TESTIMONY OF

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on the subject of

INDUSTRY PLANS TO STABLIZE THE FINANCIAL CONDITION OF THE AMERICAN AUTOMOBILE INDUSTRY

before the

COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

December 5, 2008

Mr. Chairman, my name is Ron Gettelfinger. I am President of the International Union, United Automobile, Aerospace & Agricultural Implement Workers of America (UAW). The UAW represents one million active and retired members, many of whom work for or receive retirement benefits from the Detroit-based auto companies and auto parts suppliers across the United States. We welcome the opportunity to appear before this Committee to present our views on industry plans to stabilize the financial condition of the American automobile industry.

The UAW believes the situation at GM, Ford and Chrysler is extremely dire. As is evident from the materials which have been submitted by the companies in response to the letter from Speaker Pelosi and Majority Leader Reid, it is imperative that the federal government act this month to provide an emergency bridge loan to the domestic auto companies. Without such assistance, GM could run out of funds by the end of the year, and Chrysler soon thereafter. These companies would then be forced to liquidate, ceasing all business operations. The collapse of these companies would inevitably drag down numerous auto parts suppliers, which in turn could lead to the collapse of Ford.

The UAW appreciates the desire by Congress, as expressed in the letter from Speaker Pelosi and Majority Leader Reid, to ensure that any assistance from the federal government is conditioned on strict accountability by the companies and a demonstration that they can be viable businesses in the future. We fully support both of these key principles.

Specifically, the UAW supports conditioning any emergency bridge loan on strict accountability measures, including:

- tough limits on executive compensation, prohibiting golden parachutes and other abuses, and making it clear that top executives must share in any sacrifices;

- a prohibition on dividend payments by the companies;

- giving the federal government an equity stake in the companies so that taxpayers are protected; and

- establishing an Advisory Board to oversee the operations of the companies to ensure that all funds from the emergency bridge loan are spent in the United States, that the companies are pursuing viable restructuring plans, and that the companies are meeting requirements to produce advanced, more fuel efficient vehicles.

We are prepared to work with Members of this Committee to incorporate other accountability requirements that may be appropriate.

In addition, the UAW supports conditioning any emergency bridge loan on the companies pursuing restructuring plans that will ensure the viability of their operations in the coming years. For such restructuring plans to succeed, we recognize that all stakeholders – equity and bondholders, suppliers, dealers, workers and retirees, and management – must come to the table and share in the sacrifices that will be needed.

The UAW and the workers and retirees we represent are prepared to do our part to ensure that the companies can continue as viable operations. As indicated in our previous testimony, workers and retirees have **already** stepped forward and made enormous sacrifices.

- In 2005 the UAW reopened its contract mid-term and accepted cuts in wages for active workers and health care benefits for retirees.

- In the 2007 contract the UAW agreed to slash wages for new workers by 50% to about $14 per hour, and to exclude new workers from the traditional health care and pension plans. The UAW also allowed the companies to outsource cleaning work at even lower rates.

- Under the 2007 contract, beginning January 1, 2010 the liabilities for health care for existing retirees will be transferred from the companies to an independent VEBA fund. Taken together, the changes in the 2005 and 2007 contract reduced the companies' liabilities for retiree health care benefits by 50%.

- As a result of the 2005 and 2007 contracts, workers have not received any base wage increase since 2005 at GM and Ford, and since 2006 at Chrysler. All of these workers will not receive any increase through the end of the contract in 2011. Workers have also accepted reductions in cost of living adjustments.

- New local operating agreements at many facilities provided dramatic flexibilities and reductions in classifications, and have saved the companies billions of dollars.

- Reforms in the 2007 contract have largely eliminated the jobs banks.

- Since 2003 downsizing by the companies has reduced their workforce by 150,000, resulting in enormous savings for GM, Ford and Chrysler.

Thanks to the changes in the 2005 and 2007 contracts, and changes that have subsequently been agreed to by the UAW, the labor cost gap with the foreign transplant operations will be largely or completely eliminated when the contracts are fully implemented. Industry observers applauded the sacrifices made by workers and retirees, calling the 2007 contract a “transformational” agreement.

The UAW is continuing to negotiate with the domestic auto companies on an ongoing basis over ways to make their operations more efficient and competitive. We recognize that the current crisis may require all stakeholders, including the workers and retirees, to make further sacrifices to ensure the future viability of the companies. We are willing to do our part. In particular, we recognize that the contributions owed by the companies to the retiree health care VEBA fund may need to be spread out. The UAW has retained outside experts to work with us on how this can be accomplished, while still protecting the retirees. We also recognize that adjustments may need to be made in other areas.

But the UAW vigorously opposes any attempt to make workers and retirees the scapegoats and to make them shoulder the <u>entire</u> burden of any restructuring. Wages and benefits only make up 10 percent of the costs of the domestic auto companies. So the current difficulties facing the Detroit-based auto companies cannot be blamed on workers and retirees.

Contrary to an often-repeated myth, UAW members at GM, Ford and Chrysler are not paid $73 an hour. The truth is, wages for UAW members range from about $14 per hour for newly hired workers to $28 per hour for assemblers. The $73 an hour figure is outdated and inaccurate. It includes not only the costs of health care, pensions and other compensation for current workers, but also includes the costs of pensions and health care for all of the retired workers, spread out over the active workforce. Obviously, active workers do not receive any of this compensation, so it is simply not accurate to describe it as part of their "earnings." Furthermore, as previously indicated, the overall labor costs at the Detroit-based auto companies were dramatically lowered by the changes in the 2005 and 2007 contracts, which largely or completely eliminated the gap with the foreign transplant operations.

