeks I presume they believe that it would take them fourish
14 weeks to develop the new network plan.

15 Q Okay. And you're not aware that more than two months
16 ago the unions asked for that and --

17 A No, I'm not.

18 Q -- nobody as gotten back to them to provide it?

19 A That's --

20 MR. POLLACK: Objection.

21 THE COURT: Sustained.

22 MS. KRIEGER: Okay.

23 THE COURT: Asked and answered.

24 MS. KRIEGER: Okay.

25 (Pause)

1 BY MS. KRIEGER:

2 Q In your prior testimony I think you -- you've mentioned
3 that the period of time in your experience for getting a
4 code share agreement could run from -- anywhere from 6
5 months to 24 months.

6 Can you identify any situation in which a code
7 share agreement took 30 days or less to achieve?

8 A Certainly not off the top of my head.

9 Q Okay. Now in -- in prior testimony you talked about
10 some factors contributing to American's decline in financial
11 performance over the past decade, and I think you mentioned
12 at least three factors that you described as generally
13 applicable to all airlines. The competition for low cost
14 carriers, the fuel price volatility, and unstable economic
15 situation; is that correct?

16 A That's correct.

17 Q And then you mentioned that there were some additional
18 factors specific to American Airlines. One of those factors
19 you described as consolidation which is something that
20 happened to American as opposed to something American
21 participated in; is that correct?

22 A Yeah, and what I meant to say there is this is
23 something that obviously affected the whole industry, it
24 just affected others positively and American negatively.

25 Q Okay. And I also believe that -- well, this is a self-

1 financed bankruptcy as I understand it, and you've testified
2 that it's not typical for a Chapter 11 to be self-financed
3 as AMR's is?

4 A To my understanding it's not, but I'm not a bankruptcy
5 expert, I'm not a banker, and certainly wasn't involved in
6 that decision. But if I think about the last few
7 bankruptcies that I'm aware of there's been DIP financing in
8 place, but that's -- that was the basis for that comment.

9 Q And to be clear, the EBITDAR target analysis that
10 Mr. Resnick provided that Rothschild worked on, McKinsey did
11 not express any opinion on the EBITDAR did you?

12 A No, certainly not. We were not asked to. I did look
13 at it and it seemed reasonable to me, and if I did not I
14 would have said something.

15 Q Okay. But you're not here expressing an expert opinion
16 on the necessity of that target?

17 A I'm not, no.

18 Q Okay. Thank you.

19 (Pause)

20 MS. KRIEGER: There's a few additional questions
21 having to do with the scope and code sharing RJ issue that
22 my colleague, David Dean, would pursue.

23 THE WITNESS: Okay.

24 MS. KRIEGER: Thank you.

25 CROSS-EXAMINATION

1 BY MR. DEAN:

2 Q Good morning.

3 A Good morning.

4 THE COURT: No, now it's afternoon.

5 MR. DEAN: Okay. Whoops.

6 THE WITNESS: Good afternoon.

7 BY MR. DEAN:

8 Q We'll try to make it very short.

9 A That's all right.

10 Q I'm David Dean representing the Allied Pilots
11 Association.

12 I will be focusing on scope issues, and in
13 particular just the question of who flies the very large
14 regional jets and job protections for the pilots in the
15 context of domestic code shares.

16 First, American Airlines current outsources to
17 affiliates, using your definition, flying on both 50-seat
18 and 70-seat regional jets, correct?

19 A Correct.

20 Q American Airlines owns all those jets?

21 A I do not know the current details of American's
22 arrangement with its affiliates.

23 Q Okay. In preparing the declaration that you adopted
24 today as your testimony, were you given the opportunity to
25 review the proposals that the pilots have made for

1 flexibility in regional jet flying?

2 A No, our focus was on an outcome not a means to that
3 outcome.

4 Q Okay. And you -- and similarly you've not reviewed the
5 pilot proposals for flexibility and domestic code sharing?

6 A No, I have not.

7 MR. DEAN: Then I don't think I have any
8 questions. Thank you very much.

9 THE COURT: All right.

10 THE COURT: I was wondering what the follow up to
11 that was going to be.

12 (Laughter)

13 MS. KRIEGER: You made it easy.

14 MR. SHERWOOD: Jack Sherwood, Loenstein Sandler
15 for the TWU.

16 CROSS-EXAMINATION

17 BY MR. SHERWOOD:

18 Q Good afternoon, Mr. Dichter.

19 A Good afternoon.

20 Q We might get you to that plan after all.

21 Let me ask you about your 2011 labor costs per ASM
22 exhibit that's on page 8 of your declaration.

23 A Yeah.

24 Q First let me ask, I note that Southwest is not in that
25 -- in that group. If Southwest was in that group where

1 would they fall in relation to the other airlines?

2 A That's a good question.

3 Certainly on labor costs per employee Southwest is
4 reported to be in many cases above other mainline carriers,
5 they're also typically more productive.

6 Q I just want to know where they would fall in relation
7 to the other carriers, I don't --

8 A Yeah, I'm honestly not 100 percent sure, but I don't
9 think they'd be above the average. Certainly not per ASM.

10 Q Now when you talk about labor costs per ASM does that
11 include non-union labor?

12 A Yes, it would include non-union labor to the extent
13 that non-union labor is involved in the labor cost
14 categories as defined by Form 41.

15 And I guess what I mean by that is Form 41
16 wouldn't -- there's a lot of -- if you -- so it labors any
17 human being that's doing work of any kind, which is a
18 reasonable way to think about it, there's a lot of labor in
19 G&A, general and administrative costs, that are not treated
20 as labor per such by Form 41, and so those would be excluded
21 here.

22 Q In terms of general and administrative costs how do
23 those costs at American compare to its peers?

24 A Yeah. We did not specifically analyze that. It is
25 certainly my understanding that American's general and

1 administrative costs have been higher over the last couple
2 of years than its peers, and I believe that's one of the
3 reasons that its recently embarked on an effort to reduce
4 those costs.

5 So that was in effect one of the non-labor cost
6 categories that we looked at as we looked at initiatives
7 that had been launched, and several of American's peers have
8 launched comprehensive general and administrative cost
9 reduction efforts while American has made changes over the
10 years perhaps not been as extensive as some of its peers
11 have and they've recently launched an effort that looks to
12 us very much like the efforts launched at other carriers.

13 Q But just to be clear in terms of management
14 compensation, historically American has been higher than its
15 peers?

16 A Again, that's my understanding. We did not analyze
17 that at a granular level and I don't have data to prove that
18 one direction or the other.

19 Q And let me just say I think I know the answer to this,
20 but just to be clear.

21 You understand that American, pursuant to its 1113
22 ask here, is seeking to expand its ability to outsource
23 maintenance, right?

24 A That's correct.

25 Q But you do not know do you how it plans to outsource

1 that maintenance; is that right?

2 A You mean to whom?

3 Q To whom.

4 A I do not.

5 Q And you don't know where the entities are located that
6 would be doing the outsource maintenance work; is that
7 right?

8 A I do not.

9 Q Now in your direct you talked about joint business
10 agreements as part of the revenue piece of the -- of the
11 business plan; do you recall that?

12 A I do.

13 Q And would you agree that that plan is not fully
14 implemented at this point in time?

15 A That's correct.

16 Q And that American has substantial work to do in the
17 future to implement its joint business agreements with its
18 projected partners generally?

19 A Yes, I would, I would characterize that as
20 implementation work; however, meaning the agreements are in
21 place, they need to be implemented. Some of those
22 implementation activities relate to IT systems and the like
23 as opposed to difficult further negotiations.

24 Q Now when you spoke about the use of affiliates to fly
25 planes you would agree that those -- those affiliates have

1 to hire pilots and flight crew and maintenance crew and the
2 like, correct?

3 A In most cases, yes.

4 Q So is the use of affiliates more or less subcontracting
5 out labor?

6 A It's subcontracting out operations, and certainly to
7 the extent that those operations involve labor that's a
8 component of that.

9 Q Do you know whether the Form 41 data that you relied on
10 in your report is used in labor negotiations?

11 A I believe it is.

12 MR. SHERWOOD: Give me one second, Your Honor.

13 THE COURT: Certainly.

14 (Pause)

15 THE COURT: It's always tough to bat clean up.

16 MR. SHERWOOD: Yeah, I know I'm going to miss
17 something, but --

18 THE COURT: No, if you need a minute that's fine.

19 (Pause)

20 BY MR. SHERWOOD:

21 Q All right, I have one more question. Or I had one more
22 question.

23 It -- just to closing the loop, I think this is
24 obvious, but you are not personally involved in the
25 negotiations between the unions and management concerning

1 this motion; is that right?

2 A No, I am not.

3 Q Okay.

4 MR. SHERWOOD: Thank you. I have nothing further.

5 THE COURT: Thank you.

6 MR. BUTLER: Your Honor, for the record, Jack
7 Butler, Skadden, Arps on behalf of the creditors' committee
8 personally has no examination of this witness (indiscernible
9 - 12:39).

10 THE COURT: All right.

11 MR. POLLACK: We have no redirect, Judge.

12 THE COURT: All right. In light of the objections
13 made I -- well, let me take sort of a 30-second spin on
14 where we are, because I don't know if there's -- if there'd
15 be a request to recall a witness nor to have further
16 examination to address various objections as they may be in
17 their current form.

18 So what I would ask is if the witness wouldn't
19 mind stepping down and going outside. We'll chat and
20 hopefully we'll have an answer to you very, very shortly in
21 the next five minutes --

22 THE WITNESS: Okay.

23 THE COURT: -- as to whether you can try to run
24 and catch that flight.

25 MR. POLLACK: All right?

1 THE WITNESS: Sounds good.

2 THE COURT: Well, I don't know about that, we'll
3 see. All right. We'll hold out some hope. Thank you.

4 MR. POLLACK: And Your Honor, at this point we
5 would move the admission of Mr. Dichter's declaration, which
6 is American Airlines Exhibit 400, as well as the three
7 exhibits referenced therein, 401, 402, and 403.

8 THE COURT: All right. After the testimony that
9 I've heard what is the status of the objections that are
10 going to be made or not made?

11 MS. PARCELLI: Your Honor, as regard to the issues
12 I raised I think we now have adequate foundation in the
13 record, so now I would join Ms. Krieger's objections that
14 she raised, but not our sort of global objection.

15 THE COURT: Okay. So Ms. Krieger, you have to
16 floor as to defining the scope of the objection to his
17 testimony.

18 MS. KRIEGER: Your Honor, has hit it on the head.
19 Our objections -- we are also not concerned with
20 foundation for most of the opinions that he's expressed, but
21 there are some particular portions of the declaration,
22 particularly in paragraph 16, where he purports to not just
23 describe the advantages and benefits of flying regional jets
24 and having code share agreements and so on and how that
25 factored into the model, but also purports to opine on what

1 restrictions in American's collective bargaining agreements
2 with the pilots supposedly prevent the achievement of the
3 benefits laid out there.

4 And I would want to work with I think opposing
5 counsel to indicate, you know, portions of the text of the
6 declaration, and there may be some further portions that are
7 of like kind, that would eliminate the conclusions that are
8 based on -- that would be based on a labor expertise or
9 collective bargaining expertise, and limit it to the facts
10 having to do with the -- his view of regional jets and code
11 share and so on, and I think we might be able to work out a
12 stipulation on that.

13 MR. POLLACK: Judge, if I understand Ms. Krieger's
14 objectives here we certainly are happy to discuss a
15 potential resolution.

16 THE COURT: Well, I understand his testimony to be
17 the modeling of the revenue and various other things, that
18 he wasn't really offered -- I mean it's the classic problem,
19 somebody has to -- has to be a professional, which he
20 clearly is, and a knowledgeable professional and a diligent
21 professional, he has to make sure to talk to various people
22 so that's he's not doing something that has no basis
23 whatsoever, but I also understand he's not offered really to
24 go into the minutia of various particular labor issues. So
25 I would suspect you could probably work this out.

1 MS. KRIEGER: And I would propose that perhaps if
2 you want to have it admitted subject to our being able to
3 work out the objectionable parts of it for purposes of
4 today.

5 THE COURT: Yeah. The only thing I want to make
6 clear is that's -- that's the nature of the objection, the
7 objection is not -- I got out my rules at a break here --
8 he's clearly not a lay -- this is clearly is not lay witness
9 opinion under 701 because it's not rationally based on
10 perception and it is in fact based upon scientific,
11 technical, or specialized knowledge within the scope of
12 Rule 702, and he does seem to fit well within the confines
13 of 702 which say, if scientific or specialized knowledge
14 will assist the trier of fact, which it will, and understand
15 the evidence, which it will, a witness qualified as an
16 expert by knowledge, skill, expertise, training, or
17 education may testify if the testimony is based on
18 sufficient data. There's clearly data here. And whether
19 it's by reliable principals and methods and whether he's
20 applied the principals and methods reliable to the facts of
21 the case.

22 I understood the withdrawal of the earlier
23 objection essentially to be a withdrawal of the -- of the
24 sort of objection as to reliable principal -- principals and
25 methods.

1 So if the only objection is as to his offering
2 testimony about a particular labor specific things related
3 to the collective bargaining agreements then I think we can
4 probably release him to run to the airport, but if there's
5 something else that's broader as to his expert opinion on
6 the numbers and the data and the analysis by which he came
7 up with his conclusions as part of his retention for
8 McKinsey then I think we need to have that conversation now.

9 MS. KRIEGER: No, I don't see any objections to --

10 THE COURT: All right.

11 MS. KRIEGER: -- any of the methodology that he
12 explained in reaching those others, it's just connecting the
13 dots and saying this contract provision caused this
14 restriction or this inability --

15 THE COURT: Right.

16 MS. KRIEGER: -- that we can weed out I think
17 without impairing the overall --

18 THE COURT: All right. And basically there are
19 other witnesses who've been offered for that.

20 MR. POLLACK: And there will be further and I'm
21 happy the work with counsel to try --

22 THE COURT: All right.

23 MR. POLLACK: -- to come up with --

24 THE COURT: So I think somebody can tell him that
25 we can run to the airport, and what we will do is I will

1 admit all the testimony and the exhibits, subject to that
2 one issue being resolved, and there are many detriments to
3 having sort of a bifurcated trial here, but one of the
4 benefits is our ability to do things like this, and so we
5 might as well take advantage of it.

6 (Debtor's Exhibit Nos. 400 and 401-403 were admitted)

7 MR. POLLACK: Thank you, Judge.

8 MS. KRIEGER: Thank you, Your Honor.

9 THE COURT: Thank you. And thank you. I think
10 it's a very reasonable dividing line you've come up with
11 there. I think it's appropriate, and so.

12 All right, it is a quarter to 1:00. I know we
13 have Mr. Brundage on deck. Is there a hope that we'll start
14 a third witness today? I guess that --

15 MR. MOLLEN: There is, Your Honor, if we can get
16 through Mr. Brundage. Neal Mollen --

17 THE COURT: All right.

18 MR. MOLLEN: -- for the debtors, Your Honor.

19 THE COURT: All right. And then after
20 Mr. Brundage it sounds like Mr. Brundage was kind of a key
21 witness in terms of understanding the need at this time for
22 this part of the case to delve into other witnesses, so we
23 won't have that conversation now, we'll have it after
24 Mr. Brundage. And so let's come back at 2 o'clock.

25 MS. KRIEGER: Thank you.

1 THE COURT: Thank you.

2 MR. POLLACK: Thank you, Your Honor.

3 MS. PARCELLI: Thank you.

4 THE COURT: Oh, I have somebody's deposition
5 transcript here, so let me return it since it's not
6 evidence.

7 (Recess at 12:46 p.m.)

8 THE CLERK: All rise.

9 THE COURT: Good afternoon.

10 MR. MOLLEN: Good afternoon, Your Honor.

11 THE COURT: Please be seated.

12 MR. CLAYMAN: Good afternoon, Your Honor.

13 MR. MOLLEN: Your Honor --

14 THE COURT: Proceed, Counsel.

15 MR. MOLLEN: Thank you, Your Honor. Neal Mollen
16 of Paul Hastings for the debtors. We would like to call
17 Jeffrey Brundage to the stand.

18 THE CLERK: Please raise your right hand.

19 (Witness Sworn)

20 THE CLERK: Please state and spell your name for
21 the record.

22 THE WITNESS: Jeffrey J. Brundage, J-E-F-F-R-E-Y
23 J. B-R-U-N-D-A-G-E.

24 THE COURT: Good afternoon.

25 THE WITNESS: Good afternoon, Your Honor.

1 DIRECT EXAMINATION

2 BY MR. MOLLEN:

3 Q Mr. Brundage, can you give us the current position you
4 have at -- hold at American Airlines?

5 A I'm currently the senior vice-president of human
6 resources.

7 Q And how long have you been in that position?

8 A Since March of '04.

9 Q Okay. How long have you been with American Airlines?

10 A Since December of 1999.

11 Q And what did you do before you came to the company?

12 A Immediately prior to coming to American I worked for
13 the Airline Pilots Association, and prior to that flew as a
14 line pilot and held a number of political offices at the --
15 at ALPA.

16 Q This may be the first time we've mentioned ALPA or the
17 Airline Pilots Association in this proceeding. Can you tell
18 us who they are?

19 A Yeah. They -- it's an organization that represents
20 approximately fifty airlines in the U.S. and Canada, pilot
21 organizations, but they are not the representative, as you
22 know, of -- of pilots at American.

23 Q So they are collective bargaining representatives for
24 pilots at other airlines?

25 A Correct.

1 Q Okay. And when you were at ALPA what did you do? What
2 was your job?

3 A Well, while I was a line pilot I held a whole host of
4 different political offices: Negotiating committee chairman,
5 merger committee chairman a couple of times. I was the
6 master executive council chairman, and then I moved on to
7 hold some roles at the national organization working for the
8 president of ALPA, and then eventually resigned my seniority
9 number and moved into the representation department at ALPA
10 where I was a senior collective bargaining coordinator
11 dealing with collective bargaining agreements at a whole
12 host of carriers in Canada and the U.S.

13 Q And you were involved in collective bargaining with the
14 -- when you were at ALPA engaging -- bargaining for those
15 agreements?

16 A That's correct.

17 Q Okay. Now when you started in your current position in
18 human resources in 2004, how many employees were in your
19 department?

20 A The H.R. department at American had approximately 600
21 employees at the time that I started.

22 Q How many are there today?

23 A We entered into a business process outsourcing
24 agreement around 2005 in an effort to reduce our costs and
25 we entered into this agreement with IBM and reduced our

1 headcount from 600 to about 300.

2 Q And where did those 300 jobs go geographically?

3 A A number of them are in Manila in the Philippines in a
4 call center there, and the balance are in Dallas, Texas.

5 Q It might be helpful to the Court if we begin with a
6 description of your duties in your current position as
7 senior VP of human resources.

8 A I have responsibility for all of the traditional human
9 resource functions, including leadership diversity, the
10 corporate HR functions, compensation, collective bargaining
11 and, also, collective bargaining in Mexico, Central America,
12 Latin America and the Caribbean.

13 Q Now did you have a role in the collective bargaining
14 that the company engaged in prior to the filing of the
15 Chapter 11 petition in this case?

16 A Primarily, my role was an oversight role, but for a
17 short period of time I engaged directly in bargaining at the
18 pilot table.

19 Q Now, Mr. Brundage, you and I share a fatal
20 characteristic. We both talk way too fast. So I'm going to
21 ask you for the sake of the court reporter to slow it down a
22 little, and I promise I'm going to try as well.

23 A Okay.

24 Q Okay. You should have a notebook in front of you, Mr.
25 Brundage. Do you see that?

1 A I do.

2 Q And in that notebook you should see the declaration
3 that was filed on your behalf on March the 27th in this
4 case. Do you see that?

5 A Yes, I do.

6 Q Okay. And there should also be copies of all the
7 exhibits that you authenticated in your declaration. Do you
8 see those?

9 A Yes, sir.

10 Q Okay. Do you adopt the declaration and exhibits as
11 your direct testimony in this case?

12 A I do.

13 Q Okay.

14 THE COURT: Counsel, I just want to make sure I
15 have this correct. I think you said filed on March 27th.

16 MR. MOLLEN: Yes, Your Honor. They --

17 THE COURT: All right. The one I have is dated,
18 though, executed as March 26th at 4:55, just --

19 MR. MOLLEN: Yes.

20 THE COURT: -- to make sure we're all talking
21 about the same document.

22 MR. MOLLEN: It's the same document.

23 THE COURT: Right.

24 MR. MOLLEN: It was filed with the Court on the
25 27th with the rest of the 1113 papers.

1 THE COURT: All right. Just given that there have
2 been revised and supplemental declarations. I just wanted to
3 make the record clear.

4 MR. MOLLEN: Knock on wood, Your Honor.

5 THE COURT: Thank you.

6 MR. MOLLEN: We haven't had the opportunity or
7 need to update or correct Mr. Brundage's. I hope that
8 doesn't come.

9 THE COURT: All right.

10 MR. MOLLEN: Okay. Yeah. That -- that would be
11 -- Mr. Brundage's declaration is Exhibit 500 and then his
12 exhibits are 501 through 509.

13 BY MR. MOLLEN:

14 Q Mr. Brundage, maybe a good place for us to start this
15 afternoon is to update the Court on what's happened since
16 the March 27th filing at each of the labor groups. So why
17 don't we start with the TWU. Now we've deferred much of the
18 TWU case, but there's been references to what's happened. I
19 don't think there's been any testimony, any evidence about
20 that. So why don't you just briefly tell us what's happened
21 there.

22 MS. LEVINE: Your Honor --

23 THE COURT: Yes.

24 MS. LEVINE: -- from what I remember those -- this
25 discussion wasn't going to take place on the record and now

1 we're moving to reserve all of this for --

2 MR. MOLLEN: Honestly, Your Honor, we weren't
3 intending to do anything controversial other than to simply
4 say --

5 MS. LEVINE: Well, you've said TWU. It caused me
6 to stand.

7 THE COURT: Well, I --

8 (Laughter)

9 MR. MOLLEN: Maybe if I -- maybe if I withdraw the
10 question I can cause counsel to sit back down and I --

11 THE COURT: Right.

12 MR. MOLLEN: -- you know, step on any ways.

13 THE COURT: Well, I am at the distinct
14 disadvantage and, perhaps, advantage as it may turn out of
15 not knowing what that conversation was and what the
16 agreement is. So, perhaps, you want to take thirty seconds
17 and chat with each other.

18 (Pause)

19 MR. MOLLEN: Your Honor, I'm going to withdraw the
20 question.

21 THE COURT: All right. Fair enough.

22 BY MR. MOLLEN:

23 Q Mr. Brundage, perhaps it would be best if we start with
24 the pilots.

25 (Laughter)

1 A In my -- in my position as -- as SVP of HR, I have
2 oversight, as I said earlier, for all of the collective
3 bargaining. And Ms. Denise Lynn, who is the VP of -- of
4 employee relations works directly for me. And so on a
5 regular basis I participate in telephone conferences,
6 usually about twice a day, to understand issues around the
7 bargaining so I draw on those conferences to -- to explain
8 what I know about the bargaining at this point.

9 We have had a number of bargaining sessions with
10 the pilots. We've made considerable progress in a couple of
11 areas, for instance, pensions. The pilots have worked very
12 hard with us to find -- work towards solutions in the area
13 of pensions. I can't say that we've made as much progress
14 when it comes to valuing some of the proposals and other
15 things, but there has been quite a bit of work performed.
16 But we have not been at a point where we've been able to
17 reach what I would describe as an agreement.

18 MR. JAMES: Your Honor, may I raise a question?
19 If you're getting into filing bargaining, that's beyond --
20 this declaration was signed before you filed. It's beyond
21 the scope of the --

22 THE COURT: Well, the --

23 MR. JAMES: They're talking about --

24 THE COURT: -- the declaration is not post -- I
25 mean, the declaration is -- is in March, so --

1 MR. JAMES: It's before they filed a motion.

2 MR. MOLLEN: If I understand the nub of this
3 dispute, Your Honor, it's what we discussed yesterday as --
4 in terms of which the -- which proposal is operative for
5 Your Honor's --

6 THE COURT: All right.

7 MR. MOLLEN: -- consideration. And I think we've
8 decided to post-pone the legal argument. We're going to
9 file papers with you next week on that.

