



Economic & Financial Analysis: Contract Costing

This edition of *Touch & Gos* is the second in a series that focuses on the mechanics of how negotiations are conducted under Section 6 of the Railway Labor Act. The next edition, the last in this series, will provide a general overview of what actually takes place during a typical negotiating session. This will be followed by a more focused communication effort that will include an *in-depth* discussion of Section 6 negotiations, which will include a comprehensive article that will place you in the seat as the Delta MEC Negotiating Committee Chairman as you manage the negotiating process from beginning to end.

The next step in the communications effort will be a contract history followed by an extensive contract comparison, and later this summer, you will have the opportunity to participate in a comprehensive contract survey. As MEC chairman Captain Tim O'Malley wrote in his recent *Chairman's Letter*, "*The information you have received to date and that which is yet to come is all designed to help you provide informed input to the survey. I cannot emphasize enough the need for you to carefully consider and provide that input when the time comes; the results of that survey will be a primary source of information that the MEC will use to craft our Section 6 opener.*"

About E&FA

One of the key resources available to your MEC and the Negotiating Committee is ALPA's Economic & Financial Analysis (E&FA) department.

E&FA's mission is to support ALPA members in all matters related to the economic portions of their collective bargaining agreements including providing direct support at the bargaining table and analyzing the financial condition of the their airline and the industry as a whole.

The department currently has a staff of 13 members. ALPA's E&FA professionals have rich academic backgrounds, which include undergraduate degrees in economics, business, finance, engineering and aeronautical studies as well as master degrees in business administration,

economics and finance. These academic backgrounds are coupled with real-world experience including work in the airline industry (both cargo and passenger), and for leasing companies, aircraft manufacturers and consulting companies.

E&FA has participated in virtually all ALPA contract negotiations and has undertaken over 100 analyses of internal airline business plans, projections and strategies involving nearly every major, national and regional U.S. and Canadian airline represented by ALPA. In addition, the department has provided expert testimony as airline industry and financial experts in bankruptcy proceedings and arbitrations; is often actively engaged in tracking contract compliance for scope; and helps to develop economic returns such as profit and equity sharing.

How Does E&FA Help Our MEC and Negotiating Committee Prepare For Negotiations?

When developing their bargaining positions, your MEC and the Negotiating Committee need to know and understand not only Delta's operating and financial condition as well as its strategic plans and projections, but also the condition of the industry and the trends in the overall economy. To help your team assess the environment in which they are bargaining, E&FA conducts various analyses based on meetings with senior management (with independent verification whenever possible) and assessments of industry trends.

Additionally, E&FA is instrumental in preparing a comparison of the collective bargaining agreements in place at Delta's competitors. This allows your MEC and the Negotiating Committee to see how the current contract stacks up against that of our industry peers and helps identify contractual strengths and weaknesses.

Costing of Contract Proposals

E&FA works closely with your Negotiating Committee as they develop their proposals under the direction of the MEC. E&FA will develop a

customized model that is uniquely tailored to Delta to provide costing information. The outputs from the model help your Negotiating Committee determine the overall value of their proposals (as well as the value of management's proposals).

The customized model is based on a variety of factors such as:

- Pilot headcount and distribution (i.e., data from the seniority list),
- Fleet plans (including hull count and block hours per aircraft type),
- Pilot pay hours (by aircraft type and status, including block, vacation, sick, training, credit, deadhead, guarantee, etc.), and
- Variable and fixed benefits

The model is continually updated as new proposals are considered, providing both summary overall cost impacts as well as detailed information on specific items. The model compares your Negotiating Committee's proposals to management's proposals as well as to current book.

“I Don't Care What It Costs; I Just Want It All and I Want It Now” (or Why Does Costing Matter?)

One of the reasons for costing is to help facilitate the process. By having accurate costing information, the negotiations can focus on the *issues*, rather than getting bogged down in the *numbers*.

Obtaining accurate costing data also helps in *crafting* proposals. While it is tempting for some to suggest that they do not care what a contractual improvement costs, negotiations involve two parties, and the Company does care. And ultimately, if the National Mediation Board becomes a third party to the negotiations, you can be certain that they too will care.

Additionally, overall improvements to the contract will ultimately have *some* net value. Contract costing allows your expanded negotiating team to

determine which items pack the most “bang for the buck” as well as the cost of individual improvements relative to the whole. And it allows the Negotiating Committee to determine, based on MEC direction (which in turn is based in large part on line pilot input), how to allocate negotiating capital. This is another reason why your participation in the upcoming contract survey is so important.

What Happens If ALPA and Management Can't Agree on Costing?

During negotiations, E&FA works with management as *each* side develops its *own* models, sharing data and assumptions, with the goal of reaching the same costing conclusions. On some issues (particularly work rule issues), E&FA will work directly with management to *jointly* determine costs.

There are times, however, when E&FA and management will disagree on the value of a contractual change. These often involve items that try to model a change in pilot behavior (such as changes to sick leave or vacation usage). While both sides will work together to see if agreement can be reached on valuation, sometimes you simply have to agree to disagree, but, generally speaking, E&FA and management will arrive at reasonably close costing estimates.

Conclusion

Accurate costing plays an integral role in the overall negotiating process.-Both ALPA and non-ALPA carriers often seek E&FA's services because no other entity in the financial analysis market can compare. The National Mediation Board and airline managements across the board can vouch for the expertise of the ALPA E&FA. In fact, managements and the NMB have often agreed to depend *solely* on ALPA E&FA calculations during negotiations. Your MEC and the Negotiating Committee trust in the proven reliability of ALPA E&FA's expert advice and analyses, and so can you.

Did You Know?

The expertise of ALPA's Economic & Financial Analysis's department is sought after not just domestically, but worldwide. E&FA staff has conducted financial and operational analyses at Air France, Air New Zealand, Air Jamaica, Cathay Pacific, Singapore, KLM, South African Airways, Aer Lingus, Sabena, TAP Air Portugal, CSA Czech Airlines and SAS. They have also been contracted by the Allied Pilots Association (the American Airlines pilots' union) to assist them in achieving a new contract.