10 THE COURT: Well -- well, here's what we're going
11 to do.

12 Mr. Brundage, I know you just took the stand, but
13 I -- I suspect that it is unavoidable that we need to have a
14 -- a very exciting legal discussion. So what I would ask is
15 that you -- you go out, stretch your legs in the hallway,
16 and we're going to have a little chat about and try to set
17 the framework for discussions with you.

18 MR. JAMES: Your Honor, before we get into that, I
19 think there was -- there was an issue about the case
20 management order about his going beyond what he's presented
21 --

22 THE COURT: Well, let's -- let's take one at a
23 time. We've --

24 MR. JAMES: Okay.

25 THE COURT: You know --

1 UNIDENTIFIED SPEAKER: This is assumptive.

2 MS. KRIEGER: This is -- this is the simplest
3 issue.

4 THE COURT: All right. Well -- so let me ask for
5 a very generalized proffer of what you intend to cover with
6 this witness in terms of the status of negotiations and why
7 that's what you intend to cover, and then I'll hear from --
8 from the unions as to -- as to whether that -- they think
9 that's a good idea or somehow a problem.

10 MR. MOLLEN: At -- at this point in time all I
11 intended to do was have the witness authenticate the most
12 recent term sheet that contains the proposals made to the
13 APA last week. That's all.

14 Now it's true that we're going to have testimony
15 about the proposals the company has made and the response
16 that they've heard at the bargaining table from APA and from
17 APFA, and I'm not sure that all of those questions will have
18 answers that are exclusively dated to prior to March 27th.

19 THE COURT: All right. Well, what's the --

20 MR. MOLLEN: But my --

21 THE COURT: -- what's the relevance of the term
22 sheets that were offered last week for -- for my 1113
23 inquiry? Obviously, they're relevant to a lot of people for
24 a lot of reasons that don't have to do necessarily with what
25 I have in front of me.

1 MR. MOLLEN: The statute says, Your Honor, that
2 it's the set a proposals that matter. It says that the
3 Court is -- shall reject the contract and shall grant the
4 motion if the debtor shows that prior to the beginning of
5 the hearing the debtor has made a proposal that meets the
6 series of requirements that the statute sets forth.

7 This is the point on which, I think, yesterday
8 there was a colloquy. We actually have like a three or
9 four-page bench brief on that question.

10 THE COURT: All right.

11 MR. MOLLEN: But I -- I had been under the
12 impression that an agreement had been reached among counsel
13 that we would file those the beginning of the week to give
14 the APA time --

15 THE COURT: All right.

16 MR. MOLLEN: -- to draft --

17 THE COURT: Well, the concern is, obviously -- and
18 I would have been happy to do that. But if it -- it's going
19 to come up right here and now as to what we should be
20 talking about with the witness it may be unavoidable to chat
21 about it now. So --

22 MR. MOLLEN: Okay.

23 THE COURT: Now correct me if I'm wrong. It may
24 be that there's -- let me ask the unions whether this is
25 something that we have to get into in -- in detail now. But

1 I did hear an objection and -- and I read the body language
2 to essentially say there were going to be more coming in
3 terms of talking about what's currently in the current were
4 the most recent discussions.

5 MS. KRIEGER: Okay. Your Honor, I guess the first
6 issue that surprised us is that our understanding of the way
7 this was to proceed is that the direct examination testimony
8 was to present -- be presented in writing and then today's
9 proceedings are only a summary of the direct testimony,
10 which has previously been submitted in writing. And that
11 was just a function of the generic case management order for
12 running contested proceedings and evidentiary trials during
13 this bankruptcy proceeding.

14 So it -- it's something of a surprise to then have
15 the testimony here at trial today be about events that post-
16 dated the written testimony that --

17 THE COURT: Well --

18 MS. KRIEGER: -- was presented pursuant to the --

19 THE COURT: Well, let me --

20 MS. KRIEGER: -- case management order. So that
21 was the first --

22 THE COURT: All right. Let -- well, let me ask a
23 question that's not related to -- it's not rooted in 1113,
24 but general trial principles.

25 Have you opened the door by asking various

1 witnesses are they aware that the union has agreed to do
2 this and the union has agreed to do that and the union has
3 agreed to do the other thing. So, I mean, that's -- I've
4 heard that asked of many witnesses. And when we were going
5 to have our discussion about what was -- what is the
6 relevant agreement and what's the relevant state of play, I
7 was aware that those questions had been asked.

8 MS. KRIEGER: Okay. And the second piece of the
9 issue, as you focused on, does have to do with the structure
10 of 1113. And in that case, yes, I would refer Your Honor to
11 the case -- the Teamsters' Airline Division v. Frontier
12 Airlines, which is reported at 51 Bankruptcy Court Decisions
13 247, and it's a Southern District of New York decision from
14 2009. And it lays out, very carefully, the relevance of
15 proposals made before the filing and then conduct that
16 occurs after the filing and prior to the hearing.

17 And so, just without getting into a detailed bench
18 brief -- I'm sure we'll address it in our filings, the
19 relevance. But, briefly. The Court -- the Southern
20 District explained that what -- the -- a compliant
21 proposals; that is, a proposal that meets certain criteria
22 of 1113(b)(1)(a), but it has to be based on the most
23 accurate, available information and it has to meet the
24 necessity test, must be made before the motion to reject is
25 filed. So, technically speaking, the proposal that's

1 evaluated for at least those two factors, two of the factors
2 that must be passed --

3 THE COURT: Is before the --

4 MS. KRIEGER: -- is the last proposal that was
5 filed before the March 27 application here. But they're
6 different --

7 THE COURT: But then why was -- why was the
8 question being asked about --

9 MS. KRIEGER: Yeah. And then subsequent to the
10 filing of the proposal, there are further duties on the
11 parties, including the duty of the debtor to bargain in good
12 faith, to provide information, and in -- in an attempt to
13 reach a voluntary agreement. And so for certain purposes,
14 Mr. Mollen is correct that the conduct by the debtor to
15 comply with those additional requirements will be relevant
16 for certain purposes, including --

17 THE COURT: Right. All right.

18 MS. KRIEGER: -- the union -- including responses
19 by the union and whether the union has good cause to reject.

20 But at the end of the day, if a voluntary
21 agreement is not reached, what you snap back to for
22 evaluating certain key legal criteria and sufficiency is the
23 proposal that was filed --

24 THE COURT: All right.

25 MS. KRIEGER: -- before the application.

1 THE COURT: But let -- let me ask the -- one more
2 question, then I -- I know you want to respond to that.

3 But if that's the case, all we're talking about is
4 the differing reasons why certain testimony is being offered
5 in terms of relevance, which is different than saying that
6 you have an objection to talking about it. It's rather that
7 you want me to understand what they're being offered for.
8 So my question is, is there going to be any objection to --
9 there seemed to be an objection to a line of questioning
10 being discussed at all, and maybe I misread it, but --

11 MS. KRIEGER: Can -- can we have a minute and --

12 THE COURT: Sure.

13 (Pause)

14 MS. KRIEGER: Your Honor, I think it will depend
15 on the nature of the testimony, but the gist of it, as I
16 say, goes back to the first issue we raised, which is the
17 case management order; that what we understood to be at
18 issue here in the proceeding was not free-wheeling testimony
19 that goes beyond the written declarations. The company does
20 have a rebuttal case after our presentation of the case.
21 And the union does not believe that it opened the door
22 merely by asking an expert who professed an opinion whether
23 or not he or she had seen a certain union -- the terms --

24 THE COURT: Well --

25 MS. KRIEGER: -- of a certain union proposal.

1 THE COURT: -- I don't know that I want to parse
2 it that finally.

3 MS. KRIEGER: Yeah.

4 THE COURT: But if people are being asked about
5 time periods -- and I did go through this. I don't have my
6 notes with me, but I did go through this the other evening
7 just to get a sense of -- of how to lay this out, and I do
8 -- I do have some views about what's relevant for what
9 purposes.

10 But before I get into that, let me hear from the
11 debtors.

12 MR. MOLLEN: Okay, Your Honor.

13 First of all, I believe the statute and, in fact,
14 Frontier Airlines speak directly to our position on the
15 point rather than the position just outlined. And I do have
16 the bench brief, which I would be happy to hand up. It's
17 got the language of the statute in it. It might be of some
18 guidance to the Court.

19 THE COURT: Well, I'll -- I was going to wait
20 until next week, but I'll take it now and then people can
21 either --

22 MR. MOLLEN: Yeah. I --

23 THE COURT: -- present -- the other side can
24 present something to me written or argue the point. I've
25 certainly preserved your rights to say whatever you need to

1 say. But it -- it seems that if we're talking about what
2 the scope of testimony is, I have no choice but to have some
3 of these discussions now, which I -- I didn't think we were
4 headed down this road, I confess.

5 MR. MOLLEN: So -- are the -- I'm sorry, Your
6 Honor. I didn't hear you.

7 THE COURT: No. Go ahead.

8 MR. MOLLEN: So -- so, first of all, I think, you
9 know, in the legal position that the language of the statute
10 resolves the question and it resolves it on our favor.

11 But in the second point --

12 THE COURT: But what -- what -- what is your
13 position precisely?

14 MR. MOLLEN: That -- that the proposal that
15 matters -- they all matter, but the key proposal that Your
16 Honor must consider for 1113 purposes is the proposal that's
17 on the table prior to the start of the hearing --

18 THE COURT: All right. Well, I think --

19 MR. MOLLEN: -- rather than--

20 THE COURT: -- I think we're all on the same page,
21 then. All right.

22 MR. MOLLEN: No

23 THE COURT: Prior to the start of the hearing.

24 MR. MOLLEN: The hearing, Your Honor, not on the

25 --

1 THE COURT: Okay. Not prior to the --

2 MR. MOLLEN: -- date of the motion.

3 THE COURT: -- application.

4 MR. MOLLEN: And, Your Honor, if you think about
5 it it really couldn't be any different. It couldn't be
6 structured any different way because the statute requires
7 after the initial proposal, that the debtor engage in
8 negotiations in good faith. It would be passing strange for
9 the statute to require bargaining in good faith by the
10 debtor and then say that the product of that negotiations
11 was utterly irrelevant.

12 Assume, Your Honor, a situation in which the
13 initial proposal made by the debtor was mistaken in some
14 respect, was not based on the most reliable evidence, was
15 overreaching in some regard. The employer and the union
16 met. The union pointed out the errors in the analysis. The
17 employer said, you're right. We're making changes to the
18 proposal in order to reflect your position on that; change
19 the composition of the ask to the union. The position, I
20 understand, the union is to be taking is that's utterly
21 irrelevant and the fact that the employer has modified its
22 position in good faith negotiations is utterly irrelevant
23 under the statute to whether 1113 has been satisfied. It's
24 a --

25 THE COURT: All right. But --

1 MR. MOLLEN: -- awfully odd structure.

2 THE COURT: -- but then it seems that the intent
3 is to offer testimony today that is a supplement to this
4 even though I don't have a supplement to this. I have
5 something that's March 26th, filed the 27th.

6 MR. MOLLEN: Right. So --

7 THE COURT: SO they don't have any notice as to
8 what your direct --

9 MR. MOLLEN: Right.

10 THE COURT: -- is going to be on these --

11 MR. MOLLEN: That's --

12 THE COURT: -- topic.

13 MR. MOLLEN: Right. Your Honor, that's the third
14 piece. There's no question that the Court's local rules and
15 that the scheduling order entered in this case contemplated
16 that the debtors' direct case would be put in on paper and
17 that that would be the operative set of documents. But no
18 matter how diligent the debtor is, Your Honor, there's no
19 way that the papers could reflect activity that occurs after
20 the papers have been filed.

21 THE COURT: But -- but I have seen quite a few
22 supplemental declarations, second supplemental declarations,
23 amended declarations, and -- for plenty of witnesses. I
24 forget the last that I've seen of those and I know, perhaps,
25 it can't be in real time.

1 What is the date of the proposal that you want to
2 discuss?

3 MR. MOLLEN: It was first passed on the 17th, the
4 ATA proposal. There as an error in the term sheet, was
5 correct, and so the document that we're actually having --
6 seeking to have MR. Brundage authenticate was from April
7 19th.

8 THE COURT: All right. And that's --

9 MR. MOLLEN: And finally, Your Honor --

10 THE COURT: -- Thursday, if I might -- if I my
11 calendar --

12 MR. MOLLEN: I believe that's right.

13 THE COURT: -- is correct.

14 MR. MOLLEN: I think that's right, Your Honor.

15 And the final point, Your Honor, is if I
16 understood, even under the union's interpretation of the
17 statute, evidence of the post-filing conduct of the debtor
18 can come in to show that the employer has engaged in good
19 faith bargaining.

20 THE COURT: Right.

21 MR. MOLLEN: And to the extent --

22 THE COURT: Well --

23 MR. MOLLEN: -- that the more recent --

24 THE COURT: But it does beg the question as to why
25 -- that hasn't been supplemented so that we can all -- what

1 -- deal with it with the best information available.

2 Let me ask when this witness was deposed.

3 MR. MOLLEN: This witness was not deposed, Your
4 Honor. The agreement --

5 THE COURT: Was not deposed.

6 MR. MOLLEN: -- of the parties was that only the
7 experts would be deposed.

8 Your Honor, if -- I -- honestly, I didn't expect
9 or desire to pick this particular fight right now. There's
10 no reason why we can't do this in our rebuttal case. We can
11 talk with union counsel about the scope, the narrow scope
12 that we intend to introduce on this score.

13 THE COURT: All right. Well, I think we can find
14 a practical way to do this. I would think for purposes of
15 the unions -- I understand that it's difficult to ask
16 questions about something that -- and you don't know what
17 the testimony is going to be. But I ask you whether it
18 isn't more helpful for purposes of preparing your own case
19 to know what that testimony is, at least in some bare bones
20 way. And, certainly, if it reflects term sheet that
21 everybody knows about and you reserve all your rights.

22 We could do it in the rebuttal case, but I'm just
23 -- I'm wondering if that isn't some form over substance.
24 But I'll -- I'll leave it to you to tell me whether you
25 think it's a prejudicial to you here.

1 MS. KRIEGER: Yeah. I -- I do think it is
2 somewhat, Your Honor. We -- we saw last week, as you are
3 aware, on a rolling basis including up to the eve before
4 depositions of experts, continual updating of even minor
5 details in expert declarations.

6 And so if this were just a correction of a typo or
7 something of that nature --

8 THE COURT: No. No. I understand your point.

9 MS. KRIEGER: Yeah. But --

10 THE COURT: This is --

11 MS. KRIEGER: -- but this is a major --

12 THE COURT: -- this is an area that you didn't --

13 MS. KRIEGER: -- this is a major new piece of
14 evidence that we would be happy to see an amended
15 supplemented declaration. We could then address it in our
16 case and the debtors' can address the substance of it in
17 their rebuttal case.

18 THE COURT: Although, I guess my -- my point is,
19 if -- if, unlike experts where you're talking about new
20 opinions on new issues, if it's just simply to put in the
21 record, which can be done now or later, what everybody
22 already knows, which is where's what the term sheet is and
23 it's -- it's clear that it's relevant for -- that's relevant
24 for some purposes. You may say it's relevant only for the
25 part of it that deals with good faith negotiations. You may

1 say, no. It's actually -- this is the agreement that I
2 should look at.

3 But, again, I'm wondering if it -- it isn't
4 prudent to just, in a bare bones way, while the witness is
5 here to just sketch out these -- these terms, and it is what
6 it is and you certainly reserve your rights.

7 MR. JAMES: Can we have about a minute to confer
8 internally and with Mr. Mollen?

9 THE COURT: Sure. Absolutely,
10 Again, I -- I understand -- counsel, if you could
11 stop for a second. I'm going to -- I'm going -- I'll leave
12 the bench and you can chat.

13 But -- but what -- I understand the concern about
14 prejudice and you don't know what the testimony is. But I
15 -- I also -- I seem to be getting the hint that it's simply
16 to get into the record what the terms are.

17 MS. KRIEGER: And we'll have a moment discussion
18 and if it narrows --

19 THE COURT: Yeah. So --

20 MS. KRIEGER: -- it down.

21 THE COURT: -- so figure it out. I --

22 MS. KRIEGER: We would be happy to - -

23 THE COURT: -- I understand the position, but I'm
24 just trying to -- I think we can probably find a practical
25 way to do this without anyone feeling like they're --

1 they're getting sandbagged and I don't think that was the
2 intent here.

3 So I'm going to wander off the bench, and what I
4 would ask is when you have your discussions just send
5 somebody in to come get me when -- when -- because I don't
6 know how -- whether this is going to take two minutes or ten
7 minutes, so -- and I don't want to rush you.

8 MR. JAMES: It's going to take two. Thank you.

9 THE COURT: All right. Thank you.

10 (Recess at 2:33 p.m.)

11 THE CLERK: All rise.

12 THE COURT: All right. Please be seated.

13 MR. MOLLEN: I think we've reached an accord, Your
14 Honor. We're just going to deal with it on rebuttal. The
15 --

16 THE COURT: All right.

17 MR. MOLLEN: -- the really critical change to the
18 term sheet actually came in as an APA exhibit anyway. So
19 we're just going to move on.

20 THE COURT: All right.

21 Well, here's -- just to sort of complete the loop
22 on this. I do have the debtors' papers on this. I think
23 you can submit something on the same schedule as you earlier
24 contemplated. I'm not making any rulings now. I'm taking
25 the evidence. It's clear that there's a view that various

1 proposals back and forth are relevant for different
2 purposes, but nobody is standing up to say that this is
3 irrelevant and prejudicial, keep it out. But you're going
4 to do it in the rebuttal case and that's that.

5 So aren't you glad you missed that discussion.

6 MS. KRIEGER: Thank you, Your Honor.

7 MR. MOLLEN: Thank you.

8 MS. KRIEGER: And we'll address it, I think, in
9 our formal filings on the schedule that we're due to file
10 them because --

11 THE COURT: That's -- that's fine as well.

12 MS. KRIEGER: - they'll address all the elements.

13 Thank you.

14 DIRECT EXAMINATION (Resumed)

15 BY MR. MOLLEN:

16 Q Mr. Brundage, now that we've gotten the housekeeping,
17 uncontroversial aspect of your testimony taken care of, let
18 me ask you to focus your attention on the prepetition period
19 of bargaining with the unions. You were involved in that,
20 were you not?

21 A I was directly involved with the pilot negotiations.

22 Q Okay. And as a matter of supervision at the other
23 tables?

24 A That's correct.

25 Q Okay. Again, we're on -- we're restricting your

1 testimony today to the APA and the APFA.

2 A Correct.

3 Q Okay. When did bargaining begin for each of those two
4 groups?

5 A In 2006 we exercised an early opening provision that
6 existed in the 2003 agreement with the pilots and began
7 bargaining at that time, and then the contracts became
8 amendable and we began bargaining with the APFA in 2008.

9 Q Okay. From whom did you receive your instructions with
10 respect to the goals of the bargaining?

11 A I reported directly to the CEO and the CEO gave me my
12 instructions.

13 Q And -- and what were those instructions?

14 A Mr. Arpi was very public and very clear about his
15 aversion to bankruptcy and he was quoted in numerous
16 different publications as saying that he didn't believe that
17 bankruptcy was a financial reengineering tool. He believed
18 it was what you do when you're at your last resort. And, on
19 the other hand, he believed that we absolutely needed to do
20 our very best to gain agreements with our employees, our
21 unionized employees so that we could try to meet the goals
22 of the company and move the company forward.

23 And so I would say in a nutshell the assignment
24 that I was given and my team was given was to do our very
25 best to reach accommodations with the unions that would help

1 to move the company forward and allow us to avoid being in
2 this court.

3 Q What were the specific goals that you attempted to
4 achieve when -- in these two agreements; that is, what were
5 the kinds of changes you sought to make to the agreement sin
6 order to move the company forward?

7 A Well, I need to go back to our 2003 agreements because
8 they were really the foundation for moving forward. And in
9 2003, the changes that we made at that time were primarily
10 in the area of wages. The company was in a position where
11 we were very short on cash and we were coming up against the
12 necessity to file. And, obviously, if you make adjustments
13 to wages you very quickly can preserve cash.

14 So we focused on those kinds of items that would
15 allow us to preserve as much cash as possible, as quickly as
16 possible. As a result, we didn't touch a lot of the big
17 productivity items, benefit items, those kinds of things in
18 the way that, with 20/20 hindsight, our competitors did
19 later on in the couple of years following.

20 So as we thought about what the next generation of
21 contracts needed to look like, we were very focused on
22 making sustainable changes in areas like productivity,
23 changes that would endure and allow us to compete over the
24 long-term.

25 In addition to that, we recognize that our benefit

1 structure, both active medical benefits, retiree medical
2 benefits and pensions were very much out of step with the
3 industry and, in some cases, with general industry as a
4 result of the path that we took to get there.

5 Q Okay. So those were the sorts of changes that you
6 thought about trying to implement through the bargaining in
7 2006 and 2008?

8 A And -- and I would add one more. In -- in certain
9 agreements there were impediments to business. And in each
10 of those cases we focused on attempting to relax or remove
11 those impediments to doing business.

12 Q Can you be a little more specific when you say
13 "impediments"?

14 A Well, I -- I think the obvious one that's been
15 discussed here at length is scope with the pilots and our
16 ability to expand our use of regional jets and our ability
17 to code-share much more broadly.

18 Q Now during this proceeding and in the documents that we
19 produced in this case there's lot of talk about the limp-
20 along strategy or convergence. Can you tell me what those
21 two terms meant to you in terms of your approach to
22 bargaining?

23 A I think a little explanation might be in order first.
24 The -- it's been described here as an interminable process,
25 the Section 6 process under the RLA. And the reality is

1 that even in mediation the board primarily has the power of
2 the calendar to choose to schedule meetings or not.

3 But there really isn't a binding dispute
4 resolution protocol until you get to the end of that process
5 and the board decides that further mediation is unlikely to
6 produce an agreement and they choose to proffer arbitration,
7 and they release the parties into a cooling off period. And
8 at the conclusion of that the company has the ability to
9 implement its proposals and the union has the ability to
10 strike.

11 In today's world and during the last decade I
12 can't imagine there's any airline that believed it could
13 sustain the incredible costs and book away and other
14 challenges associated with a strike. So the reality is we
15 didn't believe we had a real dispute resolution mechanism,
16 and as a result of that, we were really being governed by
17 what we -- how we believed we could push to make some of the
18 changes that I described earlier and have them ratified.

19 And so we -- we -- we were really governed by the
20 art of what we thought the possible was. We were not
21 governed by what we believed to be necessary. We -- we
22 never, I would say, made proposals that we ever believed
23 would get us all the way to being a successful enterprise.
24 We made proposals that we thought would allow us to
25 hopefully be in a position that if, for a change, we got a

1 little tailwind instead of headwind, that we could take
2 advantage, capitalize on that tailwind and move the company
3 into a position where it could become more profitable.

4 And that's where the term "limp along" came from.
5 I mean, it was a -- it was the -- two things we used. One
6 was kick the can and the other was limp along, so not very
7 dramatic, very brilliant strategies for success, but
8 strategies that we employed to hopefully put ourselves in a
9 position to meet those two goals that I described earlier:
10 Be in a position to keep the company moving forward and
11 avoid bankruptcy.

12 Q So part of this process was to project where the labor
13 agreements of your competitors would end up in years in the
14 future?

15 A Yeah. That's the convergence portion. And we were --
16 we were of the mind that there were two things that would
17 affect our cost structure. The first were those things that
18 we could control, and they were the proposals that we were
19 making in bargaining, the changes that we wanted to make to
20 productivity, the changes we wanted to make to benefits, the
21 changes we wanted to make to scope. So I -- that was the
22 active part that we could take.

23 But at the same time, we, in hindsight, improperly
24 relied on what I would describe as the history of the
25 industry. I started in the mid 80s and it -- typically, you

1 had cycles of four, six, maybe as long as eight years where
2 the economy would improve and then you would have economic
3 challenges. And just depending on where you were in the
4 negotiating cycle you either got an agreement that was a
5 rich agreement from the employee's perspective or, if you
6 happened to be stuck at the bottom of the trough, you got a
7 -- you got a concessionary agreement.

8 And almost two, three years later because of the
9 cycles and over the length of the agreement, chances were
10 you would get it all back and you would move on to the next
11 -- to the next cycle. And if you were really lucky you
12 would hit it at the top and if you were really unlucky you
13 did a couple of agreements in the trough.

14 So our -- our notion was that our competitors were
15 in a position where they had a lot of things coming at them.
16 Their agreements from bankruptcy were -- were becoming
17 amendable. There were a number of mergers on the horizon
18 which traditionally have resulted in significantly increased
19 employee costs. The effects bargaining that takes place to
20 get a merger done usually results in improvements in a whole
21 host of areas in a contract.

22 And so it --

23 Q When you say "improvements," you're talking about more
24 -- more expense, more cost to the company?

25 A Improvements from the employee's perspective.

1 Q Right. Okay. And so -- if I might interrupt here, it
2 -- now in hindsight if you look back on the convergent
3 strategy that the company adopted, how would you
4 characterize your ability to project into the future and see
5 what those terms might be for your competitors?

6 A Well, the benefit of hindsight is pretty clear and we
7 were pretty long. You know, we weren't able to predict
8 where it was going.

9 Q In 2006 when you opened the pilot agreement for
10 negotiations and then in 2008 with the APFA, was it your
11 estimation at that time that you would be sitting here in
12 2012 without agreements?

13 A Never would have predicted that then.

14 Q Now regarding this convergent strategy or world view,
15 would you say that there was consensus or internal debate
16 about that prospect or that strategy, pursuing it to the --
17 at the table?

18 A I think -- it was identical to what I would describe as
19 any good management team. We had debates almost weekly at
20 our executive committee meetings about what the right thing
21 to do was and throughout those meetings different people
22 took different sides of issues from week to week because it
23 was very sub -- you know, it was subjected to what's
24 happening. Fuel prices increasing dramatically, are we
25 looking at, you know, another outbreak of SARS, do we think

1 the economy is going to improve or do we think the economy
2 is going to get worse.

3 And, you know, because you're -- we've proven that
4 we can't accurately predict that looking forward, we had a
5 lot of opinions. But in the end I would say that we had
6 been proven to have taken an overly optimistic view of what
7 was going to happen in terms of cost convergence.

8 Q One element of the process of negotiations prior to the
9 Chapter 11 petition in this case was this exercise of
10 applying the terms of one labor agreement at a competitor
11 airline onto the American Airlines system. Can you tell me
12 what the purpose of that exercise was?

13 A Well, I -- I was here for Mr. Glass's testimony and I
14 think he did a pretty good job of explaining that that's a
15 way that airlines tend to look at what their cost structure
16 looks like in comparison to their competitors.

17 But, typically, it had -- it had been a back
18 office kind of approach, and what I mean is we're pretty
19 good at understanding our own costs. We're not as good at
20 using the publicly available data to really understand our
21 competitors costs. And, obviously, as has been testified
22 to, cost control is one of the differences between success
23 and failure in this business.

24 So we did something called the performance
25 leadership initiative with all of our unions participating

1 in the middle of the last decade. And that was an exercise
2 where we hired some outside consultants and we literally
3 opened up every aspect of the company from the management
4 team through each of our unionized groups and, also, through
5 our independent employees and we really looked at our cost
6 structure to understand where we had challenges. And so
7 that was an internal look.

8 As a result of that we decided to begin to use
9 this tool that we had used previously as a kind of an
10 internal costing model as a way to, in fact, publicly
11 address the fact that we believed our contract, our contract
12 provisions were not competitive in the industry.

13 Q Was it an effort to capture the entirety of the gap
14 between you and the other airlines or to identify specific
15 aspect of the --

16 A No. Absolute -- that --

17 MR. CLAYMAN: Your Honor, I would like to object.
18 Again, I think we're -- we're kind of delving into an arena
19 or a piece of information here in testimony that is not
20 reflected anywhere in his declaration. There's no testimony
21 at all about the genesis of the convergence analysis.
22 There's no testimony at all about the PLI, the performance
23 leadership initiative. There's nothing about trying to
24 debunk, if that's the case here, if it's what he's trying to
25 do, the convergence analysis. There's nothing like that in

1 his -- in his declaration. If that was going to be
2 testimony here today we were entitled to -- to be able to
3 read it and be able to prepare for it.

4 MR. MOLLEN: Your Honor, I'm pretty sure the word
5 convergence appears multiple times in his declarations in
6 Paragraph 21, Page 12. It is thick in the -- in his
7 declaration. The purpose of --

8 THE COURT: All right. Well --

9 MR. MOLLEN: -- this testimony --

10 THE COURT: Well, refer me to the paragraphs and
11 I'll take a moment and --

12 MR. MOLLEN: Okay.

13 THE COURT: -- read them in the context of what
14 the last question and answer were. So you're saying I
15 should read Paragraph 21?

16 MR. MOLLEN: 20. I'm sorry, Your Honor. And 34
17 uses the term, but, really, the entire section from
18 Paragraph 29 through 36 is about the very issue that we're
19 discussing now.

20 THE COURT: All right. Just give me a moment.

21 (Pause)

22 MR. MOLLEN: And -- and if I may, I'm sorry, Your
23 Honor, Paragraph 19 deals precisely with the -- this little
24 gap identified, the six-hundred-million-dollar gap, six-
25 hundred to eight-hundred-million-dollar gap we're talking

1 about.

2 (Pause)

3 THE COURT: Is there a reference to the
4 performance leadership initiative anywhere?

5 MR. MOLLEN: I haven't asked the witness about
6 that.

7 MR. CLAYMAN: He just testified about it. I mean,
8 Your Honor's --

9 THE COURT: Well, I don't -- yeah. I don't -- and
10 for purposes of -- of this inquiry I don't know if it
11 matters whether it was the question or it was the testimony
12 because I think the objection is that the testimony here is
13 not essentially sort of a summing up of the direct that's
14 written. It's rather additional details. And so I don't
15 know if it matters whether you've asked for them or not.

16 MR. MOLLEN: Maybe -- maybe if I can direct the
17 witness to give me less expansive answers I can pull his
18 attention to the specific --

19 THE COURT: Well -- well, let --

20 MR. MOLLEN: -- information.

21 THE COURT: -- let me ask what is it, for purposes
22 of your direct in light of what I have here, that you really
23 need to cover --

24 MR. MOLLEN: What -- Your Honor, the purpose of
25 this line of inquiry, one of the principle things we heard

1 about in the opening statements by union counsel and one of
2 the things that we've heard about in their question is the
3 change of direction or the change of perspective between the
4 pre-filing, between the pre-Chapter 11 negotiations and what
5 happened after November the 29th. And what I'm asking the
6 witness to describe is how the company involved, why is it
7 that the --

8 THE COURT: No. I -- I understand that, but --

9 MR. MOLLEN: Right.

10 THE COURT: -- I think I'm asking a different
11 question. I'm sort of asking a process question, which is
12 if it's in his declaration, that's -- that's fine. And you
13 can point me to that and you can say, you heard a lot about
14 this. Look at this paragraph, look at that paragraph, or --
15 or you can just say we rest on our -- on our direct that's
16 been submitted.

17 But if -- if you're supplementing it, I think that
18 that's where the nature of the objection is, which is to say
19 that then they've got to deal with it on the fly.

20 Now this is a bit -- more than a bit artificial
21 because this is opening salve, one of many to come, but for
22 -- for -- that can work several ways, right? It can be, why
23 worry about it. It can also be, well, why do it now. Do it
24 in your rebuttal case.

25 So -- so if it's not in the direct -- because,

1 certainly, it would not be inconceivable that I would just
2 simply say, I don't need anything because I have the direct.
3 Let's move to cross. So I've been letting people give sort
4 of an overview because I think it's generally helpful to set
5 the stage for the cross. But -- but to the extent that it's
6 additional, it should -- it either should have been the
7 subject of a supplemental declaration or it should be in the
8 rebuttal case.

9 MR. MOLLEN: Your Honor, it was intended solely as
10 an overview. It was not intended to supplement or --

11 THE COURT: All right.

12 MR. MOLLEN: -- add new material. All of this
13 material --

14 THE COURT: No. That's fine. I know when you ask
15 a question you're going to get an answer and you may not
16 sort of -- and -- and he's answering the questions best he
17 can. But I guess what I'm wondering is if at this point,
18 just so we don't get bogged down in this particular inquiry,
19 why don't I just take the direct and then we move to cross,
20 and then if they open some doors on cross, well, I'm sure
21 you'll -- you'll leap into it and then you can always deal
22 with these things in your rebuttal case.

23 MR. MOLLEN: Well, we can certainly do that, Your
24 Honor. I think that in sum and substance everything that
25 I've asked Mr. Brundage since our last break has been

1 covered at some length in his declaration. There are a
2 couple of aspects that -- of a couple of lines of
3 questioning that I wanted to ask him --

4 THE COURT: All right.

5 MR. MOLLEN: -- based on testimony and questions
6 asked by counsel during this proceeding.

7 THE COURT: All right. But if it's -- if it's
8 going to be new stuff --

9 MR. MOLLEN: Okay.

10 THE COURT: -- that's where we'll run into the
11 issue. So, again, this is a bit artificial and, you know,
12 parties are usually allowed to sort of respond to trial
13 testimony as sort of an organic matter and we do the direct
14 testimony and sometimes people do supplement it. But since
15 there seems to be a dispute about what the agreement of the
16 parties is in terms of the scope, we can -- we can fix that
17 objection without doing any violence to the debtors' ability
18 to present their case.

19 MR. MOLLEN: Your Honor, I -- I certainly didn't
20 intend for this to become contentious. And if Your Honor's
21 direction is that --

22 THE COURT: No.

23 MR. MOLLEN: -- we should have Mr. Brundage stand
24 down --

25 THE COURT: If -- if it's new material, I think

1 we'll put a pin in it for right now, so I'll leave that to
2 your judgment. But -- but let's not get too bogged down on
3 this or Mr. Brundage will have a very exciting afternoon
4 listening to all of us argue and he actually won't say very
5 much. So that -- I don't think that's the way it's supposed
6 to work.

7 So --

8 MR. MOLLEN: I suppose my difficulty, Your Honor,
9 is I thought that I was summarizing and going over material
10 that was in his declaration and --

11 THE COURT: Well, your questions may have been
12 designed to elicit that, but, you know, testimony is --

13 MR. MOLLEN: Right, Your Honor.

14 THE COURT: -- I always think of direct testimony
15 as --

16 MR. MOLLEN: Okay.

17 THE COURT: -- as a conversation between two
18 people overheard by many, and you may ask a question and he
19 may just give you -- he's not -- he's not trying to connect
20 the dots with his declaration. He's just going to answer
21 it. I'm not certainly going to blame him for that. But it
22 does put these folks over here at a disadvantage.

23 MR. MOLLEN: Very well, Your Honor.

24 THE COURT: So let -- let's -- let's -- I would --
25 if you want to ask him questions to sort of set the stage I

1 would ask you to point him to his -- to his direct and we'll
2 take it from there. But we'll leave new stuff to another
3 day.

4 MR. CLAYMAN: Thank you, Your Honor.

5 THE COURT: Certainly.

6 BY MR. MOLLEN:

7 Q Mr. Brundage, this is going to be extraordinarily
8 brief. I would like -- I would like to draw your attention
9 to the change of the company's perspective between the pre-
10 filing negotiating position and the position the company
11 took in 1113 and tell me how that process --

12 THE COURT: All right.

13 MR. MOLLEN: -- worked.

14 THE COURT: Where are we referencing in the --

15 MR. MOLLEN: It is --

16 THE COURT: -- declaration.

17 MR. MOLLEN: -- the entirety of the section
18 starting on Page 17, Paragraph 29 through 36.

19 THE COURT: And, Mr. Brundage, I -- all this has
20 nothing to do with you. I actually have had the distinct
21 privilege of being a witness in something and it's much
22 harder to be a witness than it is to ask the questions. So
23 Paragraph 17 and --

24 MR. MOLLEN: No. No. Page 17 --

25 THE COURT: Page 17. Okay.

1 MR. MOLLEN: -- Paragraph 29 through 36.

2 THE COURT: All right. Just give me one second to
3 just --

4 MR. MOLLEN: Very well, Your Honor.

5 (Pause)

6 THE COURT: All right. Proceed.

7 BY MR. MOLLEN:

8 Q So, Mr. Brundage, we're looking for sort of a
9 description of how it is that the company's perspectives
10 changed prior to November 29th to the process of bargaining
11 in the Section 1113 environment.

12 A We -- we were directed by the CEO to do everything we
13 could to avoid bankruptcy through the consensual bargaining.

14 Q And that's -- that was prior to the filing of the
15 Chapter 11?

16 A Prior -- prior to the filing of the Chapter 11.

17 Q What were the goals the company set -- first of all,
18 who set the goals for the post-filing bargaining for you?

19 A The business plan set the goals for the post-filing
20 bargaining to the extent that we -- we needed the same kinds
21 of changes post-filing that we needed pre-filing. Our
22 benefit structure was still out of touch. Our -- our
23 productivity was still low. A whole host of those same
24 issues I described earlier.

25 Q Okay. And did you get directions from any individual

1 as to how to go about achieving those goals?

2 A Yes. As I said earlier, my direction came from the
3 CEO.

4 Q There's a different CEO post-filing, though, was it
5 not?

6 A That is correct.

7 Q Okay. When you compare the set of instructions that
8 you have that were operative in the pre-filing environment
9 to the set of instructions that you received in the Section
10 1113 environment, tell me how they changed?

11 A The pre-filing environment was you and your team use
12 your very best judgment to get as much as you can in these
13 critical areas so that we have an opportunity to avoid
14 bankruptcy and continue. So bankruptcy was the backstop.

15 Q Okay.

16 A Once the determination was to file, then it became,
17 what is absolute -- what is necessary for the successful
18 restructuring of the company and we -- we spent a lot of
19 time making sure we understood the standards and we
20 attempted to put proposals together that would meet the
21 standards and allow us to get there in terms of successfully
22 restructuring.

23 Q Were there any particular principles involved in
24 decided which proposals you would make, which portions of
25 the contract you changed?

1 A Yes. The -- our competitors had all taken relatively
2 large wage reductions early on in their bankruptcies and we
3 were in a somewhat different situation in that we filed with
4 a reasonable amount of liquidity and we didn't have DIP
5 financing, so there were no restraints -- constraints put on
6 us in terms of what we needed to do kind of day one.

7 So we -- we made the election that what we would
8 prefer to do would be preserve rates of pay to the greatest
9 degree possible and understanding that some of this would
10 come through an additional amount of work performed to the
11 degree that people's relative incomes could be preserved,
12 that would be a goal. It didn't -- weren't sure we could
13 accomplish it in its entirety. But it would be a goal.

14 And that left us in a situation that because it
15 was a -- a significant change that we had to look at every
16 other section of the contract. So the second thing we
17 looked at was benefits and we've talked a lot about the 1.25
18 billion that were the requirements from labor. Almost half
19 of that came in our proposals from changes to benefits.

20 So first it was to preserve rates of pay and W2
21 income to the greatest degree possible; second, it was to
22 make benefit changes so that our benefits would be in line
23 with the industry; third, it was to focus on productivity to
24 try to get levels of productivity that would allow us to be
25 competitive.

1 We also focused very much on anything that we
2 thought was a constraint to being successful in our
3 restructuring. And -- and we also looked at how we would
4 ensure there were some success sharing in the -- in the
5 agreements so that if the company met its business plan or
6 exceeded its business plan, our employees would participate
7 in first dollar profit-sharing.

8 Q Okay. Now did the decision to try to leave pay rates
9 alone to the extent possible have ramifications for the
10 number or kind of items you put on your term sheets?

11 A That -- of course it did because, you know, pay rates
12 are a relatively large lever. You move -- you may a ten or
13 a fifteen or even a twenty percent change in rates of pay
14 and you can achieve savings very, very quickly. But once
15 you get into these agreements -- and at least in my opinion
16 they're pretty complex -- you -- you start moving a lot of
17 pieces and when you start moving productivity pieces and
18 other pieces, it has -- it has implications for other parts
19 of the agreement. So you end up having to make a lot of
20 proposals to be able to try to get the savings.

21 Q Now one of the complaints that we've heard during this
22 trial and in the popular press from labor has been that the
23 company has taken a take or leave it approach at the table,
24 and you've addressed this at some length in your deposition.
25 But if you could briefly say what your reaction is to that

1 accusation.

2 A I think we have focused on being as flexible as we
3 possibly can. But as I understand and as our attorneys have
4 informed -- informed me, the standard for 1113 is what's
5 necessary. And it's also that it has to be fair and
6 equitable, and that we are not in the traditional Section 6
7 bargaining where you make a big ask assuming that you're
8 going to negotiation to some place in the middle that might
9 be acceptable.

10 We -- we started out and have remained steadfast
11 that we would only ask for what we believed to be necessary
12 to successfully restructure. We have made some pretty
13 significant changes along the way.

14 Q Can you list a couple of them for us?

15 A Sure. I think probably first and foremost the decision
16 in concert with the PBGC and the UCC to take a different
17 approach on pensions was a pretty significant change. Our
18 initial proposals had us at some point in this process
19 asking the Court to terminate the pension plans. We have
20 modified those proposals so that for all of our non-pilot
21 groups we have proposals that are to freeze the pension
22 plans.

23 For the pilot group we've modified the proposal
24 that if we're able to work with the PBGC and treasury, to
25 have what is a particularly thorny part of the pilot pension

1 plan fixed. We then would freeze that plan as well. We had
2 a little over \$4 billion in -- in unfunded liability on our
3 books as part of the plan. And we have elected to amend the
4 plan to deal with that \$4 billion differently.

5 Q Amend the business plan?

6 A The business plan to deal with that differently. A
7 couple of individual examples. We've -- we have not had --
8 we've had a number of meetings with the advisors for our
9 unions and a lot of discussion about the business plan.
10 Many of those meetings, which I participated in and I think
11 Bev Goulet -- Ms. Goulet talked about those meetings a
12 little bit, and we -- in some of those meetings we had a lot
13 of questions about the business plan, but questions about
14 whether the amount was sufficient, insufficient --

15 Q Before we get into -- I want to ask you about what
16 you've heard about the sort of bottom line for each labor
17 group, but were any changes made to the active medical
18 proposal?

19 A Yes. We had initially proposed, on February 1st, that
20 we would move to three plans with an average employee
21 contribution of about twenty-three percent, and a lot of
22 push back from the unions in -- in bargaining about the
23 level of that contribution. So we elected to separate the
24 plans and put what -- what I would call is a richer plan and
25 hold it out separately where we would be able to make

1 adjustments to the employee contributions in that plan, but
2 reduce the employee contributions for the -- for the first
3 two plans to twenty-one percent or seventeen percent for
4 individuals from -- from twenty-three to twenty-one.

5 And that was a relatively significant move as
6 well.

7 Now I just want -- again, I just think it's
8 important that -- that of that 1.25 billion, almost half of
9 that amount that we're requesting from our employees and the
10 unions will be met by benefit changes.

11 Q Now the contention is made that the company has acted
12 unfairly by not changing the bottom line figure that had
13 been allocated to each of the groups. Perhaps it would be
14 helpful if first you would explain why it is that you
15 allocated the amounts that have been allocated to each
16 group.

17 A Well, this is a pretty well worn track in terms of
18 looking at what other carriers have done. And in the last
19 1113 proposals made by United, they used the same allocation
20 methodology as you see in my declaration. Delta did the
21 same as well.

22 Q And -- and what was that methodology?

23 A To simply take the percentage of total labor costs and
24 equally by group. So in our case it ends up that each group
25 is approximately a twenty percent reduction.

1 Q Is that true for management and non-union employees as
2 well as union employees?

3 A We did. We elected to -- to take the same approach
4 with management and non-union employees.

5 Q And was there a particular equity situation involved
6 there?

7 A Well, back in 2003 we used a different methodology
8 when we assigned the amounts that we thought we needed to
9 achieve in our consensual restructuring. And without trying
10 to be too long-winded here, at that time we were in the
11 middle of this situation where some of our contracts were
12 pretty rich in the industry because they had been recently
13 negotiated. And, others, had not been negotiated in some
14 time and, in fact, had been open for some period of time.

15 So as a result of that we -- we did some work to
16 try to, I would say, harmonize and level the asks. And so
17 we started with where is this -- where is the particular
18 union's group contract in relation to what we saw as kind of
19 the industry. And so some people were asked to make larger
20 contributions and some lesser contributions, and we did not
21 go across the board equally.

22 At that time we -- we discussed with the unions
23 whether they thought we had allocated the amounts correctly
24 and it's no surprise that that was a question that the
25 unions weren't able to deal with and, in the end, they

1 accepted our allocations and we move forward.

2 Since then, the only things that have changed in
3 American have been one-and-a-half percent increases across
4 the board, which everybody participated in. So,
5 essentially, that level-setting that took place in 2003
6 still exists today. And if you look outside American and
7 look at the industry, because all of our principal
8 competitors that -- all the competitors set that we've been
9 talking about here over the past few days have all been
10 through bankruptcy. They have all done and met that favor
11 and equitable test as well. They all put in to a different
12 degree across the board increases for their employees, and
13 one of them have negotiated new agreements.

14 So it seemed to us that the -- that the absolute
15 -- the most fair approach at this juncture would be to
16 simply take percentage of labor costs, allocate it by group,
17 and it ended up that based on the output of the business
18 plan it -- it resulted in being at twenty percent.

19 Q So that's how you arrived at the figure that was
20 assigned to each labor group?

21 A That's correct.

22 Q Okay. Now the company has been reluctant to move off
23 those numbers; isn't that correct?

24 A That - that is absolutely correct.

25 Q Have you been willing to discuss those numbers with the

1 union?

2 A Yeah. We've -- and as I said earlier, I -- I started
3 down this track. We had a number of meetings with advisors
4 from the unions where they -- we gave them the opportunity
5 to have discussions with our principles n the business plan.
6 And although there were questions on the business plan, no
7 one ever made any specific recommendations of change in the
8 business plan.

9 And we -- we've said there were only a couple of
10 circumstances where we would be able to change the ask that
11 we had made. And that was someone would have to convince us
12 that either we had something wrong or that there was a
13 better alternative. So if -- if someone had made a
14 suggestion to modify the business plan in a way that -- that
15 we thought would have produced a different outcome for
16 labor, we would have been happy to have undertaken that
17 discussion. And if it had been reasonable, I think we would
18 have made the change.

19 Q Did anyone take you up on that offer?

20 A They did not.

21 MR. MOLLEN: Your Honor, may I have a moment?

22 THE COURT: Certainly.

23 (Pause)

24 MR. MOLLEN: Your Honor, we pass the witness.

25 THE COURT: All right.

1 CROSS-EXAMINATION

2 BY MR. JAMES:

3 Q Mr. Brundage --

4 A Mr. James.

5 Q -- that --

6 THE COURT: I -- I see you've met.

7 (Laughter)

8 MR. JAMES: We're like an old married couple.

9 THE WITNESS: We may disagree, but we like each
10 other.

11 THE COURT: That's -- that's good to hear.

12 Life's too short.

13 MR. JAMES: Edgar James on behalf of the pilots.

14 BY MR. JAMES:

15 Q Mr. Brundage, you talked about the 370 and I'm not
16 going to repeat. Mr. Mollen did some of my cross about --
17 you've always been firm. The 370 is the 370 and you came to
18 our board meeting and said after the freeze, if you ever
19 thought a 370 was not firm, it's really firm now, correct?

20 A That's correct, sir.

21 Q Now I want to go back to how you built the 370 and you
22 described that in Paragraph 24 and 26 of your declaration,
23 if I could turn you to that. And as I understand it on
24 Paragraph 24 you said, "Given that that target savings had
25 to be achieved, we formulated 1113 proposals," and that's

1 your testimony?

2 A That's correct.

3 Q Yeah. And then in Paragraph 26 it's basically
4 reiterates slightly -- a slight variation as saying, "After
5 detailing the annual cost savings attainable from everyone
6 else, the business plan required that additional 1.25
7 billion" -- should say billion -- "average over six years in
8 cost reductions." That's your understanding?

9 A Yes, sir.

10 Q Uh-huh. So who gave you the 1.25 billion? Where did
11 it come from?

12 A It came from the work that Ms. Goulet's team did and
13 the McKinsey team did. I mean, we heard testimony -- I was
14 here in the courtroom for Alex Dichter's testimony. They --
15 they came to the labor relations department and to the labor
16 portion of the finance department and said, this is what
17 we're going to need in the plan.

18 Q Uh-huh. And did you talk to Mr. Dichter ever yourself?

19 A The first time I spoke to Alex -- well, I know him from
20 previous lives. Since he has been engaged by American I had
21 not spoken to him until last evening.

22 Q I see. So you were given a number, an average of 1.25
23 over six years and to figure out how to achieve that labor
24 cost savings, correct?

25 A That's correct.

1 Q And as I understand what you did is you took that labor
2 cost savings and then back-checked against items -- you
3 constructed an 1113 list and then cost it out against --
4 trying to achieve for the pilots -- well, let me strike that
5 a minute. Can you just explain -- it's in your declaration,
6 but it's a little tricky -- how you come up with 370, and
7 this is not a trick question. It's --

8 A No. No. I -- as you know well, we had been bargaining
9 for a long time with all of our organized labor groups, so
10 we were not in a position where we needed to spend a lot of
11 time understanding what kinds of proposals needed to be
12 made, what some of those proposals were. And we had also,
13 obviously, done a lot of costing work during those
14 negotiations.

15 So the way I would describe it is we had the
16 benefit of all of those negotiations on the shelf when the
17 company decided to file. We then, as we -- as we thought
18 through the approach we were going to take for the 1113 term
19 sheet, develop those principles that I described earlier
20 about not trying to touch wages to the smallest degree
21 possible. And then we went on and simply just evaluated all
22 of the places there was opportunity for change.

23 So we were literally sitting with -- on a parallel
24 track with the business plan folks. And -- and we made the
25 decision that we were not going to make the 1113 proposals

1 to the unions until we felt comfortable that we had a very
2 solid business plan. So, yes. We were working on
3 understanding what all of the -- all of the pieces of the
4 puzzle could be, but we really didn't know the size of the
5 puzzle.

6 Once the business plan had been tested and people
7 began to firm it up and it moved to the point where it was
8 clear through that process the work that we were going to be
9 asked to do was 1.25 average over that term, we then went
10 about taking all those pieces we had for all of those groups
11 and trying to construct proposals that meant the objectives
12 that I described earlier.

13 Q Uh-huh. And did you feed that back through the -- the
14 people doing the business model to see what these various
15 provisions, how they would feed into the model?

16 A No. We -- we worked with our finance department, and I
17 know Brian is set -- Mr. McMenemy is set to testify. But
18 they primarily are the folks who are responsible for costing
19 the labor proposals. And so we had labor proposals. We had
20 costs developed by Brian -- by Mr. McMenemy's department,
21 and so we literally ran a tally sheet and would go back to
22 the business folks and say, okay. Here is a way that we
23 think we can achieve the savings that are necessary, did the
24 allocation first, obviously. That's how we got to the 370.

25 Q Uh-huh.

1 A And then worked back towards that and presented them
2 with alternatives as to how we would do this. And -- and,
3 you know, generally they left it up to the labor relations
4 team, our folks, to develop the pieces of the puzzle that
5 would get us there.

6 Q Uh-huh. What -- was there -- did that number change
7 from the time the company -- well, I know -- let me ask you,
8 when did you first start working on the labor cost -- labor
9 ask?

10 A Well, that's what I said. We -- that was in progress
11 -- all of those pieces were being created for the previous
12 four years while we were in negotiations. I mean, you know,
13 proposals around productivity, those kinds of things. So
14 they were on the shelf.

15 So we began to work towards, you know, a target
16 that -- that was based on -- not on the business plan, but
17 just based on our knowledge of what we believed we needed
18 from the history of the previous four years of bargaining,
19 and then once the business plan product was kind of firmed
20 up, it adjusted that number a little bit. WE made
21 adjustments to those proposals. So we were in pretty good
22 shape to be able to have proposals that totaled to the
23 necessary amount and we thought that would meet -- meet the
24 objective.

25 Q I got it. So you didn't go to them and say, look, here

1 is the labor cost piece; we can give you before you got the
2 1.259?

3 A No.

4 Q Okay.

5 A No.

6 Q And you described, Mr. Brundage, in -- about how you
7 came up with the twenty percent costing methodology and said
8 it was the same as United and Delta, and you -- you put that
9 Footnote 19 and you cite that, and you just testified to
10 that that methodology, correct?

11 A Yes, I did.

12 Q But you don't know how United and Delta came up with --
13 you know how they -- once they decided what they wanted, how
14 they allocate it, you don't know how they came up with the
15 ask for labor; you don't know what their methodology was to
16 come up with their counter-part to 1.25?

17 A If I understand your question, didn't see their
18 business plan, have no clue what -- what drove that number
19 for them.

20 Q I got you. You're just -- you're just saying, once I
21 was given a number. Here is a methodology I can use in
22 applying it to the respective labor --

23 A Yeah.

24 Q -- groups?

25 A Yes. Two --

1 Q Okay.

2 A -- two components of that. First, what will the
3 provisions be and, second, what does it need to add up to.

4 Q And let me raise a point that violates the Irving
5 Younger (ph) rule: Never ask a question you're not sure
6 what the answer is going to be. But you -- you said unlike
7 other bankruptcies, we're not taking an immediate labor pay
8 rate. We're not giving the employees immediate pay cut. Do
9 you recall that testimony?

10 A I think what I said -- I hope what I said was or what I
11 meant to say was we attempted not to change pay rates and we
12 wanted to do as much as possible to preserve as much double
13 D2 income as well.

14 Q Correct. But isn't it true that in the period, the
15 early 2000 period until those companies went through
16 bankruptcy -- I mean, United, Delta, Northwest -- their pay
17 rates, at least for part, went way over the top of ours, did
18 they not?

19 A In 2000 I believe the United agreement was twenty-plus
20 percent higher in rate as was the Delta agreement.

21 Q And they stayed that way until they went into
22 bankruptcy?

23 A I believe -- yes, sir.

24 Q When the DIP financiers got to them. And what about
25 Northwest?

1 A I -- I would be guessing and I don't want to do that.

2 Q Okay. Okay. Let me go to one of your -- I'm not going
3 to say complaints -- your laments is that in Paragraph 29 we
4 pushed our three bankruptcy proposals across the table and
5 is it fair to say you thought that was unproductive?

6 A I think any amount of negotiations is helpful. I think
7 that's how we're going to actually resolve this and find
8 consensual deals. I don't think that an inability to
9 recognize what is necessary to successfully restructure is
10 helpful, but I think the dialogue back and forth is what
11 will cause us to get to the point where we all understand
12 that's what we have to do.

13 Q Good answer.

14 (Laughter)

15 Q That was a trick question.

16 The -- in fact, of the forty-one proposals we
17 reached pre-bankruptcy you've accepted twenty-three of them;
18 isn't that correct?

19 A I don't know the numbers.

20 Q Okay. But -- but a significant number of those
21 agreements we've worked on you've accepted?

22 A That is correct.

23 Q Okay. Now the other point you -- let me just see. I
24 think it's Paragraph 38. You're talking about the
25 overheated rhetoric and God forbid we should ever engage in

1 overheated rhetoric, you would admit you owe Captain Bates
2 an apology. He's not the one that's been trying to derail
3 bargaining in the period prior to bankruptcy, correct?

4 A Yes. I -- I think all I've done is quote Captain Bates
5 and --

6 Q And you characterize Greg Schayman (ph) as the moderate
7 and Captain Bates as the hardliner? I think you and I
8 outside this courtroom would find that amusing.

9 The -- this take it or leave it, Mr. Brundage,
10 isn't it true that -- and you say -- you say in Paragraph 46
11 that you came up with 22 million in savings and that's
12 showing how reasonable you were and your willingness to
13 move, correct?

14 A Well, the intent was to demonstrate that when the
15 pilots came forward with an analysis that we were able to
16 evaluate and either agree that it was as good as ours or
17 better than ours. We were willing to accept it and move
18 forward.

19 Q But that was because pay-banding prior to bankruptcy
20 you had put a significant cost savings on it and post-
21 bankruptcy you had no cost savings for pay-banding, correct?
22 Do you remember that disconnect?

23 A I think there are a number of disconnects and if I can
24 expand for a second, my goal pre-bankruptcy was to get
25 whatever might be possible to move forward. Post-bankruptcy

1 it was what do we absolutely need to restructure.

2 Q Okay. And of the cost savings that you achieved, you
3 use that as the example of where -- how -- our willingness
4 to move. Isn't it fact you took the cost savings and just
5 came back with a new term sheet?

6 A I think we've -- I think we've provided three term
7 sheets. I --

8 Q Well, the March --

9 THE COURT: I'll -- let me just --

10 MR. JAMES: March 21st.

11 THE COURT: -- I'm not sure what's confidential
12 and what's not confidential or -- or what -- whether there's
13 an objection. If you -- if you want to say something that
14 has to do with what was testified to, somebody's got to
15 spring to life and actually mouth the words objection.

16 MR. MOLLEN: It -- it has nothing -- it has
17 nothing to do with object -- objecting or confidential
18 information, Your Honor.

19 THE COURT: All right.

20 BY MR. JAMES:

21 Q It's just -- you -- you say take it or leave it. We
22 were willing to discuss with the union what to do with the
23 cost savings and my question is, didn't you, on your own,
24 unilaterally, just redo the term sheet and hand it back on
25 March 21st?

1 A We wanted -- yes. We wanted to provide back to the
2 pilots a representation of the change and the best way to do
3 that was to put it on a new term sheet.

4 Q Thank you.

5 If I can just take -- let me ask you about the two
6 other examples you use as examples of willingness to move.
7 One is the pension freeze. You're aware that the unions,
8 the first thing they asked the company was what's the
9 costing on a pension freeze and -- and the company said they
10 had not done the costing on a pension freeze, correct?

11 A Yes, sir.

12 Q Uh-huh. And on the medical plan you talk about in
13 Paragraph 44, when you went back and redid the medical plan
14 isn't it true that all -- that you had the same cost
15 savings, you just changed the deductibles and the premiums
16 among those plans, but it's the same number on the cost
17 savings?

18 A The request or the feedback that we were responding to
19 was that the medical plans were too expensive for the
20 employees. So we wanted to be as creative as possible. And
21 you are correct. We adjusted the design of the plan so that
22 we could accomplish that goal and still achieve our savings.

23 Q Okay.

24 MR. JAMES: Can I have one minute, Your Honor?

25 THE COURT: Sure.

1 (Pause)

2 MR. JAMES: Mr. Brundage, I think you're free of
3 me.

4 CROSS-EXAMINATION

5 BY MR. CLAYMAN:

6 Q We've met before.

7 A Mr. Clayman.

8 Q I just wanted to get into the -- my understanding of
9 exactly where you fit in within the corporate structure. I
10 take it you are a member of the executive committee?

11 A That's correct.

12 Q And how long have you been a member of that committee?

13 A Since 2004, spring of 2004.

14 Q And those are weekly meetings that you attend?

15 A Normally, yes, weekly.

16 Q From time to time do -- does the executive committee
17 bring in people from outside, consultants and the like to
18 attend any of the executive committee meetings or are they
19 always limited just to the members of the committee?

20 A No, sir. Sometimes people are asked to attend.

21 Q Okay. Have people from McKinsey attended the executive
22 committee?

23 A No, sir, not while I've been --

24 Q What about from Rothschild?

25 A Yes.

1 Q Okay. And who from Rothschild has attended that
2 meeting?

3 A Chris Lawrence has been in the room.

4 Q Okay.

5 A And -- I think just Chris. I -- let me just be
6 perfectly clear. David Resnick could have been there, but I
7 don't remember for certain.

8 Q And how many times has Mr. Lawrence attended those
9 meetings?

10 A Less than a handful.

11 Q Okay. And has he ever spoken at any of the meetings?

12 A Yes, he has.

13 Q And what is the first time that he attended one of
14 those meetings where you remember that he spoke?

15 A Probably sometime back in 2006, 2005. We -- we had a
16 regular long -- we had a regular relationship so I -- if
17 you're asking me related to this process?

18 Q Yes.

19 A It would have been sometime in -- sometime in late
20 November, probably.

21 Q Okay. And how many times after -- was that late
22 November, I take it, preceding the bankruptcy?

23 MR. MOLLEN: Your Honor, I'm going to object to
24 the question being beyond the scope of the witness's direct.

25 THE COURT: Well, it's an interesting question

1 because we have been spending some time on that. So what --
2 what say you?

3 MR. CLAYMAN: I think that this is just background
4 for his testimony about considering alternatives and whether
5 or not and to what extent those alternatives were
6 considered.

7 THE COURT: Well, but if -- if -- we've certainly
8 had a lot of witnesses on a lot of topics. But, again,
9 there was a big point made about what he was being offered
10 for and what he wasn't being offered for, and I don't
11 believe -- if you can tie this into some opinion he has or
12 some views he has that's one thing. But if it's generally
13 about the process and communications, I don't think he's
14 that -- been offered as that witness.

15 So if you can tie it into something in his -- in
16 his declaration, I'm -- I'm fine with that and that -- that
17 may take a couple of questions and I'll -- I'll be happy to
18 give you that latitude.

19 MR. CLAYMAN: Let me see if I can.

20 THE COURT: But if it's more generalized --

21 MR. CLAYMAN: I understand.

22 THE COURT: -- I think I'm going to shoot it down.

23 MR. MOLLEN: Or, fundamentally, Your Honor, it
24 seems to me that the witness's testimony on direct was
25 limited to a very specific temporal time frame and to the

1 specific language that was contained in his declaration. I
2 hardly think it's fair to subject the witness to cross --

3 THE COURT: No. Well, that's --

4 MR. MOLLEN: -- that is far beyond --

5 THE COURT: -- that's why I -- I -- again, that's
6 why I think it's got to be tied to something that's in his
7 declaration, which sometimes takes a few questions to do.
8 So --

9 MR. MOLLEN: Thank you, Your Honor.

10 THE COURT: -- we'll -- we'll -- I'll give some
11 latitude on that, but -- but I do agree -- this -- this is
12 -- I know there's an aspect, sort of a discovery-like aspect
13 to some of these questions on occasion, given the procedural
14 posture. But we sort of have gone down the road of tying
15 these things to the direct testimony. So --

16 MR. CLAYMAN: Fair enough. Well, let me see if I
17 can tie it up at the end, maybe we'll touch on it throughout
18 -- as I proceed here.

19 BY MR. CLAYMAN:

20 Q You testified, I think, that you came up with a number,
21 a target that was then presented, I guess, to McKinsey or
22 whomever and it was adjusted, you said, a little bit to
23 become the 1.25 billion-dollar number. Do you --

24 MR. MOLLEN: Objection. Misstates --

25 MR. CLAYMAN: -- remember that testimony?

1 MR. MOLLEN: -- his testimony.

2 THE COURT: Well, I think he can answer the
3 question if he says, is that right or not.

4 MR. CLAYMAN: Right.

5 BY MR. CLAYMAN:

6 Q Is that correct?

7 A It is not.

8 Q Okay. Well, can you --

9 A The way you stated it is not correct.

10 Q Okay. Well, tell me exactly what I -- what I heard was
11 that there was a number that you first came up with and then
12 it was adjusted.

13 A We had made numerous presentations to our board over
14 time, and one of those presentations or a number of those
15 presentations included a reference to the methodology we
16 talked about earlier, the six-hundred-million-dollar, I
17 think we called it contract gap. And in a number of those
18 presentations you'll see that we also talked about a two-
19 hundred-million-dollar pension under -- annual pension
20 underfunding and we talked about the fact that our employees
21 are very senior in their positions, so as a result of that
22 they're at the top of their wage scales and that produces
23 about another \$100 million in deficit that wasn't included
24 in that six to 800 million.

25 We also talked about the fact that our operations,

1 the nature of our operations drive differences. So we had
2 been talking with our board for some time about having
3 approximately a one-billion-dollar gap to our competitors,
4 on average. And I think that's an important point. People
5 talk to this 600 or the billion-dollars as if it's to a
6 specific carrier. It is to the average when you run that
7 model. So there is no carrier that that represents. It's
8 the average of carriers, so some much higher, some much
9 lower.

10 So I didn't expect for a moment that we would be
11 working in a zone dramatically different than what we
12 assumed we were just on a competitive basis without even
13 ever having seen the business plan. So that was the
14 starting point, and I never gave a number to McKinsey. They
15 did work. They worked through the business plan. They
16 developed what they thought was necessary in conjunction
17 with our team and it so happens that the numbers were quite
18 close.

19 Q Well, let me -- let me just understand because I think
20 I've seen the six-hundred-million-dollar number and the \$200
21 million for -- I think it relates to pension benefits?

22 A That's correct.

23 Q Okay.

24 A That's the annual --

25 Q And I believe there's \$100 million associated with the

1 seniority differences, right?

2 A Correct.

3 Q Okay. But the \$100 million for operational
4 differences, what does that refer to?

5 A Well, for instance, we have a much higher sick rate at
6 American than any of our competitors, and so as a result we
7 have less productivity in that area and that absolutely
8 drives a cost structure that's much higher. And I think we
9 could -- we could look at some other things like that.

10 Q Did you ever quantify that and -- and create a document
11 that contained that \$100 million difference in operation --
12 operational differences?

13 A I did not.

14 Q Have you ever seen a document that contained that \$100
15 million?

16 A I have. Brian McMenamy, who will be testifying in a
17 little bit, has done quite a bit of work using Form 41 data,
18 and as we've spent a lot of time talking about Form 41 data.
19 But it is not particularly detailed, but it does allow you
20 to break out labor costs, and Brian has taken a look at the
21 publicly available results of companies, public companies
22 report each quarter and annually. So he has taken a look at
23 their results. He has taken a look at the Form 41 data and
24 that analysis triangulates on the same place. It's a --
25 we're -- we've got a little more than a billion-dollar

1 shortfall on average to the industry.

2 Q Okay. When you said he looked at other industries; is
3 that correct?

4 A No. I said other airlines. If I said industries, I
5 apologize.

6 Q Oh, okay. So the spread between the number that you
7 kind of came -- came up with internally and the number that
8 McKinsey came up with is about \$250 million?

9 A Well, I'm -- if I gave the impression I was being that
10 specific I was not. But it's -- it was generally in the
11 billion-dollar or slightly larger range of what we believed
12 our deficit was, and the 1.25 was specific.

13 Q And is it -- the 1.25 billion number that McKinsey came
14 up with or is it really the 1.5 billion-dollar steady state
15 number that is an apples to apples comparison?

16 A I think we've had numerous conversations and testimony
17 about those two numbers being actually the same, but two
18 different ways to describe it.

19 Q But if you -- is it -- is it fair to compare the
20 billion-dollar -- or when you say slightly higher number to
21 the steady state number of 1.5? Is there any reason why
22 that comparison doesn't hold up?

23 A They are two numbers derived from totally different
24 sources and approaches, and if you want to compare them I
25 think you can compare them, but --

1 Q Okay. Turning your attention to Paragraph 6 of your
2 declaration -- I'm sorry. It's actually Paragraph 10. I
3 apologize. Before you -- I turn your attention to the --
4 your statement in that paragraph, isn't it true that in 2003
5 the company went to each union and stated that this was a --
6 that they designated a certain amount that the unions would
7 have to give?

8 A Yes, sir.

9 Q And each of the unions met that amount that was asked
10 of them, correct?

11 A That's correct.

12 Q And there was no variation from that amount. The
13 amount was stated and there was no change. It was never
14 lowered or anything like that?

15 A Not to my knowledge.

16 Q Okay. So then when you say in Paragraph 10 that the
17 company -- and I'm looking at the second line of that
18 paragraph on Page 6. It says, "The company watched as one
19 by one its competitors used the bankruptcy process to do
20 what American had been unable to do consensually." And
21 point of fact, you asked for a certain amount of money and
22 that amount of money was given, correct?

23 A We -- it is correct that we asked for a certain amount
24 of money and that's what achieved in the restructuring.
25 However -- the consensual restructuring in 2003. However,

1 we didn't have the benefit of understanding what was going
2 to happen at US Air. We didn't have the benefit of
3 understanding what was going to happen at United. Those two
4 had filed, but had just begun to do concessions and, as you
5 know, US Air didn't get it right the first time and ended up
6 back in bankruptcy. And United took three years in
7 bankruptcy and we had no idea that either Northwest or -- or
8 Delta were going to file. So as a result, we based it on
9 what we thought the future might look like and the reality
10 is --

11 Q Right.

12 A -- we were very short.

13 Q But it wasn't that you were unable to do it
14 consensually. You never -- at that time you never asked for
15 changes in the benefits that were ultimately changed in the
16 bankruptcies of other airlines?

17 A We took a -- we took a different approach in 2003 and
18 went to the unions and said, look, we're going to set the
19 target and we'll give you the methodology for the target.
20 But we are not going to focus on putting you -- on asking
21 you to do specific things. Each union chose to achieve
22 their target in their own individual manner.

23 You know, as you know, the flight attendants took
24 a very different approach than the pilots did in certain
25 areas like benefits and the TWU was the outlier in benefits

1 in terms of the approach that they took because they chose
2 to meet their savings targets in different ways. We didn't
3 prescribe how they needed to meet those savings targets.

4 Q Correct.

5 Now turning your attention to Paragraph 15, just
6 tell the Court briefly who Laura Gladding (ph) is?

7 A She is the president of the flight attendants union.

8 Q And you state in this Paragraph 15 that Ms. Gladding,
9 in -- on April 1st of 2008, laid out the union's bargaining
10 strategy; is that correct?

11 A Yes, sir.

12 Q Okay. And April 1st, isn't that the date that Ms.
13 Gladding first took office as president of APFA?

14 A I know that it was around that time. I assume you're
15 correct.

16 Q And the statement that you have quoted here, have you
17 ever heard Ms. Gladding say that again since April 1st of
18 2008?

19 A I have heard Ms. Gladding on a number of occasions talk
20 about returning the flight attendants to their rightful
21 place, talking about recovering what had been given in 2003
22 and have -- you know, Ms. Gladding is a strong political
23 leader and she's made very political statements about her
24 intent to do the very best she can do for her flight
25 attendants, which include getting as much back as -- of what

1 they did in 2003 as possible.

2 Q Well, Mr. Brundage, isn't it true that in April of 2011
3 there was an exchange of "supposals" in which the spread
4 between the union and the company was approximately \$30
5 million"?

6 A I think 30 million is about right.

7 Q Right. And the union -- and the company was at about
8 60 million; is that right?

9 A I -- I apologize. And I'm not --

10 Q No.

11 A I really don't want to be argumentative --

12 Q That's all right.

13 A -- but you were actually at the table and I was on the
14 periphery of the negotiations --

15 Q Well --

16 A -- so you have much better knowledge of this than I do.

17 Q Well, no. No. You came to the hotel room the final
18 night so just to refresh your memory.

19 A I absolutely remember that, but I didn't participate in
20 the bargaining all --

21 Q I know.

22 A -- all along the way.

23 Q Okay. But is it fair to say that roughly the company
24 was at about 60 million and the union was at about 90?

25 A I'm -- I'm going to agree with you because --

1 Q Okay. Now at the time that they gave up their
2 concessions in 2003, the five-year average was \$340 million,
3 was it not?

4 A Yes, sir.

5 Q Okay. And the last year that -- of those concessions
6 the amount was substantially higher in 2008; isn't that
7 true?

8 A (No verbal response)

9 Q And you would agree that \$90 million is not quite
10 restoration of the concessions that were given in 2003?

11 A Yes, I would.

12 Q Okay. In Paragraph 16 you state in the last sentence
13 that on many occasions union representatives declined to
14 attend these presentations of management, I think is what
15 it's referring to?

16 A Do you mind if I --

17 Q Oh, of course. I'm sorry. Yeah.

18 A -- take a second to really read it.

19 Q Last sentence.

20 (Pause)

21 A Yes, sir.

22 MR. MOLLEN: I'm sorry. What paragraph?

23 THE WITNESS: Yes, sir.

24 MR. CLAYMAN: Oh, I'm sorry. It's Paragraph 16.

25 MR. MOLLEN: Thank you.

1 BY MR. CLAYMAN:

2 Q You've read that?

3 A Yes, sir.

4 Q "On many occasions union representatives declined to
5 attend these presentations." Do you ever recall the APFA
6 refusing to attend any of those presentations?

7 A I don't believe we have a hundred percent attendance
8 from any union, but I would -- I'll tell you that the APFA
9 was a regular attendant at those meetings.

10 Q Okay. And you know of no instance where they
11 affirmatively said we're not going. It may just have been a
12 matter that they weren't -- were not able to be there on a
13 particular day?

14 A Yes, sir.

15 Q All right. Now you referred, in Paragraph 21, to two
16 tentative agreements that were reached with the maintenance
17 control technicians and the ground school instructors.

18 MR. MOLLEN: Objection, Your Honor. I thought we
19 were going to leave the TWU out of this part of the --

20 MR. CLAYMAN: I think this is -- doesn't go into
21 any of the substance as to -- of concern. It's not --

22 THE COURT: All right. Well, let -- let me hear
23 the question first and if --

24 MR. CLAYMAN: The question is simply --

25 THE COURT: -- if it --

1 MR. CLAYMAN: -- I just wanted to know how many
2 members in each of those bargaining units; those contracts
3 covered how many people.

4 THE COURT: I see somebody rising from the TWU.

5 MR. CLAYMAN: It's okay.

6 THE COURT: It's all right.

7 MR. CLAYMAN: I have --

8 THE COURT: All right.

9 MR. CLAYMAN: -- I have clearance.

10 THE COURT: It's been blessed, so proceed.

11 MR. CLAYMAN: Yes.

12 (Laughter)

13 THE WITNESS: They are small groups in terms of
14 American groups. I do not know the exact number in either
15 of those groups, but it's hundreds, not thousands.

16 BY MR. CLAYMAN:

17 Q And it's -- one of the groups could even be less than a
18 hundred?

19 A Yes, it could.

20 Q Okay. Okay. Turning to Paragraph 22, you mentioned
21 within that paragraph, I believe, let's see -- I'm sorry.
22 Well, let me -- I don't -- I can't find the reference and I
23 apologize, but I think it's easy enough to get in the
24 record, which is part of the term sheets for each of the
25 unions was a profit-sharing proposal. Is that correct?

1 A Yes, sir.

2 Q As well as a proposal in the event of a consensual
3 agreement that each -- there would be five one-and-a-half
4 percent annual increases?

5 A Yes, sir.

6 Q Okay. And that was obviously -- not obviously, that
7 was contingent upon an agreement as well?

8 A Yes, sir.

9 Q And the third contingency that was dependent upon an
10 agreement was the match of the 401(k)?

11 A Yes, sir.

12 Q Now let's take the profit-sharing first. If there were
13 no consensual agreement and the company ultimately realized
14 the profits that they are projecting, or let's back up a
15 minute. If there were a consensual agreement and there was
16 profit-sharing, then, obviously, out of those proceeds the
17 flight attendants would receive some sort of -- some amount
18 of money?

19 A Pro rata share. Yes.

20 Q Pro rata share. And that pro rata share would
21 effectively reduce the \$230 million; that is, in terms of
22 the net savings that would be realized by the company, if
23 they paid out, let's say, \$30 million in profit-sharing and
24 the savings were \$230 million in cost savings, isn't the net
25 then just \$200 million?

1 A I apologize. I'm -- I'm not following your question.

2 Q What I'm saying is that you're looking -- you're --
3 you're saying that you need \$230 million in savings --

4 A Yes, sir.

5 Q -- right? You say that and that's true, but in the
6 course of the year under the profit-sharing isn't it true
7 that that amount of money could be offset by payments of
8 profit-sharing to the flight attendants?

9 A The -- I'm have -- I'm having a hard time understanding
10 the relationship between the 230 and the profit-sharing
11 payments. The 230 is what is necessary for the successful
12 restructuring. The profit-sharing is there so that if we
13 have, in fact -- if we perform better than expected on our
14 plan, if the economy improves, or if some other external
15 circumstance occurs, our employees will have the ability to
16 share in -- in those profits.

17 I have a very hard time understanding the
18 connection between cost savings and revenue.

19 Q Okay. I -- I appreciate that -- that distinction. But
20 let's go to another example. Let's talk about the one-and-
21 a-half percent wage increases. If there were a consensual
22 agreement, then the flight attendants, I believe, very
23 roughly -- and tell me if this is in the ballpark -- that
24 the five one-and-a-half percent increases comes out to
25 somewhere around twenty, \$25 million a year on average over

1 that five-year period? Ball park.

2 A Okay. Yes, sir.

3 Q Okay. So if there's a consensual agreement and those
4 one-and-a-half percent increases are paid, then the \$230
5 million yearly average savings is reduced by that \$20
6 million, is it not, in terms of the net savings that the
7 company will realize?

8 A All money is green, so if we have savings over here and
9 we pay something out over here, obviously, it offsets.

10 Q So in that case \$210 million would be necessary for the
11 company's reorganization?

12 A No. That's not correct because --

13 Q Well, give me just yes or no. That's all I need to
14 know.

15 A No.

16 Q No. Okay. Well, let's talk about one more item, and
17 this one, unlike the cost savings, is not embedded in the
18 term sheet.

19 One of the savings or one of the -- excuse me --
20 costs of the term sheet is the five percent or the five-and-
21 a-half percent match for the 401(k).

22 A Okay.

23 Q And that offsets the overall savings that the 230
24 represent; that is, if you were not paying the five-and-a-
25 half percent, then you would be saving more money, correct?

1 A Correct.

2 Q Okay. And so if there were not a consensual agreement
3 and that five-and-a-half percent were not paid, and let's
4 assume for sake of argument that that five-and-a-half
5 percent for the flight attendants represents roughly \$30
6 million, then what's necessary for the reorganization would
7 be \$260 million; isn't that true?

8 A No. The target would still be the same. We just would
9 have had a credit against the target.

10 Q Right. And you would not have achieved the necessary
11 -- the amount that you have deemed necessary for purposes of
12 1113?

13 A I disagree with that, but maybe I'm not understanding
14 your question. At the -- you know, I think --

15 Q That's all right. I don't think there's a question
16 pending at this point. I think -- if you don't understand
17 it, I -- I'm happy with the way it's -- the answers and I'm
18 fine.

19 THE COURT: Okay. Next question.

20 MR. CLAYMAN: Yeah.

21 BY MR. CLAYMAN:

22 Q Now looking at Paragraph 34, Footnote 23 that's part of
23 34, I believe. Yeah. Now you, I take it, Mr. Brundage, in
24 your capacity are very, very much aware of what's going on
25 within the industry at competitors?

1 A I try to be.

2 Q Okay. And you know, for example, that United Airlines
3 flight attendants reached an agreement in January of 2012?

4 A Yes, sir.

5 Q And you know that that agreement was ratified in
6 February of 2012?

7 A Yes, sir.

8 Q And that agreement was, on net, cost the company money.
9 It was not a zero sum agreement, did not save the company
10 money. It cost the company money?

11 A I've never seen an analysis of the agreement. I do
12 know that there were increases to wages, but there were also
13 substantial improvements to productivity.

14 Q Okay. But you know that that agreement was ratified by
15 upwards of eighty percent of the membership of AFA at
16 United?

17 A I only know that it was ratified.

18 Q Okay. And you know that an agreement was reached with
19 US Air in February of 2012?

20 A With which group?

21 Q I'm sorry. With the flight attendants?

22 A Yes.

23 Q Okay. And you know that that -- ultimately, that went
24 out for a ratification and the membership rejected it at the
25 end of March of this year?

1 A Yes, sir.

2 Q Okay. Then how would you reconcile those events with
3 your testimony in paragraph -- in the footnote that
4 "American's competitors no doubt anticipate that the
5 company's costs will be reduced in bankruptcy and they would
6 naturally be reluctant to agree to higher wages and benefits
7 for their own employees while the bankruptcy process is
8 underway?

9 A Can you point me to that so I can look at it?

10 Q It's in the footnote, paragraph -- Footnote 23.

11 (Pause)

12 THE COURT: And once he reads it if you would
13 restate the question, just --

14 MR. CLAYMAN: Yeah. Okay.

15 BY MR. CLAYMAN:

16 Q I just would like to know how if -- having that
17 information, knowing that there were agreements reached at
18 United and US Air, one of which was ratified, how you could
19 make the statement in Footnote 23 that the company's
20 competitors would be reluctant to reach agreements that
21 provided higher wages and benefits?

22 A Because I have no idea what they might have done
23 otherwise.

24 Q I'm not sure I understand that -- that answer.

25 A Well -- well, I -- the -- each management team is going

1 to make determinations as to what they're willing to offer
2 or willing to -- to do in their union agreements. And I
3 don't know that the US Air folks or the United folks might
4 not have added another twenty percent to their agreement had
5 they not been concerned that American would have a
6 significantly lower cost structure.

7 So the fact that they simply added something to
8 the agreement tells me nothing about convergence.

9 Q But I think you're -- I think the statement stands for
10 itself, which is that they would -- you're saying it's that
11 they would agree -- they were reluctant to agree to higher
12 wages and benefits, not that they would have agreed to more
13 or even higher wages and benefits absent the agreement?

14 MR. MOLLEN: Objection. Asked and answered.

15 THE COURT: Umm --

16 MR. CLAYMAN: That's fine. That's fine.

17 THE COURT: I'm going to sustain the objection
18 just -- because I'm -- just as to -- as to the form of the
19 question.

20 BY MR. CLAYMAN:

21 Q But let me just ask if you are aware of Delta having
22 announced to its flight attendant that they will be
23 receiving a five-percent wage increase in July of this year?

24 A The Delta flight attendants or the Northwest?

25 Q The Delta.

1 A Just the Delta flight attendants.

2 Q Well, my understanding is those agreements are now
3 merged. But that may be wrong. I -- well, do you -- do you
4 have an understanding as to whether those agreements have
5 been merged?

6 A Well, there -- there are no agreements. They're non-
7 union.

8 Q Well, that's a very good point.

9 (Laughter)

10 Q The terms and conditions of employment, are they now
11 uniform for both groups?

12 A I honestly don't know that. I know that there has been
13 a representation dispute at Delta, which has been very
14 robust. And as I understand it, there are -- there are
15 still claims of interference out there and the NMB has not
16 ruled. But my information could be old and it's my
17 understanding that Delta has told its Northwest -- former
18 Northwest flight attendants that until those representation
19 issues are resolved, they won't -- will not move to the --
20 to the -- to the pay rates, the Delta pay rates.

21 Q But are you -- do you understand that they have
22 announced, whether it be for the Delta and Northwest --
23 former Northwest flight attendants or just the Delta flight
24 attendants that some portion of the Delta workforce will be
25 getting a five-percent wage increase?

1 A I understand there's a wage increase. And, really, I'm
2 not trying to be difficult. I just don't know for sure that
3 it's five percent. I know --

4 Q Okay.

5 A -- there's an increase on the horizon.

6 Q Okay. Do you have any idea as to what the percentage
7 is?

8 A I -- I don't.

9 Q Okay. You -- you were here, I think you stated, for
10 Mr. Dichter's testimony?

11 A Yes, sir, I was.

12 Q And I think you said that you had not met with
13 Mr. Dichter during the course of the bankruptcy until last
14 night?

15 A That's correct.

16 Q Have you met with other members of the McKinsey team?

17 A I have not.

18 Q Okay.

19 MR. MOLLEN: Your Honor, I'm sorry to interrupt
20 Mr. Clayman. Can I inquire as to how long this examination
21 will continue? I think maybe the witness could use a break.
22 He had to listen to lawyers arguing and that's --

23 THE COURT: All right.

24 MR. CLAYMAN: Yeah. I -- I probably have at least
25 another twenty minutes, thirty minutes. So --

1 THE COURT: All right. Let me get a ballpark
2 sense of -- of the other cross to come, just in terms of
3 making plans for -- for this evening, if necessary.

4 MR. SHERWOOD: We have none, Your Honor. By
5 stipulation we're not going to cross-examine this witness.

6 THE COURT: All right.

7 MR. SHERWOOD: And we reserve our right to set the
8 rebuttal --

9 THE COURT: Okay. So -- yeah. That's fine.
10 Let's take a break. But, also, during that break if folks
11 would talk and just, perhaps, give me some sense, if they
12 know, as to what it looks like for other witnesses this week
13 so we can just plan. The reason why I ask and why it's
14 related to today is because I'm wondering whether we should
15 go late today if -- if there's a desire to finish this week
16 and there's going to be more witnesses added to the queue.
17 So it may actually have an impact on what we do today.

18 MR. FLICKER: Your Honor, one other question.
19 Does the Court have any constraints tomorrow in terms of its
20 court day, assuming that we need to use it?

21 THE COURT: I can answer that question now if you
22 think it's helpful in your planning purposes. I think that
23 everything we had we have moved to make room for all of you,
24 so I think we don't have any restrictions.

25 So, again, if -- if I ask people to stay late I've

1 got to give them some notice here, so that's what I'm trying
2 to figure out. So if you would do me the favor of chatting
3 about that during the break and -- and we'll talk about it
4 when we come back.

5 MR. FLICKER: Thank you.

6 MR. MOLLEN: Thank you, Your Honor.

7 THE COURT: Thank you.

8 (Recess at 4:02 p.m.)

9 THE CLERK: All rise.

10 THE COURT: Please be seated.

11 MR. MOLLEN: Your Honor, I think we've got a plan.

12 THE COURT: All right.

13 MR. MOLLEN: As I understand it, and union counsel
14 can correct me if I'm wrong, the remaining cross for this
15 witness is likely to be in the thirty-minute range.

16 THE COURT: All right.

17 MR. MOLLEN: We'll finish with Mr. Brundage.

18 Mr. McMenemy is here. He's ready to testify. As
19 I understand it, his direct is likely to run twenty minutes,
20 approximately, we think. And, again, you can correct me if
21 I'm wrong. We understand that only one of the unions is
22 going to cross Mr. McMenemy and that should take twenty
23 minutes to a half an hour. So going forward with him it
24 seems to me makes very good sense.

25 And Mr. Newgrin (ph) has been released.

1 THE COURT: Okay.

2 MR. MOLLEN: He will not be crossed, and that
3 leaves us with Mr. Vaughn (ph), who I don't believe will be
4 long, but I think it may be unduly optimistic to project
5 covering all of this tonight. So --

6 THE COURT: No. That's fine. And we -- I do
7 have tomorrow reserved. I just wanted to make sure we
8 weren't in a situation where there were folks that -- that
9 the unions wanted to talk to this week where --

10 MR. MOLLEN: Right.

11 THE COURT: -- we couldn't fit them in if we broke
12 today at six and spent all day tomorrow. So it doesn't
13 sound like that's -- that's --

14 MR. CLAYMAN: No.

15 THE COURT: -- going to be a problem in any event.

16 MS. LEVINE: Your Honor, we -- I don't know which
17 one of the unions was going to cross Mr. McMenemy, but we --
18 we have a couple of questions for him.

19 MR. MOLLEN: Okay. I was --

20 THE COURT: Okay. What --

21 MR. MOLLEN: -- incorrect in my assumption, but at
22 any rate --

23 THE COURT: Well, that's all right. We'll get
24 through this nice gentleman here and then we'll see where we
25 go. But if we're only down to one other witness other than

1 Mr. McMenamy, we have been able to handle two a day so I
2 think we'll be fine.

3 Let me -- let me just ask one -- I just want to
4 make one clarification. I don't think this is an issue and
5 I'm probably over-thinking it as a matter of trial theory.

6 I assume by agreeing to push off the questioning
7 about the term sheets, the more recent term sheets, which --
8 which the debtor says are -- is the operative term sheet for
9 purposes of 1113, although the unions disagree, no one is
10 going to make the argument legally that they haven't somehow
11 met their burden and -- as a matter of trial procedure where
12 we should -- we should cease proceedings.

13 I just want to make sure that everyone
14 contemplates -- contemplates their ability to --

15 MR. MOLLEN: Your Honor, I think that one of the
16 quid pro quos for staging things as we did was that the
17 scope of the debtors' rebuttal would be somewhat broader
18 than typical rebuttal.

19 THE COURT: That's -- that's exactly what I'm
20 getting at. And, again, I think I'm probably over-thinking
21 this as a matter of -- of trial tactics. But I just -- this
22 job has taught me to -- to -- that, you know, you can be
23 surprised by arguments people may make if -- if they have
24 the right to make them. So I just wanted to make sure that
25 we're -- we're not going to face that kind of problem.

1 So, that's fine. I didn't expect we would, but
2 proceed, Counsel.

3 MR. CLAYMAN: Thank you, Your Honor.

4 CROSS-EXAMINATION (Resumed)

5 BY MR. CLAYMAN:

6 Q Mr. Brundage, you've been involved in the negotiations
7 of a number of collective bargaining agreements over the
8 years; is that right?

9 A Yes, sir.

10 Q And wouldn't you agree that valuing the various
11 proposals that the parties put on the table is a critical
12 element to reaching an agreement?

13 A It's a critical element of understanding the cost of
14 the agreement you reach.

15 Q And isn't that often times a very critical element to
16 -- coming to an agreement?

17 A There are disagreements over the costs of --

18 Q Right.

19 A -- proposals which are -- make it difficult to come to
20 agreement.

21 Q Yes. And -- and often times those -- those differences
22 have to be reconciled before an agreement can be reached?

23 A Yes, sir.

24 Q Okay. And in the case here you have costed out each of
25 your term sheets to each of the three unions; isn't that

1 true?

2 A I have not.

3 Q I understand. I'm using the royal I --

4 A Okay.

5 Q -- for you.

6 (Laughter)

7 Q Whatever that is.

8 A The company has --

9 Q Yes.

10 A -- posted (sic) out each of its proposals.

11 Q Yes. And they've posted that on the interlink document
12 website?

13 A Yes, sir.

14 Q So any one union can see the term sheets of the other?

15 A That I don't know.

16 Q Okay.

17 A I know that each union can see its own term sheet, but
18 I don't know --

19 Q Okay.

20 A -- that unions can see the other unions --

21 Q Okay.

22 A -- term sheet.

23 Q That's fine. But you -- do you think that it's
24 important there be some level of transparency between what's
25 being -- the elements of the various term sheets and their

1 valuation, that that's an important thing for each union to
2 know to have the assurance that things are being done fairly
3 across the board?

4 A Yes. In fact, we took the unprecedented step in the
5 airline industry when we began negotiations back in '06 and
6 '08 to begin to publish, at the time on our -- a
7 negotiations.com website all of the information related to
8 both our proposals and the reasoning for our proposals and
9 then we continued that on the -- a restructuring site post-
10 filing.

11 Q But in order to have that level of transparency in a
12 situation like this where a lot of money is -- is on the
13 table so to speak, isn't it important, also, to be
14 transparent about the valuations of each term sheet?

15 A Yes, sir.

16 Q Okay. Now you have made a, I guess -- I don't know
17 whether you would call it a term sheet because it's not
18 negotiable, but you have set forth the changes that you are
19 going to make to the management's support staff?

20 MR. MOLLEN: I would -- Your Honor, I'm not
21 inclined to object -- to interrupt Mr. Clayman's
22 examination, but the -- he's asking a lot of questions of
23 this witness regarding costing without any foundation of the
24 witness's own job description and we have a witness to talk
25 about costing --

1 THE COURT: All right.

2 MR. MOLLEN: -- coming up immediately after.

3 THE COURT: Let me -- let me repeat the -- could
4 you repeat the question?

5 MR. MOLLEN: No. It's just -- I don't remember
6 what the question was.

7 THE COURT: All right. We actually have the
8 benefit of being able to have it read back if you would be
9 so kind.

10 THE COURT REPORTER: Now you've made, I guess -- I
11 don't know whether you would call it a term sheet because
12 it's non-negotiable, but you had set forth the changes that
13 you were going to make to the management's support staff.

14 THE COURT: All right. I'll allow the question.

15 MR. MOLLEN: Right. It was the document that we
16 were trying to get in that led to the brew-hah-hah earlier,
17 the term sheet for the --

18 MR. CLAYMAN: I'm not asking about any of the -- I
19 have one question about that and --

20 THE COURT: All right.

21 MR. CLAYMAN: -- and it has nothing to do with the
22 actual costing.

23 THE COURT: All right. Well, I -- I think we've
24 got two objections. One is costing. I -- I think we're
25 okay on costing so I'll allow it on costing.

1 The second, I think, is that we're getting into
2 what was earlier objected to in terms of the more recent
3 negotiations. But I'll -- I'll allow a question or two and
4 --

5 MR. CLAYMAN: Okay.

6 THE COURT: -- see where it goes.

7 MR. CLAYMAN: Okay.

8 BY MR. CLAYMAN:

9 Q And just -- you have done the same thing for the --
10 what's been referred to as the ARP group?

11 A Yes. The agents', representatives, and planners.

12 Q Okay. And you have a term sheet that you have
13 published that covers -- will cover them?

14 A We have not published a term sheet. We've put out a
15 series of information packets that describe the changes that
16 will be made to the employment conditions for those folks so
17 that they, too, can meet their twenty percent objective.

18 Q But you have not put up or posted anywhere for the
19 union's to see what the valuations of the changes that you
20 intend to impose on those two groups are?

21 A I think we've been public about the total amount and I
22 think we have published that.

23 Q You have published the savings that you will realize
24 from each of the changes that you have proposed to those two
25 groups?

1 A I -- I'm not aware of an item by item representation.

2 Q But there -- there is an item by item representation on
3 the union term sheets, correct?

4 A Because they're subject to negotiation, as you
5 described earlier, and that's a significant part of reaching
6 agreement there -- there are. What we've done in occasion
7 -- in the case of the agent's reps and planners and the
8 management team has -- we've announced the changes that we
9 will make and we've announced that the -- the total savings
10 associated with those term sheets, and been pretty public
11 about the changes.

12 Q Now could you just briefly describe what furlough pay
13 is and what -- how -- how that comes about, just --

14 A Well --

15 Q -- very briefly?

16 A -- many collective bargaining agreements have an amount
17 of compensation that's paid to an individual when the person
18 is furloughed from their position. As you know, in -- in
19 our agreements when you're laid off, furloughed, you usually
20 have recall rights. And so someone with recall rights would
21 -- would -- because we no longer need their services based
22 on the needs of the service they would be furloughed and we
23 would pay them up -- the specified amount in the agreement.

24 Q Are you aware that for most of the contracts, or at
25 least I think the mechanics and possibly the pilots, that

1 the maximum furlough pay is about thirteen weeks?

2 MR. MOLLEN: Your Honor, I object. This isn't in
3 Mr. Brundage's declaration. It's beyond the scope of the
4 direct. I mean, I --

5 MR. CLAYMAN: This goes to fair and equitably,
6 Your Honor.

7 MR. MOLLEN: But --

8 MR. CLAYMAN: If I could just close --

9 THE COURT: Yeah. But --

10 MR. CLAYMAN: -- the loop.

11 THE COURT: But you're closing the loop on
12 something he hasn't offered any testimony about. So, again,
13 raising the scope of the direct issue is sort of a double-
14 edge sword. Sometimes parties just sort of let it all go
15 and say, it's not worth it. Other times they raise it, and
16 -- and, legitimately so, in this instance because you didn't
17 know what the direct was going to be. But having raised it,
18 we're -- we're now sort of -- we've all decided to take a
19 collective look at the issue and - and we're sort of stuck
20 with it.

21 So this does seem to be beyond what he was
22 proffered for, both in his declaration as -- as well as his
23 --

24 MR. CLAYMAN: Right. But can I --

25 THE COURT: -- oral direct. So --

1 MR. CLAYMAN: Yeah. Well, I think that a major
2 part of our thrust of Mr. Brundage's testimony is to
3 demonstrate that the changes that have been proposed to the
4 unions have been done in a fair and equitable matter and
5 that they have been -- accordingly, have been costed in a
6 fair and equitable manner as well.

7 And that's all I'm trying to get to. I can do
8 that in about three questions.

9 THE COURT: All right. Well, I do think that that
10 is the subject of his direct, starting at Page 14. So --
11 and to the extent it's a top level view I'll -- I'll allow a
12 few questions on that.

13 MR. CLAYMAN: Yeah.

14 BY MR. CLAYMAN:

15 Q And I think, just to cut to the chase here a little
16 bit, virtually all of the work groups -- I think all of the
17 work groups will suffer furloughs. Is that --

18 A That's correct.

19 Q Okay. And isn't it not true that the only contract
20 that does not have furlough pay is the flight attendant
21 agreement?

22 A That's correct. And I think we discussed it earlier
23 today. We did not specify the types of changes that would
24 be required from --

25 Q Yes.

1 A -- the unions to meet the objective in 2003, and the
2 flight attendant group at that time chose -- choose to
3 eliminate furlough pay in their agreement. It was actually
4 the flight attendants proposal to the company to eliminate
5 that compensation so that they could achieve their target.

6 Q Okay. Okay. And what I would like to know is isn't it
7 true that in costing out your proposals and knowing that
8 certain of the productivity changes will result in
9 employee's being furloughed and receiving furlough pay, that
10 you did not credit the cost of the furlough pay against the
11 total savings of the term sheet?

12 A The contracts are each individual contracts. They have
13 a large number of terms that role up to a cost. We looked
14 at the cost of the contracts and then we proposed to changes
15 to those contracts to be able to achieve the savings we
16 needed to achieve.

17 In the case of our -- if one of our other unions
18 had chosen in this round to suggest that they did not want
19 furlough pay as -- in terms of any layoffs associated with
20 what we're doing, then, of course, we would have credited
21 that savings because the company intended to save that.
22 It's just like pay. I mean, we have a -- we have -- we have
23 compensation that we pay.

24 Q All right.

25 A And that's a creature of the contract. And if you

1 reduce the amount of compensation that you want to take,
2 that's a savings.

3 Q I understand. And I'm just trying to clarify for the
4 record, and I -- whether or not in adding up the total
5 savings, if there were furloughs that the furlough pay that
6 would result from that, whatever the amount was,
7 credited against the savings. So, for example, if it were
8 20 million, in the case of an ask of 200, that -- that did
9 not reduce the savings to 180? That's what I'm trying to
10 get et at?

11 A Well, we've been here a couple of times before. My
12 understanding and what I've tried to testify to is that we
13 proposed a certain amount of savings to each union that we
14 needed -- that we -- that we believed were fair and
15 equitable that we needed to restructure. And we then began
16 the process of any changes that the union made to its work
17 rules or its compensation in the 1.25, to reach that goal we
18 would give them credit for.

19 Q I understand. I -- I still don't think you've answered
20 the question, but I'll move on.

21 Let me just wrap up on the -- on the issue of the
22 one-and-a--quarter-billion-dollar number. When did you
23 first see that number?

24 A Oh, I think it would have been sometime in early
25 January, thereabouts, mid-January.

1 Q But isn't it true that the business plan was not
2 finalized until the end of January?

3 A Yes. And there was -- as Mr. Dichter testified to in
4 his and Ms. Goulet testified, too, it's a very iterative
5 process, and over time people were constantly making changes
6 to the plan, those kinds of things. But we started to see
7 the labor number in the midst of confirming that the plan
8 actually -- that all the pieces tied together, that it all
9 checked out.

10 Q But the number that you saw at the beginning of January
11 turned out to be the same number at the of January, yes or
12 no?

13 A Yes. Yes.

14 Q Okay. Now you mentioned during your direct examination
15 that you are responsible for employees in Mexico, Latin
16 America and the Caribbean?

17 A The collective bargaining in those countries.

18 Q Okay.

19 A And -- but I have a direct report who is responsible
20 for --

21 Q And how many --

22 A -- that work.

23 Q -- collective bargaining agreements are there in those
24 countries?

25 A About twenty.

1 Q About twenty?

2 A Yeah.

3 Q Have you talked to any of those unions in those
4 countries about --

5 MR. MOLLEN: Your Honor, I'm going to object on
6 the grounds of relevance. This has nothing to do with the
7 1113 trial.

8 MR. CLAYMAN: If I could ask the question it would
9 help, I think, in terms of --

10 THE COURT: Well --

11 MR. CLAYMAN: -- relevance.

12 THE COURT: -- I think he knows what the topic is.
13 So explain to me the relevance -- is this in the direct
14 testimony, remind me, or -- or --

15 MR. CLAYMAN: It goes -- again, Your Honor, it's
16 -- let me finish the question, if I may? The question is
17 simply, in those countries have you tried to seek changes
18 consistent with the changes that you're seeking in the
19 United States.

20 MR. MOLLEN: Same objection, Your Honor.

21 MR. CLAYMAN: This is supposed to be under fair
22 and equitable, Your Honor, and if there are employees of
23 American who are escaping unscathed, then it really goes to
24 the issue of whether or not they can satisfy the fair and
25 equitable standard.

1 THE COURT: Why is that not relevant?

2 MR. MOLLEN: Your Honor, it's just simply legally
3 irrelevant to the scope of Section 1113. The Railway Labor
4 Act in Section 1113 doesn't apply to employees that don't
5 work in this country. Mr. Brundage's direct testimony --

6 THE COURT: All right. Well --

7 MR. MOLLEN: -- has nothing to do with --

8 THE COURT: All right. Well, we -- you can make
9 that legal argument, but for purposes of -- of moving this
10 along I'll let -- I'll let the facts come in and --

11 MR. MOLLEN: Thank you, Your Honor.

12 THE COURT: -- we'll -- we'll take it from there.

13 So if you remember the question --

14 THE WITNESS: I do.

15 THE COURT: All right.

16 THE WITNESS: I do. I was listening carefully.

17 The -- each country has what I would describe as
18 dramatically different labor laws than the U.S., and in many
19 of those countries employees have acquired rights. There's
20 actually no legal ability to reduce their incomes. What we
21 have done is for each and every -- we've -- we have scoured
22 every opportunity to make whatever changes are legally
23 available to us in each of those separate countries.

24 So whether it was Peru or Columbia or whether we
25 were in Brazil, wherever we have employees and we have union

1 groups, we've looked at what the local laws allow us to do
2 and we've made our very best effort to make cost reductions.
3 In some cases, we've been able to negotiate with unions to
4 significantly reduce, for instance, the payments that are
5 required due to inflation. We have no ability to take and
6 extend the 1113 process to those employees, but we've been
7 very diligent, and as well as employees in Europe to do the
8 exact same thing. Even though they are not covered by this
9 process, we're very focused on understanding that what this
10 is really about is getting the company successfully
11 restructured in a way to preserve all these jobs.

12 So we're -- we're making every effort we can,
13 whether it's in 1113 or any other way the company can to get
14 to the point where we can do that.

15 BY MR. CLAYMAN:

16 Q And are those discussions ongoing with some of those
17 countries?

18 A Constantly, yes. In fact, those negotiations are
19 sometimes very short duration contracts. They may come open
20 as often as annually or semi-annually in some cases and each
21 time we have an opportunity to try to reduce costs we do it,
22 and we've had some success.

23 Q Is that something that you did prior to the bankruptcy?

24 A Not with the focus -- we -- we tended, prior to the
25 bankruptcy, to do, quite frankly, what was necessary to keep

1 the employees satisfied working on side.

2 Q I think I just have two other questions, Mr. Brundage.

3 You had mentioned that the approach that the
4 company was taking prepetition was referred to as the limp
5 along strategy and kick the can strategy. Is that right?

6 A I actually didn't coin it. I described how it's been
7 described in this trial.

8 Q Well, with -- were those terms that were used prior to
9 the bankruptcy filing?

10 A They -- yes, they were. They were shorthand terms to
11 describe some of the discussions we were having about what
12 the art of the possible was to make changes that would
13 facilitate achieving the goals that my team was charged with
14 trying to achieve.

15 Q And were that -- was that phrase or those phrases ever
16 mentioned before the board of directors of American or AMR?

17 A Unfortunately, I probably did do that, which was to my
18 detriment.

19 Q Do you remember if you were the only person who ever
20 said -- you used those phrases before the board?

21 A I absolutely did.

22 Q But you were the only person who did?

23 A No. I'm not sure that's the case.

24 Q Okay. When you mentioned that United and I believe you
25 said one other airline, I think, was it Northwest, maybe it

1 was Delta, used the same methodology that you're using for
2 allocating the costs --

3 A Well, I --

4 Q -- for the savings?

5 A -- I reviewed their court papers and I have a note that
6 I can read, but I actually took that right out of the papers
7 that I read that described their process.

8 Q But do you have any idea in -- in either of those cases
9 what the relative position of -- in the case of United of
10 the various unions were to the marketplace when that across
11 the board change was made?

12 A At -- at the risk of a little supposition because --

13 Q Well, no. I don't --

14 A -- United had been through a number of rounds with its
15 employees before it got to its final 1113 round, I'm
16 assuming that some of the leveling, some of the homogenizing
17 of the positions of the various employee groups took place
18 during that process --

19 Q So that if they applied --

20 A -- because --

21 Q -- an even amount or allocated the same percentage,
22 then -- then it would not disturb the relative position of
23 each of those unions --

24 A Yeah.

25 Q -- to the -- to their peers at other airlines?

1 A Very similar to what I described in our circumstance
2 between 2003 and this proceeding.

3 Q Okay.

4 MR. CLAYMAN: Thank you, Mr. Brundage.

5 THE WITNESS: Thanks.

6 MR. MOLLEN: I have no redirect, Your Honor. But
7 I do want to move Mr. Brundage's declaration, which is
8 Exhibit 500, and the exhibits to his declaration, which are
9 501 through 509 into evidence.

10 THE COURT: All right. Any objection?

11 MS. LEVINE: No objection, Your Honor. But
12 pursuant to our stipulation we reserve our rights to assert
13 objections if and when they become appropriate.

14 THE COURT: Say that last part again. Objections?

15 MS. LEVINE: We just reserve our rights to assert
16 objections if and when it becomes necessary or appropriate.

17 THE COURT: You -- you're going to have to uncode
18 that for me. I'm not -- I'm not -- you're probably
19 addressing something specific of -- of the many --

20 MS. LEVINE: Your Honor, we -- we've -- per
21 discussions with the company, to the extent it becomes
22 necessary, they've agreed to produce Mr. Brundage after we
23 put in our direct case for cross-examination. And at that
24 time, if that becomes necessary, we would also reserve our
25 right to assert objections with evidentiary --

1 THE COURT: All right.

2 MR. MOLLEN: That's right, Your Honor.

3 THE COURT: This goes to, essentially, your unique
4 procedural posture. All right. I'm -- I'm losing track of
5 the different sort of things we've put a pin in in this
6 proceeding, so I wanted to make sure that that was not
7 something -- something brought in that --

8 MS. LEVINE: Nothing new.

9 THE COURT: Okay. Thank you.

10 MR. MOLLEN: I inadvertently preempted Mr. Butler
11 in --

12 MR. BUTLER: No worries. I just wanted to say
13 again, Your Honor, on behalf of the creditors' committee
14 that we have no cross-examination of Mr. Brundage.

15 THE COURT: All right.

16 All right. Mr. Brundage, you are free to go.

17 THE WITNESS: Thank you.

18 THE COURT: And I will accept his direct
19 testimony, much discussed scope of which is in Exhibit 500,
20 and then the other accompanying exhibits in this binder to
21 which his direct testimony relates.

22 (Debtors' Exhibit Numbers 500-509 were admitted)

23 THE COURT: All right.

24 MR. GALLAGHER: At this point, Your Honor, the
25 debtor would call Brian McMenamy to the witness stand.

1 (Pause)

2 THE COURT: If you would swear the witness.

3 THE CLERK: Can you please raise your right hand?

4 (Witness Sworn)

5 THE COURT: Can you please state and spell your
6 name for the record?

7 THE WITNESS: Brian McMenemy, Brian is with an I,
8 McMenemy is -M-C-M-E-N-A-M-Y.

9 MR. GALLAGHER: For the record, Your Honor, Jack
10 Gallagher from Paul Hastings for American Airlines.

11 I regret to report, Your Honor, that I have to
12 begin this discussion with a correction. I was informed
13 this afternoon that in the course of reviewing Mr.
14 McMenemy's testimony Towers Watson discovered an error in
15 one of their calculations and they have, within the past
16 hour, I've had hand-delivered to me a correction page. And
17 I apologize to the Court and I apologize to all counsel for
18 the fact that this is necessary. But I will, with your
19 permission --

20 THE COURT: Absolutely.

21 MR. GALLAGHER: -- distribute that correction and
22 then call attention on the record to where the changes are.

23 THE COURT: Thank you.

24 MR. FLICKER: Your Honor, Scott Flicker for the
25 debtor. I will note that this exhibit has been, I believe,

1 filed under seal. So we would like to make sure that those
2 who get a copy of it are all in the protective order and we
3 will, of course, file in the public record a redaction to
4 indicate that that's the case.

5 THE COURT: All right. Now is the correction to
6 confidential information or public information?

7 MR. GALLAGHER: It is to confidential information,
8 Your Honor.

9 THE COURT: All right.

10 MR. GALLAGHER: But I can, I think, describe the
11 changes on the record without indicating -- without
12 breaching confidence.

13 If everyone can take the original exhibit side by
14 side with the new exhibit, the new exhibit will be marked
15 for identification, Your Honor, as American Exhibit 703-C;
16 that is, that was the same as the old exhibit, and this will
17 have an A -- dash A behind it. So this is -- the amended
18 703 -- Exhibit 703-C.

19 And I will call everyone's attention -- the
20 changes are all in one column, Your Honor, and --

21 THE COURT: All right.

22 MR. GALLAGHER: -- that is the first column, the
23 2012 column. And the changes are in the -- under pilots in
24 the second line.

25 THE COURT: All right. I see that.

1 MR. GALLAGHER: In the third line.

2 THE COURT: I see that.

3 MR. GALLAGHER: And that's all under pilots.

4 Under AMS, which is the management and non-union
5 DB plan, it is only in the second line.

6 THE COURT: All right.

7 MR. GALLAGHER: Under the TWU, it is in the third
8 line -- excuse me -- the second line.

9 THE COURT: Second line. All right.

10 MR. GALLAGHER: Second line.

11 THE COURT: I see that.

12 MR. GALLAGHER: Under flight attendants it is in
13 the second line.

14 THE COURT: All right.

15 MR. GALLAGHER: And under total it is in the
16 second line and the third line.

17 THE COURT: All right.

18 MR. GALLAGHER: So I do apologize for those
19 corrections, Your Honor. They do come from Towers Watson.

20 And I would note that we had hoped to finish Mr.
21 McMenemy's cross-examination tonight, but if these changes
22 require further time for counsel we will understand and he
23 will be available for consideration tomorrow.

24 THE COURT: All right.

25 Thank you.

1 DIRECT EXAMINATION

2 BY MR. GALLAGHER:

3 Q Mr. McMenemy, welcome.

4 A Thank you.

5 Q What is your position with American Airlines?

6 A I'm the vice-president and comptroller for American.

7 Q And how long have you held that position?

8 A For six years.

9 Q All right. And what department is that position in?

10 A It is in the finance department, reporting to the CFO,
11 Bella Gordon -- Goren.

12 Q Okay. And how long have you been with American
13 Airlines?

14 A It will be twenty-eight years in July.

15 Q And what other positions have you held with American
16 since joining the company?

17 A I joined the company as an entry-level financial
18 analyst in the finance department and have rotated through
19 various positions all in finance for most of my career.
20 More recently, rather than go through them all, I was senior
21 vice-president of finance for our TWA, LLC unit after we
22 acquired them early in the decade in St. Louis, then back in
23 Dallas I was director of financial planning, director of
24 airline profitability and financial analysis, and then most
25 recently my current position.

1 Q All right. Do you have an MBA or a CPA?

2 A I do. I have both.

3 Q Okay. Would you describe your responsibilities as
4 vice-president and comptroller of American? And I presume
5 is it also AMR Corporation?

6 A Yes, it is.

7 Q Okay.

8 A Well, I shouldn't say -- it's of American Airlines.
9 I'm not quite sure legally if there is a different
10 designation for AMR.

11 As -- in the current position as a vice-president
12 and the comptroller, the comptroller shop has all of the
13 accounting functions for American Airlines and AMR, and the
14 financial planning and analysis function for the airline and
15 AMR and in the financial analysis function we do the -- we
16 support the employer relations group in pricing out and
17 valuing different labor measures and actions.

18 Q Does the accounting function include financial
19 reported?

20 A It does, all the external financial reporting and
21 internal.

22 Q And does that include SEC reports?

23 A Yes, it does.

24 Q And are those audited financial reports?

25 A Yes, they are.

1 Q And are they subject to Sarbanes-Oxley requirements for
2 the verification by senior executives of the accuracy of the
3 reports?

4 A Yes, they are.

5 Q All right. And does the financial planning and
6 analysis function include the annual budgeting of the
7 airline?

8 A Yes, it does.

9 Q All right.

10 A Yeah. We do all the budgeting function.

11 Q There's been discussion here and in your declaration
12 about financial briefings, periodic financial briefings by
13 American for its unions. Are you familiar with that subject
14 matter?

15 A Yes, I am.

16 Q Does American provide financial information to its
17 unions periodically?

18 A We do. Every months since earlier in the decade we
19 meet with the labor groups, whoever wants to attend,
20 advisors or members of the union to review our financial
21 results. It's the same deck that we present to the board
22 every month that reviews our results for the prior month or
23 prior quarter and then has an outlook for the -- for the
24 remainder of the quarter or the next quarter.

25 Q And what role do you play in that process?

1 A I present to the groups.

2 Q and -- and when you talked about a deck, is that a
3 PowerPoint presentation?

4 A Yes. It's the power -- it's the board PowerPoint
5 presentation. Correct.

6 Q The same presentation that you give to your board of
7 directors?

8 A Yes, it is.

9 Q All right. And is there -- is it simply -- do you
10 simply hand them the deck or is there discussion or dialogue
11 about them?

12 A No. There -- it depends on the month. But there's
13 usually quite a bit of discussion.

14 Q All right.

15 A Correct. And we -- it is -- we pass it around in hard
16 copy.

17 Q And do union financial -- or union financial advisors
18 welcome to attend?

19 A Yes. Yes.

20 Q And when was the most recent of those meetings?

21 A Last week.

22 Q Does -- has your CEO ever attended?

23 A No.

24 Q Okay. Is the CEO involved in the information sharing
25 process?

1 A Yeah. I was -- I was going to, I guess, add to that.
2 He doesn't attend. There is a financial briefing, then
3 following the financial briefing, usually the next hour or
4 sometimes it will be a day or two later, there's what we
5 have called a national joint leadership team meeting where
6 Gerard Arpi, our former CEO -- I'm less familiar if Tom
7 Horton has been doing it just recently -- would meet with,
8 again, at this point all of, again, the -- each of the labor
9 groups. This would usually be the president of the labor
10 union or their vice-president position, and they would meet
11 with Gerard and open invitation extension and some of the
12 other senior officers just depending on the topics that they
13 were going to chat about.

14 Q Okay. And now what role does your department play in
15 labor contract negotiations?

16 A We support the employer relations group in -- in the
17 negotiations, particularly in pricing and valuing different,
18 you know, contractual changes that -- that we may want to
19 visit.

20 Q And do you do that all yourself?

21 A No, I do not.

22 Q Okay.

23 A My -- my staff does it.

24 Q And what -- how many -- what kind of staff, how many
25 people is involved to -- or assigned to perform those tasks?

1 A Well, in this -- the -- for this negotiation, again,
2 it's all groups at once, so a little more intense than --
3 than the Section 6, but we have -- for each we have our
4 director of financial planning and analysis, who is on site
5 most of the time with the labor groups and the labor teams,
6 and then each labor team is assigned a level 5 manager and
7 -- or a manager for the company and an analyst for the
8 company that helps support that team. So they're there kind
9 of -- they're on the negotiating team and -- and on site.

10 For the TWU, we have two analysts under the
11 manager just because there are the two large agreements and
12 the five smaller ones.

13 Q All right. So in your -- your people on your staff are
14 members of the company negotiating committee to assist in
15 the financial analysis of the issues under discussion?

16 A Correct.

17 Q All right. Now you submitted a written declaration in
18 this case which is American Airlines Exhibit 700. Is that
19 correct?

20 A Correct.

21 Q And you also proffered American Exhibit 701 through
22 708; is that correct?

23 A Yes, it is.

24 Q And those consist largely of inputs from outside
25 consultants at Towers Watson and Mercer Health Advisors,

1 LLC; is that correct?

2 A That is correct.

3 Q And do you adopt and incorporate your declaration and
4 exhibits as if you testified to them fully here today?

5 A Yes, I do.

6 Q All right. I'm going to ask you briefly about some of
7 those. Before I do, though, I want to ask you ten years ago
8 how many people were working in the department you now head?

9 A I would say approximately 600.

10 Q And how many are working in your department today?

11 A Approximately 350.

12 Q And those are all management personnel?

13 A Management and support staff.

14 Q All right. What happened to all of the jobs that are
15 no longer there?

16 A Well, a fair amount were removed to outsource some
17 functions so we outsourced some functions to Juarez, Mexico,
18 to India, and to Fiji, and those positions went away. And
19 then others were, through reductions, continually trying to
20 become more efficient. Automatization helps play a big role
21 in the shop at times. So any time we could -- could become
22 more efficient through a system or otherwise make a process
23 more efficient.

24 Q Beyond job reductions initiated by the company in your
25 department, have you had any significant attrition in your

1 department over the last twelve months?

2 A We have, particularly recently.

3 Q And do people tell you why they're leaving?

4 A Generally, something to do with more pay and less work.
5 But, you know, imagine that.

6 Q Do you have an understanding as to whether your pay for
7 the people in your department is competitive with the job
8 market?

9 A Well, no. I mean, I have -- in -- in my job with the
10 different evaluations I -- we do and I have, with human
11 resources, it tends to run some of the benchmarks and I -- I
12 see those, and our management team is generally below market
13 or is below market in compensation, both excluding any cash
14 incentive and excluding that.

15 Q All right. If -- may I ask you to take a look at
16 Company Exhibit 701? Can you identify this document?

17 A Yes, I can. This is a document that we walked through
18 on February 2nd, so the day after the 1113 process launch on
19 February 1. The next day we met with each of the labor
20 groups, each of the unions and their advisors and walked
21 them through this document which is an explanation, still
22 it's somewhat of a high level, but some of the consistent
23 themes and approaches we take to -- to costing out and
24 valuing the different potential changes that we were going
25 to talk about.

1 Q And when you say "walk through," Mr. McMenemy, does --
2 do you mean that someone gave a presentation of this
3 document?

4 A Yes. I gave the present -- I walked through and gave
5 the presentation.

6 Q And were all of the union leaders and their financial
7 advisors invited to attend?

8 A Yes.

9 Q And did they attend?

10 A To my knowledge, yes.

11 Q Okay. And what was the purpose of giving this
12 presentation?

13 A This was a lead-in presentation. Following this
14 meeting each labor group, we then broke out into the
15 subgroups, each labor group independently to walk through
16 their specific term sheet and their specific valuation of
17 those terms. So we have kind of a summary valuation of all
18 the elements, and then the detail behind those; the
19 spreadsheet that supports each line on that summary term
20 sheet. And this was the lead in presentation to say, it
21 varies by work group, but this is how we will approach an
22 outsourcing measure, or this is how we will approach a
23 change in pensions, or this is how we will approach a change
24 in active medical.

25 Q And when you say approach you mean for purposes of

1 financial -- financial valuation or costing?

2 A Correct. For the valuation of those measures.

3 Q All right. So your presentation was about the subject
4 of costing methodology?

5 A Correct.

6 Q Only. Not -- you were not explaining the terms, just
7 the valuations?

8 A That is correct.

9 Q And I presume the employee relations negotiators had
10 already exchanged term sheets and explained terms -- or
11 explained the -- the nature of the proposals?

12 A Right. I believe I am forgetting now. My -- I think
13 it was right after this meeting where we actually presented
14 them with the -- with the written term sheets, here's the
15 terms and the description of what we're changing, but it
16 might have been the day before, I believe it was after this.

17 Q February 1 was --

18 A Was it?

19 Q -- opening day for the business plan and the proposals.
20 Does that sound right to you?

21 A Correct, yes, it is. Yes, it was, right.

22 Q And then this presentation, as I understand it,
23 followed the next day; is that --

24 A That's right.

25 Q Okay.

1 A Uh-huh.

2 Q If you would turn the page 6 of this presentation on
3 costing methodology, and let me ask you to briefly what's
4 set forth here.

5 A Uh-huh. This talks a little bit to the -- to the
6 modeling, most of it Excel based, that we establish and use
7 for all work groups, management, each of the organized
8 groups, and the agents, and representatives -- the non-
9 organized groups, and at the -- for each work group
10 similarly we use the exact same kind of -- we use the exact
11 same Excel model, which has heads by level of seniority for
12 that work group and average compensation for that level of
13 seniority and average benefits cost by element of benefits
14 cost for that work group, and then it talks to individual
15 measures that we make changes to. There may be an Excel
16 base spreadsheet that calculates that impact in head count,
17 but that then feeds back into the kind of core model we have
18 that is heads by level of seniority and pay rate and
19 calculates through the impact of that head count change.

20 Q Okay. Well, you're obviously very familiar with this,
21 Mr. McMenamy, but I want to go back over it a little bit so
22 that I can understand it.

23 When you talked about head count I take it that
24 means people?

25 A Correct.

1 Q And so the -- you have a -- this is a -- we're talking
2 about at computer model, correct?

3 A Yes. Yes.

4 Q And this computer model already has in it the actual
5 number of people that you have in each job class?

6 A Right.

7 Q And --

8 A Correct.

9 Q -- it actually has their actually seniority
10 distribution?

11 A Correct, right.

12 Q And I presume then that changes every year?

13 A It does change every year. As people move through
14 different seniority steps you're going to get different
15 impacts on your overall cost of the work group over time.

16 The -- the model for flight attendants and TWU a
17 little less complicated because their compensation is -- is
18 not impacted like pilots, where they are impacted by bid
19 statuses, which is there's a different pay rate for each
20 aircraft type and whether they're sitting in the captain or
21 the first officer seat and whether it's domestic or
22 international. So that model is more robust, just required
23 to have more cells in it.

24 Q But a flight attendant is paid the same thing as
25 another flight attendant at the same level of seniority

1 without regard to what airplane they fly?

2 A Correct.

3 Q Except if it's international and then there's some
4 differentials?

5 A Right. Right.

6 Q All right. So is it one labor model or is it a
7 separate labor model for each union group and each -- and
8 non-union group?

9 A Yeah, it's the same model for each group. I mean it's
10 a separate Excel spreadsheet, if you will, pretty big Excel
11 model, but it's the same model for every work group.

12 Q And that's the labor cost model, if I can call it that?

13 A Correct.

14 Q All right. And there's been other testimony in this
15 proceeding about the business plan model that American has.
16 Are you familiar with that term?

17 A I am.

18 Q And is the labor cost model one of the inputs to the
19 business plan model?

20 A Yes. For -- for the restructuring we will take the
21 value of any changes and feed it back into the business plan
22 model so then it has the value of those changes.

23 Q All right. Now this modeling -- this costing
24 methodology and model, is that the same costing methodology
25 and model that American Airlines uses for all purposes?

1 A It is.

2 Q All right. So that methodology and model is used for
3 internal analysis?

4 A It is used to internal analysis and it's what we use
5 through Section 6 negotiations, and we've used it for many
6 years.

7 Q So you use the same data and sources and methods for
8 reports to senior management?

9 A Correct.

10 Q Okay. And you used it during the Section 6 bargaining
11 since 2006 with the pilots and 2008 with the other unions?

12 A We have.

13 Q All right. You don't have a separate model or separate
14 methods for evaluating union proposals do you? Or do you?

15 A No, we do not.

16 Q All right. Is the model perfect?

17 A No.

18 Q Okay.

19 A The people running it may it -- no, never mind.

20 (Laughter)

21 Q If you become aware of an error or an imperfection or
22 something that can be improved in the model what do you do?

23 A Certainly, we fix it. I mine we're always trying to
24 may as well improve it, make it better, and you know, active
25 discussion on the right inputs to the model.

1 Q Okay. Now on page 5 of this presentation, company
2 Exhibit 701, you talk about having prepared for each
3 contract group a summary page of the proposed changes and
4 the detailed spreadsheets. And did your staff prepare
5 those?

6 A We did.

7 Q And you gave them out to the unions that day?

8 A We did, yes. Following this meeting they broke out and
9 reviewed those spreadsheets.

10 Q And they were posted on IntraLink?

11 A And then posted on IntraLinks.

12 Q And what is IntraLink?

13 A It is a site hosted by Weil -- I believe by Weil,
14 Gotshal, correct me if I'm wrong -- but where we've posted
15 all it will document, all the data requests of all the work
16 groups through this whole process.

17 Q All right.

18 MR. GALLAGHER: Your Honor, the exhibit -- all of
19 those price outs are -- have been offered in the company's
20 direct case. I can identify the exhibit numbers if Your
21 Honor would be interested in that, but they are attached to
22 the various declarations about the collective bargaining
23 process.

24 THE COURT: As it might be helpful to have that
25 list in one place if you wouldn't mind, if it's not going to

1 be too time consuming.

2 MR. GALLAGHER: No, I have it right here, Your
3 Honor.

4 THE COURT: All right.

5 MR. GALLAGHER: For the pilots the cost out of the
6 company's opening proposal is Exhibit 914.

7 For the flight attendants the cost out of the
8 company's opening proposal is American Exhibit 1026.

9 For the TWU fleet service it's American
10 Exhibit 1130.

11 For the TWU dispatchers it's American
12 Exhibit 1131.

13 For the TWU simulator technicians it's American
14 Exhibit 1132.

15 For the TWU instructors it's American
16 Exhibit 1133.

17 For the TWU mechanics and related it's American
18 Exhibit 1205.

19 For the TWU stores employees it's American
20 Exhibit 1206.

21 And for the TWU maintenance control technicians
22 it's American Exhibit 1207.

23 And I believe the Court is maybe aware of this,
24 Your Honor, but with the TWU there are two very large
25 groups; the fleet service group who are the ramp workers and

1 baggage handlers, and the mechanics and related group. Both
2 of them have more than 10,000 members. There's the stores
3 group is the next largest at 1300. And all of the others
4 are much smaller, 1- or 200.

5 THE COURT: The first one you mentioned, I just
6 want to make sure I understand which -- mechanics is 1205
7 and the stores is 1206. The first group you said, which is
8 also more than 10,000, what --

9 MR. GALLAGHER: Is the fleet service, Your Honor,
10 the ramp and baggage handlers.

11 THE COURT: And that's at number?

12 MR. GALLAGHER: 1130.

13 THE COURT: Okay. Thank you.

14 BY MR. GALLAGHER:

15 Q Now, Mr. McMenemy, did -- has your office also priced
16 out the other American Airlines proposals made subsequent to
17 February 1st?

18 A Yes.

19 Q All right.

20 MR. GALLAGHER: I can also list those price outs
21 for Your Honor if you would like.

22 THE COURT: Yes.

23 MR. GALLAGHER: American's March 21st proposal to
24 the flight attendants, the price out is at American
25 Exhibit 919.

1 The company's price out of its March 22nd proposal
2 to the flight attendants is American Exhibit 1004. And
3 that's an important note, Your Honor, because in
4 Mr. McMenemy's declaration on page 7, footnote 2, contains
5 an error, it incorrectly identifies Exhibit 1030 as the --

6 THE COURT: Right.

7 MR. GALLAGHER: -- price out.

8 THE COURT: Where are you again?

9 MR. GALLAGHER: I'm in his declaration --

10 THE COURT: Right.

11 MR. GALLAGHER: -- at page 7, footnote 2.

12 THE COURT: All right.

13 MR. GALLAGHER: And the flight attendant price out
14 is not Exhibit 1030.

15 On the second entry on -- in footnote 2 --

16 THE COURT: All right.

17 MR. GALLAGHER: -- should be 1004, 1004.

18 THE COURT: All right. Thank you.

19 MR. GALLAGHER: I'm told that I misspoke, Your
20 Honor, I just want to make sure that I get it right.

21 The -- when I mentioned the March 21st price out,
22 which is American Exhibit 919 --

23 THE COURT: Right.

24 MR. GALLAGHER: -- that's for pilots.

25 THE COURT: That's what I had assumed.

1 MR. GALLAGHER: Okay. For the flight attendants,
2 March 22nd is 1004, as we just covered.

3 Now I can move through the fleet -- or the TWU
4 exhibits much more quickly.

5 The TWU fleet service the companies March 22nd
6 price out, the price out of its March 22nd proposal is
7 American Exhibit 1140.

8 THE COURT: All right.

9 MR. GALLAGHER: For the dispatchers American
10 Exhibit 1141, also March 20 -- all of the TWU price outs for
11 the second --

12 THE COURT: Are the 22nd.

13 MR. GALLAGHER: -- are March 22nd.

14 For the simulator technicians it's American
15 Exhibit 1143.

16 For the instructors it's American Exhibit 1142.

17 For the mechanics and related it's American
18 Exhibit 1212.

19 For the stores employees, also known as stock
20 clerks, it's American Exhibit 1213.

21 And for the maintenance control technicians it's
22 American Exhibit 1214.

23 THE COURT: All right.

24 BY MR. GALLAGHER:

25 Q One last series of questions, Mr. McMenamy, on

1 terminology.

2 Just for -- to clarify the record and for the
3 Court's understanding, I think there's some confusion in the
4 record about the types of financial reports that are
5 periodically circulated by your department -- prepared by
6 and circulated, so I want to clarify if I can.

7 Do you circulate monthly result reports of the
8 type that you present to the unions and to the board of
9 directors?

10 A Do we circulate?

11 Q Well, do you distribute to anyone the monthly financial
12 results that you give to the unions and the board of
13 directors?

14 A Yes. All the senior officers receive all those reports
15 as well, it's part of the board package.

16 Q And so that includes actual results for the preceding
17 month?

18 A Correct.

19 Q What else is in that package?

20 A It is our results for the prior month or the quarter to
21 date, if you're in the second month of the quarter, and then
22 an outlook for the remainder of the quarter, or for the next
23 quarter if they're in end of first quarter it will have
24 second quarter.

25 Q All right.

1 A If you're in April it'll have second quarter.

2 Q And is an outlook the same thing as a forecast?

3 A Yeah, forecast. We call it -- yeah, forecast, we call
4 it an outlook.

5 Q All right. And that includes projections -- actuals to
6 date plus projections for the remainder of that time period?

7 A Correct.

8 Q All right. Now are any of those documents or reports
9 -- financial reports, are they a business plan?

10 A No, not in what -- absolutely not.

11 Q Okay. Prior to the restructuring business plan what is
12 the last prior business plan that you're aware of?

13 A The last prior business plan that is similar to this
14 business plan was in the 2003 restructuring that I'm aware
15 of.

16 Q Okay. So other -- there have been very various
17 announcements of strategies or objectives since then as I
18 understand it; is that right?

19 A Yes, absolutely. But nothing -- you're realizing the
20 business plan is a very, very robust five and ten-year
21 outlook or forecast of the company that's exceptionally
22 robust for this purpose, and there's been nothing that
23 robust constructed in normal course.

24 MR. GALLAGHER: Thank you, I have no further
25 question, Your Honor.

1 THE COURT: All right. Cross?

2 MR. HARISTON: Good afternoon, Your Honor, Chuck
3 Hairston for the Allied Pilots Association.

4 THE COURT: Good afternoon.

5 CROSS-EXAMINATION

6 BY MR. HAIRSTON:

7 Q Mr. McMenemy, good afternoon, I'm glad that you got on
8 the stand.

9 Q I have a very focused cross-examination, and that is
10 going to deal with two things, your evaluations on the
11 proposed changes to the active medical, and your evaluations
12 on the proposed changes to future retiree medical and life.

13 And just to clarify that second piece again, we
14 are not talking at all in this proceeding about current
15 retirees, correct?

16 A Correct. Active employees, right.

17 Q So the valuations you did that I'm calling the
18 valuations for future retiree medical and life, those
19 concerned valuations based on what active employees would be
20 receiving as a future benefit, correct?

21 A That is correct.

22 Q Okay. Let's start in your declaration, if you could
23 turn to page 9, paragraph 22.

24 A Okay.

25 Q And that's in AA-700.

1 A Okay.

2 Q Now this chart is actually a reproduction, directly
3 underneath the paragraph at the top of the page, a
4 reproduction of AA Exhibit 705, correct?

5 A I'm sorry, say that again?

6 Q It's a reproduction of AA-705? Average annual cost
7 reductions --

8 A Yes.

9 Q -- from --

10 A Yes. Yeah, right. Right, correct.

11 Q Now this reflects in the left and center column the
12 active employee medical and then the retiree -- future
13 retiree medical and life, correct?

14 A That is correct.

15 Q And then it's broken out by employee group?

16 A Yes, it is.

17 Q There's pilots, flight attendants, TWU, ARP,
18 management, support staff, and then at the bottom there is a
19 total, correct?

20 A Yes, correct.

21 Q And that total for the active employee medical, the
22 first column on the left is 134 million, correct?

23 A That is right.

24 Q And then the next one for future retiree medical and
25 life is 151 million, correct?

1 A That is right.

2 Q This brings up an issue that I did want to touch base
3 with you on before we get too much further into this. We're
4 talking about numbers. Your declaration contains
5 confidential information, correct?

6 A It does.

7 Q I'm going to identify when I'm about to talk to you
8 about a number and I'm going to tell you whether in my
9 estimation it is confidential or not. If it is confidential
10 I'm not going to tell you the number, and I would ask you to
11 please not tell me the number, instead we're just going to
12 refer to it by its location in the relevant paragraph, okay?

13 A Okay.

14 Q If it is not confidential I'll go ahead and tell it to
15 you and you can respond in kind, okay?

16 A Okay.

17 THE COURT: And I would also ask both counsel and
18 the witness if for some reason you believe something is
19 confidential and you're afraid that maybe the parties aren't
20 on the same page don't be overly polite, just blurt it out.
21 We'd rather be safe than sorry.

22 MR. HAIRSTON: Understood, Your Honor.

23 THE COURT: Thank you. Proceed.

24 BY MR. HAIRSTON:

25 Q Now these projected cost reductions, what I'll call

1 savings, they are based on a comparison between the
2 proposals and existing book; is that correct? The status
3 quo?

4 A That is correct.

5 Q All right. Well, let's start with AA medical -- or
6 active medical. If you could look at paragraph 24, at the
7 bottom of the page, this paragraph contains two numbers,
8 both of which are confidential, so I'm not going to be
9 asking you to repeat those numbers and I'm not going to
10 repeat those numbers.

11 The first number, which is two lines up from the
12 bottom on page 9 in paragraph 24, that represents the
13 projected cost under the current plan design, head count,
14 and enrollment selections taking into account medical
15 inflation, correct?

16 A Yeah, I'm really -- again, make sure which number to
17 make sure I got the right -- I have the right number.

18 Yes, the second to the bottom line would be our
19 active medical cost over the six years.

20 Q And that's actually the second question I'm going to
21 ask you, but that is comparing it based on not the proposed
22 changes, but based on what is currently in effect, correct?

23 A Right, yes. It is -- that is right.

24 Q And that is a projection that was done by Mercer,
25 correct?

1 A That is right.

2 Q Okay. Now I did have one question for you about the
3 projection period, because in the line above where the
4 number is indicated it indicates that Mercer projected the
5 cost to American in the current plans for the years 2011
6 through 2018. Is that correct?

7 A I believe so. Yeah, I -- I can't actually say I've
8 ever counted up or focused on, gee, was there -- how many
9 years were in those columns as we did it, but --

10 Q Well the individual who had this responsibility was
11 Mr. Matthew Num (ph); is that right?

12 A That's correct.

13 Q And he works for Mercer, correct?

14 A Yes, that's right.

15 Q And he also has a declaration that is an exhibit to
16 your declaration, correct?

17 A He does.

18 Q Okay. Let's look at AA-704.

19 A Okay. 704?

20 Q 704. I'm going to direct you in AA-704 to paragraph 7
21 and specifically that first sentence which does not contain
22 any confidential information.

23 A Okay.

24 Q And if you could just please read that to yourself.

25 A Okay.

1 (Pause)

2 Q And let me know when you're finished.

3 (Pause)

4 A Okay, I'm finished.

5 Q Now after reviewing that would you agree that the
6 projection period is actually 2012 through 2018?

7 A So seven years. Yes, I would agree with that.

8 Q So with respect to the language in paragraph 24 at the
9 bottom of page 9 of your declaration, AA-700 that indicates
10 an eight-year period, 2011 through 2018, that is incorrect?

11 A Yes, there's a -- the two conflict, so assuming the
12 exhibit is right then -- and I would assume that's right,
13 but I can't be sure, but then -- then page 9 of my
14 declaration should actually be at 2012 through 2018.

15 Q Understood.

16 Now in the same paragraph turning to the next page
17 you see the second confidential number, that again I'm not
18 going to utter and I hope you do not. So now --

19 A All right.

20 Q -- we're at the top of page 10 in your declaration?

21 A Correct.

22 Q And that number as compared to the first number is
23 projecting the cost under the same what I'll call steady
24 state scenario but based on the proposed changes as opposed
25 to the current scenario; is that correct?

1 A I'll read to make sure that I've got the right number.
2 That is correct.

3 Q And again, the period there is also 2012 through 2018,
4 correct?

5 A That -- yes, it appears -- yes. If I went back to
6 exhibit -- okay, I believe that's right.

7 Q Now I'll note that at the end of that sentence with the
8 second confidential number there is a footnote, that is
9 footnote 3, which sites to AA Exhibit 704A and B. Do you
10 see that?

11 A I do.

12 Q Now we looked at 704, that was the declaration of
13 Mr. Num, correct?

14 A Yes, it was.

15 Q And 704A and B are exhibits to his declaration which is
16 an exhibit to your declaration, correct?

17 A Yes.

18 Q I don't have an interest in 704A, but I would like you
19 to look at 704B.

20 A Okay.

21 Q And let's start on the first page with the caption, and
22 again, this is not a confidential document.

23 AA Exhibit 704B, Mercer's actuarial assumptions.

24 So these would be the actual assumptions that Mercer used in
25 projecting the cost savings for 2012 through 2018?

1 A That's correct.

2 Q And that is on the active medical. We're still on
3 active medical, correct?

4 A That's right.

5 Q All right. If you could please look at paragraph 12,
6 which is on the second page of AA Exhibit 704B.

7 A Okay.

8 Q I'm going read you a sentence that is in the middle of
9 that paragraph, and what it says is, "No changes in
10 utilization are reflected in the plans." You see that?

11 A That is right.

12 Q Is that accurate?

13 A That is correct.

14 Q So the projected cost savings when comparing the status
15 quo to the proposed changes do not take into account any
16 reduction and use of the benefits or increase in the use of
17 the benefits, correct?

18 A That is right, yes.

19 Q Now do you know on the active medical piece what the
20 company is proposing?

21 A I do. I can't quote it by memory, but --

22 Q Sure. Well, aren't they proposing among other things
23 higher co-pays?

24 A We are. Yes.

25 Q Higher deductibles?

1 A Higher monthly contributions, higher co-pays, and
2 higher deductibles in general.

3 Q Now the net effect of those proposals, assuming they go
4 into effect, is going to be increasing the employees cost
5 share for the active medical benefit, correct?

6 A It will.

7 Q So the price for employees to use the benefit would go
8 up --

9 A Uh-huh.

10 Q -- but your valuation does not include anything that
11 would reflect a parallel reduction in use, correct?

12 A That's right. That's right.

13 And I will -- this particular -- and again, we do
14 rely on for many of the actuarial assumptions we rely on
15 Mercer to provide the numbers, but review them, we test
16 them, we kind of push them on different assumptions.

17 This is one that we happened to have discussed
18 with them in some detail, and you know, is in their
19 professional experience and what they've experienced with
20 other companies that have made these sorts of plan changes
21 and their estimation is that what you tend to see.

22 And so it made sense to us was initially there is
23 some change in utilization, then there's a catch-up period,
24 then you go back to steady state of about the same
25 utilization.

1 Because what happens is people -- they're sick
2 just as much, there's no change in how -- in their
3 occurrences of sick, they're going to use their medical plan
4 when they're sick, it will -- they'll have to be
5 contributing more, but it does not in the long run decrease
6 their utilization.

7 That was his -- from his experience and estimation
8 what Mercer sees.

9 Q And that's the explanation contained in the last
10 sentence there in -- or I guess second to last sentence in
11 paragraph 12? I'll read it to you.

12 "While utilization changes may occur, the
13 assumption is that modeling the increase in utilization
14 before plan changes than the decrease after the plan changes
15 followed by a higher than average trend would average it out
16 over the seven years versus assuming no change to
17 utilization or trend."

18 Correct?

19 A Correct.

20 Q All right. So essentially the theory is that even
21 though the trend is -- the trend of utilization is going up
22 -- well, the higher costs would be paralleled over the
23 period at issue with a trend of utilization that is actually
24 increasing?

25 A Right. I think -- I don't know quite as I read by what

1 he means before plan changes, other than we may get some
2 increases in utilization before the changes are effected to
3 try to beat the increase in deductibles or that sort of
4 thing, but I would be at that point -- he -- they wrote
5 this.

6 But after that it parallels what we discussed with
7 him, which was initially he would anticipate seeing a
8 decrease, followed by an increase as people catch back up,
9 and in the long run utilization is what it has been.

10 Q So higher costs on the individual lead to a utilization
11 trend that goes up?

12 A No, in the long run the same utilization.

13 Q And that's based on his anticipation that there would
14 be a spike before the plan changes were implemented?

15 A Well, we discussed no changes in utilization are
16 reflected in the claims, and that's what we have in the
17 modeling. So the numbers reflect no change in utilization.

18 And then I think in the next sentence he's
19 describing how he expects that to play out, which is he
20 expects that the assumption is that those claims may
21 increase before the plan changes, then decrease after the
22 plan changes, followed by a higher than average trend over
23 the six-year period would even itself out.

24 Q And that's what I'm speaking to is a higher than
25 average trend. That is a higher than average trend of

1 increasing utilization, correct?

2 A Yes, after the initial period, right.

3 Q That is paralleling a period when the costs have gone
4 up for the individual?

5 A Correct.

6 Q Now in the event Mercer or you had factored in a
7 decrease in utilization to go with the increased employee
8 cost share that would have an effect on the cost savings?

9 A Yes, it would. The utilization rate will impact the
10 cost savings.

11 Q And in fact if there is significant lower utilization
12 of the active medical benefit then in fact the cost savings
13 realized by AA could increase greatly, correct?

14 A There actually I'm not sure what -- how -- what would
15 you call significant and what would you call greatly, but it
16 would impact the cost savings. I don't have a good frame or
17 reference at hand on how sensitive that would be.

18 Q Well, let's look back in your declaration again, this
19 is AA-700, back at paragraph 25. Sir, you have another
20 chart. And this is a representation of AA-706; is that
21 correct?

22 A Correct.

23 Q And there are differences between this and AA-705 as
24 this breaks out the active medical as opposed to including
25 it in the chart with future retiree medical and life?

1 A That is right. That is right.

2 Q That chart shows 134 million and then it breaks it out
3 by work group, correct?

4 A That is right.

5 Q Now getting to 134- is not as simple as simply
6 subtracting the second confidential number in paragraph 24
7 from the first, correct?

8 A That is correct.

9 Q And that's because of a couple of different things.
10 First of all as it indicates in paragraph 25, AA-706, and
11 the average annual cost reductions contemplate a projection
12 period of 2012 through 2017 as opposed to 2012 through 2018,
13 correct?

14 A That is right.

15 Q So you knocked a year off, so that's going to change
16 it.

17 A Right. That's right.

18 Q Additionally in that second sentence you indicate that
19 you adjusted for head count changes anticipated by our labor
20 models; is that right?

21 A That's right.

22 Q So essentially not only is the projection period
23 different, be you also adjusted the cost savings based on
24 the company's evaluation of how many employees are going to
25 be using this benefit?

1 A We did, right.

2 Q And that is where you get the 134-?

3 A Yes.

4 Q Now that 134- just like Mercer's calculations would be
5 different in the event the calculation had included a
6 decrease in utilization, correct?

7 A Yes, a change in utilization will impact the number.

8 Q It'd be higher --

9 A Right.

10 Q -- if there was a decrease in utilization?

11 A Yes, correct.

12 Q All right. Let's look at the next topic.

13 Now we're on to future retiree medical and life
14 benefits. This is not Mercer, this the Towers Watson; is
15 that correct?

16 A Yes, it is.

17 Q So instead of Matthew Num we're dealing with Sandra
18 Loyal (ph); is that right?

19 A Yes, we are.

20 Q Okay. And Towers Watson was tasked with projecting the
21 future cost of providing current retiree medical and life
22 benefits to future retirees, correct?

23 A Yes.

24 Q Now there's no need to compare two numbers here because
25 the company's proposal is to eliminate this benefit,

1 correct?

2 A That is right.

3 Q So essentially the cost savings is going to be whatever
4 the current cost is?

5 A That's right.

6 Q Paragraph 26 has another confidential number there at
7 the end, and again, I'm not going to say it, please don't
8 you say it, but I do have a question about AA-703A, which is
9 cited at the end of that sentence.

10 A Uh-huh, okay.

11 Q It's also confidential, so we're not going to get into
12 the substance of that.

13 But just based on your index that document is the
14 American Airlines, Inc. all RPB's current plan contribution
15 projections. And I'm sorry, your index is on little ii?

16 A I believe -- I'm sorry, what did you say?

17 Q I was just directing you to where it is. Do you see
18 how it's described in your index?

19 A Right.

20 Q It's on little ii.

21 A Okay. I was just looking at the first page of 703A, I
22 believe is actually the pension contribution estimates, not
23 the retiree medical.

24 Q Well, that's my question. Is that a miscite? It
25 appears to be a pension document.

1 A Yeah, that is a -- that is a pension document.

2 Q Okay. So that figure that is cited there in
3 paragraph 26 is not supported by AA Exhibit 703A, correct?

4 A Yes.

5 Q Now we already identified Sandra Loyal, she was the
6 employee who work would you from Towers Watson, correct?

7 A Yes, she is.

8 Q And she has a declaration that is an exhibit to your
9 declaration, and that is AA-702. Could you please turn to
10 702?

11 A Okay.

12 Q I would like you to look at paragraph 9 in AA-702.

13 Now this paragraph also has confidential
14 information, and that confidential information is contained
15 in the second sentence of paragraph 9, and I will not be
16 reading you any portion of that, and I would not like you to
17 do that. I am however going to read you the first sentence
18 in paragraph 9, which is not confidential.

19 MR. FLICKER: I believe that's correct, but let me
20 double check. If you could ask the witness what the
21 discount rate is, it's public. I mean that's really the
22 question isn't it?

23 BY MR. HAIRSTON:

24 Q Is the discount rate public?

25 A I believe this is. This is a construct that is -- that

1 we use totally internally, not a -- so it -- it is public,
2 that's fine.

3 Q All right. I'm going to go ahead ask just read this to
4 you.

5 "In order to determine the employer liability
6 associated with providing retiree medical and life benefits
7 to future retirees, Towers Watson calculated for each group
8 the present value of the projected employer portion of the
9 medical and life claims, parentheses, which is net of the
10 present value of the current and projected future employer
11 prefunding contributions, close parentheses, based on an
12 eight and a quarter percentage discount rate."

13 Just to break that out a little bit, as far as the
14 parenthetical is concerned that is simply accounting for
15 assets that are already prefunded; is that correct?

16 A That's right. That's correct.

17 Q Not the pilot group, but some of the other groups --

18 A No --

19 Q -- have prefunding?

20 A That is right. That's right.

21 Q The discount rate -- just to make sure that I
22 understand what a discount rate is -- a discount rate is
23 needed in this case because we're trying to get a presently
24 value for a benefit that is a future benefit, correct?

25 A Uh-huh.

1 Q Which means American Airlines has not actually realized
2 any cost at this point, correct?

3 A Right. I should -- it may help to kind of explain --

4 Q Sure, by all means.

5 A -- the economic costing methodology that we use. It's
6 -- it is a construct that we worked or used with our -- with
7 the labor groups really since the 2003 restructuring, and we
8 use it only -- the labor target and all of the measures that
9 we will do to -- proposals to change anything in the
10 contract are all based on year one through six cash amounts,
11 except for two items. One being pension and the other being
12 retiree medical.

13 For those two items I'll particularly give retiree
14 medical and that's why we initially went to this construct,
15 when you're talking about changes to retiree medical for
16 active employees, not retirees, over the next six years most
17 of those benefits are going to occur well beyond the six-
18 year cycle.

19 And so you really are faced with what is the fair
20 representation and value to place on those changes for
21 active employees today. It would clearly value them very
22 low and isn't the correct value of that change in economic
23 terms the cash cost over the next six years.

24 Pensions, a little bit less dramatic in that
25 regard, but again, because pension law can change funding --

1 cash funding for pensions over the years not necessarily
2 based on the economics of changing those plans we use this
3 construct for pensions as well.

4 But strictly then for retiree medical we take for
5 active employees the cost of those employees at the point
6 that they retire for the rest of their lives and we present
7 value it to today to say what is the cost of those plans.
8 We divide by the remaining service life of the employees,
9 the present value of that service life of the employees, and
10 that gives you the cost per employee per year of providing
11 retiree medical into the future.

12 So long-winded but I think it might be important
13 because it's a unique construct, so.

14 Q Understood. And just to sort of break it out a little
15 bit more, the discount rate is like an interest rate, it's
16 to account for the time value of money, correct?

17 A It is, right.

18 Q So in a sense you're talking about a future benefit,
19 but you're trying to get a present value to it you have to
20 account for that time gap?

21 A Right. To do the present value the concept clearly
22 behind an interest rate is the economic indifference point
23 between a dollar today and a dollar tomorrow. That's --
24 it's very theoretical. But if you're going to earn ten
25 percent on your money you earn between receiving a dollar

1 today or \$1.10 in one year.

2 And so for this purpose we had to determine what
3 is the economic indifference point for American Airlines
4 between a dollar benefit today or dollars of benefits 20
5 years from now. For that we used 8.25 percent, which is the
6 return on asset rate from our pension plans that we have
7 audited every year and it is our average return on assets in
8 our pension plans over the last ten years, slightly below
9 that actual return actually, and we use that to say any
10 reasonable investment of these funds over -- over a long
11 term period -- when we invest the prefunding for retiree
12 medical similar to pension plans -- that investment and our
13 economic indifference between a dollar today and a dollar
14 tomorrow on that would be .25 percent.

15 So again long-winded, but --

16 Q Understood. So the eight and a quarter percent, that
17 is not a bond rate?

18 A I'm sorry?

19 Q That is not a bond rate?

20 A No, it is not. It is our return on investment in our
21 pension plans, which is allocated between bonds and stock.
22 So it's a mix of what we invest in, so.

23 Q As far as developing the eight and a quarter percent
24 rate is that something that Towers Watson came up with?

25 A No. You know, in retiree medical again there the

1 actuaries have -- all the actuarial tables and we use --
2 they use for purposes of calculating all this, all the same
3 assumptions they use for the books. So they didn't change
4 anything for our audited financials.

5 The discount rate -- well again, this is a
6 construct that we work with them to build with the unions,
7 our finance team, and they said, we don't -- that unique
8 discount rate for what you're building here, we don't have a
9 discount rate for that, you guys determine what it should
10 be.

11 Q So that is something that American Airlines developed
12 internally?

13 A That is right. That's our -- that's our own team.

14 Q And Towers Watson has not agreed whether or not that's
15 appropriate, that rate?

16 A They have told us they don't want to opine on it
17 because it's nothing -- this construct is nothing that is in
18 their realm of anything they do from a normal fiduciary
19 responsibility.

20 Q Now as far as the impact of the discount rate, if in
21 fact you had used a bond rate or any lower rate than eight
22 and a quarter percent that would impact the present value of
23 these future benefits, correct?

24 A It would. Let me tell you my thought on this. Because
25 I mean you inquire, this has been inactive, this is no

1 secret, we've had these discussions with the labor, so this
2 back and forth.

3 Clearly there's a range of interest rates out
4 there you could use. If you use strictly a risk-free rate
5 or something closer to risk free that invested 100 percent
6 in bonds it gives you a lower discount rate. If you use
7 weighted average cost to capital, as many companies do to
8 determine investments and long-term investment decisions,
9 that normally would be closer to 10 to 15 percent discount
10 rate. So you can -- there's a range of discount rates you
11 can reasonably use. I think I fairly kind of gave you the
12 logic of why we used this.

13 A lower discount rate would increase the value
14 attributed to this change, at the same time I will tell you
15 the target is based on economic cost as well for changes in
16 pension and retiree medical. So if you used a lower
17 discount rate your target would go up and the savings
18 attributed to these measures would go up and it would be
19 generally a wash any way. But there has been some
20 discussion over interest rate.

21 Q Well, and just looking briefly back in your declaration
22 to the chart below paragraph 28, and that is a reproduction
23 of AA Exhibit 707.

24 A Paragraph 28, sorry. Let me get there.

25 Q Paragraph 28 on the bottom of page 11 of your

1 declaration AA-700.

2 A Okay.

3 Q And that chart again breaks out by work group the
4 valuations for the proposed changes for future retiree
5 medical and life, correct?

6 A That is correct.

7 Q And that bottom line number there is not a confidential
8 number?

9 A No, it is not.

10 Q One hundred fifty-one million?

11 A That is right.

12 Q In the event a lower discount rate had been used, since
13 that reflects the presently value, that number, 151-, would
14 be -- would be greater, correct?

15 A Can't argue with the math.

16 Q One last topic, it has to do with head count. If you
17 could please look at paragraph 50. Still on your
18 declaration, AA-700.

19 A Okay.

20 Q The second sentence in paragraph 50, which does not
21 have any confidential information in it, says, "As a result
22 in 2014 American requires approximately 1200 fewer pilots."
23 Do you see that?

24 A I do.

25 Q Now you signed this declaration on March 23rd; is that

1 right?

2 A I did.

3 Q And is that the anticipated head count reduction as of
4 that date for the pilot group?

5 A As of that date it was. Now --

6 Q It's not now?

7 A That is correct. I've -- my team told me that they
8 have found -- actually I believe they said it was an error
9 in the model and they've talked with the pilots about it,
10 and we do find those as we've gone along. We make changes
11 and active discussions with the groups. But that number was
12 at the time we wrote this the number that we had in our
13 model, and that number is now 1420 or so.

14 Q So it's about 20 percent higher?

15 A Right.

16 Q That is relevant to the determination of cost savings
17 for the benefits we've just discussed because the fewer
18 pilots you have using the benefits the more savings the
19 company realizes, correct?

20 A Right.

21 Q So you would agree then based on the revision to the
22 head count number that's reflected in page 50, the actual
23 cost savings that would be realized by the company under
24 this plan would be higher?

25 A I'm not with that change. Again, I should have asked a

1 little bit more when they told me that, so I'm not familiar,
2 but the -- they have flowed through the economics of that
3 change through everything. I'm not so sure if it wasn't a
4 change in -- in what we quote as the number where the number
5 coming out of the model for savings is still right, but --
6 so I'm not sure.

7 If head count savings is higher then it would
8 impact the other savings, but I'm -- I want to be clear,
9 because I'm not sure that impacted some of the other cost
10 items, but I can't tell you why.

11 Q Okay. Mr. McMenemy, thank you.

12 MR. HAIRSTON: I'll pass the witness.

13 THE COURT: All right.

14 MS. LEVINE: Good afternoon, Sharon Levine,
15 Lowenstein Sandler for the TWU. Just a couple of questions.

16 CROSS-EXAMINATION

17 BY MS. LEVINE:

18 Q Do you have your affidavit in front of you?

19 A I do.

20 Q Page 29, paragraph 72.

21 A Okay.

22 Q There's a discussion there about outsourcing
23 maintenance and related?

24 A Yes, there is.

25 Q Ask you talk about a percentage of aircraft maintenance

1 that's going to be outsourced. And if you go down to the
2 middle of that paragraph it talks about a road map of how
3 it, which is American Airlines, foresees utilizing
4 outsourcing to achieve the savings that they want to
5 achieve, correct?

6 A That is correct.

7 Q Are the full amount of -- in the calculation of the
8 cost savings associated with the TWU offers, is the full
9 amount of hours in the road map in those cost savings?
10 Actually let me say -- I said that in artfully.

11 You're talking about a specific percentage leading
12 up to a specific dollar amount. Is there a working into the
13 valuation a lower percentage and a lower dollar amount as
14 you implement the cost savings or is the full amount of the
15 percentage outsourcing and full amount of cost savings
16 immediately in the analysis?

17 A No. Yeah, no, it is the year one -- the savings
18 attributed are the one through six average savings, and if
19 it takes a year to implement the savings ramp up over a year
20 and average over the -- and then you average it out over the
21 six years.

22 Q And is there an analysis of cost saving by aircraft?

23 A No. No, because again, in outsourcing you do it per
24 hour of our cost versus an outsourced. Generally
25 maintenance cost per hour for labor don't vary by aircraft

1 time.

2 Q In paragraph 73 you talk about the costs the company
3 reasonably anticipates being able to achieve through
4 outsourcing. Do you see where you say that? Fourth line
5 down from the top of the page.

6 A Okay, I'm reading here. On page -- I'm sorry, so
7 you're talking paragraph 73, right?

8 Q Paragraph 73 --

9 A Okay.

10 Q -- if you're on page 30 it's the fourth line down.

11 A Oh, I'm on the wrong page.

12 (Pause)

13 A Yes, okay, I'm there.

14 Q Have you -- do you know what an RFP is?

15 A Yes.

16 Q What is an RFP just so we have it for the record?

17 A It's a request for a proposal.

18 Q Right. Have you issued RFPs with regard to the
19 outsourcing you propose?

20 A I believe we have, but actually I'm not -- I'm not
21 certain, so I can't answer for sure.

22 Q Do you know whether those RFPs were to domestic
23 companies or foreign companies or a combination?

24 A Again, I know that is being worked on, but I don't know
25 the status. Quite honestly I just don't know.

1 Q In doing the calculations with regard to outsourcing
2 have you taken into account the difference between domestic
3 outsourcing and foreign outsourcing?

4 A Well, I do know in the rate we used we used a mix of
5 where we thought outsourcing would occur, and some of that
6 is international and some of that is domestic.

7 Q Okay. Now with regard to foreign outsourcing, isn't it
8 true that there's no DOT drug testing with regard to foreign
9 outsourcing?

10 MR. GALLAGHER: Objection, Your Honor, far beyond
11 the scope of direct and --

12 THE COURT: What's the relevance of that?

13 MS. LEVINE: Well, it goes to execution risk and
14 whether or not the costs are actually comparable, Your
15 Honor.

16 THE COURT: Does it? I mean, I don't know that
17 you have a foundation for that.

18 MS. LEVINE: Well, if this witness isn't the right
19 witness we can go to a different witness, but at some point
20 we are going to take a look at whether or not some of the
21 other airlines have actually achieved the levels of savings
22 they purported to achieve through outsourcing and some of
23 the issues that they may have wished they had looked at more
24 closely before they made those decisions.

25 MR. GALLAGHER: Your Honor, if I may, that's

1 totally speculative. There's no testimony anywhere that
2 there will be any international outsourcing.

3 THE COURT: Well, again, this is the challenge of
4 sort of a staged proceeding. I'm not sure how all this will
5 get connected or if it will get connected and we may have
6 strands that float out there and other things that are
7 neatly tied in a bow. So in light of that as I've done a
8 couple times I'll give a little bit of latitude to ask a few
9 questions.

10 MS. LEVINE: It's very short, Your Honor.

11 THE COURT: All right. With -- and the relevance
12 and perhaps any admissibility of that being subject to tying
13 some things together in the future.

14 THE WITNESS: Now you'll have to ask the question
15 again.

16 BY MS. LEVINE:

17 Q Yeah, I forgot the question.

18 A It's a fair point.

19 Q With regard to foreign outsourcing have -- are you
20 aware that there's no DOT testing with regard to many
21 foreign sources?

22 A I hate to disappoint after all that, but no, I'm not
23 aware.

24 (Laughter)

25 Q Do you know if the entities to which some of the

1 foreign outsourcing might occur require DOT -- have the same
2 DOT requirements with regard to licensing?

3 A Again, I don't.

4 Q But outsourcing does take place at a remote location,
5 that's the point of outsourcing, correct?

6 A Yes. Yes, I mean we -- our cost outs contemplate some
7 internationals and domestic.

8 Q Okay. And you would have to get the planes back and
9 forth from their remote locations, correct?

10 A We would if they are -- if they don't fly there as a
11 part of normal scheduling. Any maintenance you do anywhere
12 you have to route the aircraft.

13 Q And there's a -- there's an execution risk associated
14 with that isn't there?

15 A No matter where you do the maintenance there will --
16 there -- yeah, I don't -- well, I should ask what you mean
17 by execution risk, but --

18 Q When you're taking the planes there and back there's a
19 time associated with getting them there, there's a schedule
20 when you hope to get them back --

21 A Right.

22 Q -- and when the plane is down isn't it true that it
23 costs the airline money if the plane is out of service?

24 A Yes, as it does internally. You know, we have routing
25 costs when we do maintenance internally ourselves, we'll

1 have routing costs if we do it external.

2 Q So, for example, just recently in April in Dallas there
3 was a huge tornado with hail, it was well publicized,
4 American got a lot of good press and put out a lot of good
5 press about the fact that they had over 100 planes that were
6 out of service and got those planes back up and running
7 within three days.

8 THE COURT: Hold on a minute.

9 BY MS. LEVINE:

10 Q Do you recall that?

11 MR. GALLAGHER: Objection, Your Honor, relevance,
12 far beyond the scope of direct.

13 MS. LEVINE: Well, the point --

14 THE COURT: Well, now I think we've gone from what
15 you had originally sort of proffered as the connection, I'm
16 not sure the anecdotal discussion really goes to -- goes to
17 this. So if that's your only --

18 MS. LEVINE: Well, they're actually -- there
19 actually are some facts, just a little -- three or four more
20 questions, Your Honor, maybe less, maybe only two that would
21 tie it together, and then dinner.

22 (Laughter)

23 THE COURT: All right. We'll give it a shot.

24 BY MS. LEVINE:

25 Q Isn't it true you were able to fly in 21 mechanics from

1 AFW and 45 mechanics -- and you had 45 mechanics from Tulsa
2 that were able to work on that aircraft immediately to turn
3 it quickly?

4 A I do not know the numbers, but yes, we brought in
5 mechanics from Tulsa and other locations to work on the
6 aircraft.

7 MS. LEVINE: No further questions, thank you.

8 THE COURT: Oh, you did that one in, all right.
9 All right.

10 MR. BUTLER: No questions (indiscernible -
11 5:59:51), Your Honor.

12 THE COURT: Any redirect?

13 MR. GALLAGHER: No, Your Honor.

14 THE COURT: All right, you're excused. Thank you
15 for your testimony.

16 And that's rather a neat bow time wise because it
17 is exactly 6 o'clock.

18 So as I understand based on our prior discussion
19 of plan tomorrow is Mr. Vaughn starting at 10 a.m.

20 MR. GALLAGHER: Okay.

21 THE COURT: And we expect Mr. Vaughn to roughly
22 take a half a day, consistent with other witnesses.

23 MR. GALLAGHER: Right. Your Honor, I am advised
24 that I did not yet move in the admission of Mr. McMenamy's
25 declaration, Exhibit 700 and the related company Exhibits

1 701 through 708.

2 THE COURT: All right. Any objection?

3 MR. DEAN: No, objection.

4 THE COURT: All right. They are --

5 MR. MEYERHOFF: They are --

6 MR. GALLAGHER: Thank you, Your Honor.

7 MR. MEYERHOFF: -- the PBGC reserves it's
8 objection as it has with respect to the prior witnesses.

9 THE COURT: Okay. Certainly. All right.

10 MR. MEYERHOFF: For the record, Gary Meyerhoff.

11 THE COURT: All right, thank you, Mr. Meyerhoff.

12 Subject to that they are received.

13 (Debtor's Exhibit Nos. 700, 701-708 were admitted)

14 MS. KRIEGER: Oh, Your Honor, there's one other
15 matter and I apologize to the belated.

16 There was an objection that we had meant to
17 interpose and I was out of the courtroom at the time when
18 Mr. Brundage's declaration was moved for admission. It was
19 a legal objection of the same nature as the one raised with
20 respect to Mr. Dichter's that is a legal conclusion.

21 THE COURT: I -- I am -- that's a witness ago, and
22 in this case it's a lifetime ago, so I am sure that in your
23 briefing you will explain to me the relevance of it and that
24 whatever it is you're objecting to is completely irrelevant
25 and really has no weight. So I think you can accomplish the

1 same purpose.

2 MS. KRIEGER: Thank you, Your Honor.

3 THE COURT: So I don't think that will ultimately
4 -- how you phrase it will make too much of a difference
5 there.

6 All right. So, Mr. Vaughn is set for tomorrow. I
7 think given that we only anticipate that one more witness I
8 think we can simply start at 10:00.

9 And let me just ask one other thing. There
10 obviously are a lot of other declarations and exhibits that
11 I have been provided with, and I imagine you're going to
12 address that tomorrow to sort of wrap things up in a bow so
13 I know what the record is and then we can talk about the
14 true up, the timing of that, and then I guess we can also
15 talk about the schedule for further proceeding consistent
16 with the scheduling order and whether there's any need to
17 make any changes or all that good stuff tomorrow.

18 MR. GALLAGHER: Thank you, Your Honor.

19 THE COURT: All right. Anything else?

20 UNIDENTIFIED SPEAKER: No, Your Honor.

21 THE COURT: All right. Thank you, have a good
22 evening.

23 (Whereupon these proceedings were concluded at 6:02 PM)

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I N D E X

T E S T I M O N Y

DEBTOR'S

WITNESS

EXAM BY

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E X H I B I T S

PARTY	NO	DESCRIPTION	ID.	EVID.
Debtor	400	Declaration of Mr.		
		Dichter	--	141
	401-			
	403	Exhibits to Declaration	--	141
	500	Declaration of Mr.		
		Brundage	--	249
	501-			
	509	Exhibits to Declaration	--	249
	700	Declaration of Mr.		
		McMenamy	--	306
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I, Dawn South, certify that the foregoing transcript is a true and accurate record of the proceedings.

AAERT Certified Electronic Transcriber CET**D-408

Also transcribed by:

Sherri L. Breach

AAERT Certified Electronic Reporter & Transcriber CERT*D-397

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Date: April 30, 2012