The UAW submits that it is not feasible for Congress to hammer out the details of a complete restructuring plan during the coming week. There is simply not enough time to work through the many difficult and complex issues associated with all of the key stakeholders, including equity and bondholders, suppliers, dealers, management, workers and retirees, as well as changes in the business operations of the companies.

What Congress can and should do is to put in place a process that will require all of the stakeholders to participate in a restructuring of the companies outside of bankruptcy. This process should ensure that there is fairness in the sacrifices, and that the companies will be able to continue as viable business operations. This process can begin immediately under the supervision of the next administration. By doing this, Congress can make sure that the emergency assistance is indeed a bridge to a brighter future.

Contrary to the assertions by some commentators, in the current environment a Chapter 11 reorganization – even a so-called “pre-packaged” bankruptcy – is simply not a viable option for restructuring the Detroit-based auto companies. As previously indicated, research has indicated that the public will not buy vehicles from a company in bankruptcy. It also is doubtful that the companies could obtain debtor-in-possession financing to operate during a bankruptcy. In addition, attached to this testimony is a more detailed analysis prepared with the assistance of experienced bankruptcy practitioners explaining why a “pre-packaged” bankruptcy is not a feasible option for the domestic auto companies because of the size and complexity of the issues that would necessarily be involved in any restructuring, including relationships with thousands of dealers and suppliers and major changes in business operations. Thus, the UAW wishes to underscore that any bankruptcy filings by the domestic auto companies at this time would inevitably lead to Chapter 7 liquidations and the cessation of all business operations.

The collapse of the domestic auto companies would have disastrous consequences for millions of workers and retirees and for the entire country.

- Hundreds of thousands of workers would directly lose their jobs at GM, Ford and Chrysler, and a total of three million workers would see their jobs eliminated at suppliers, dealerships and the thousands of other businesses that depend on the auto industry.

- One million retirees could lose part of their pension benefits, and would also face the complete elimination of their health insurance coverage, an especially harsh blow to the 40 percent who are younger than 65 and not yet eligible for Medicare.

- The Pension Benefit Guarantee Corporation could be saddled with enormous pension liabilities, jeopardizing its ability to protect the pensions of millions of other workers and retirees. To prevent this from happening, the federal government could be forced to pay for a costly bailout of the PBGC. The federal government would also be liable for a 65% health care tax credit for pre-65 retirees from the auto companies, at a cost of as much as $2 billion per year.

- Revenues to the federal, state and local governments would drop sharply, forcing cuts in vital social services at a time when they are urgently needed.

- The ripple effects from the collapse of the Detroit-based auto companies would deal a serious blow to the entire economy, making the current recession much deeper and longer.

- There also would be a serious negative impact on many financial institutions that hold large amounts of debt from the Detroit-based auto companies and their auto finance associates. This could pose a systemic danger to our already weakened financial sector.

For all of these reasons, the UAW submits it is imperative that Congress and the Bush administration act next week to provide an emergency bridge loan to the Detroit-based auto companies. The consequences of inaction are simply too devastating; the economic and human toll are too costly.

The UAW believes that the recent actions by the federal government to provide an enormous bailout to Citigroup reinforce the case for providing an emergency bridge loan to the Detroit-based auto companies. The total assistance provided to Citigroup will dwarf that being sought by the domestic auto companies. Citigroup received this assistance without being required to submit any "plan" for changing its operations or demonstrating its future viability. It was not required to change its management. And it is still able to continue paying bonuses and other forms of lucrative executive compensation.

If the federal government can provide this type of blank check to Wall Street, the UAW submits that Main Street is no less deserving of assistance. Since the domestic auto companies have come forward with detailed plans relating to accountability and their future viability, there is simply no justification for withholding the emergency bridge loan that is necessary for them to continue operations.

The UAW also notes that other governments around the world are actively considering programs to provide emergency assistance to their auto industries. In particular, the European Union is considering a $51 billion loan program for automakers. And there are ongoing discussions with Germany, Great Britain, Sweden, Belgium, Poland, South Korea, China and other nations about steps their governments can take to assist their auto industries. Clearly, other governments recognize the economic importance of maintaining their auto industries. The UAW submits that the economic importance of GM, Ford and Chrysler to the U.S. economy is no less important and no less deserving of assistance.

It is not enough, however, for the federal government to provide an emergency bridge loan to the Detroit-based auto companies, and to oversee and facilitate the restructuring of the companies. The 111th Congress and the Obama administration have a responsibility to pursue policies in a number of areas that will be critically important to the future viability of the domestic auto companies, as well as the well being of our entire nation.

First, the UAW is very pleased that Congressional leaders and the Obama transition staff are already making plans to move forward quickly with a major economic stimulus package that will create jobs and give a boost to the entire economy. We believe this is urgently needed to prevent the economy from slipping into a deeper and more serious recession. This is particularly important for the auto sector. In order for the Detroit-based auto companies to succeed, it is vital that auto sales rebound from the record low levels we have seen in recent months. The single most important thing that can be done to increase auto sales is to reinvigorate the overall economy.

Second, the UAW believes it is critically important that Congress and the Obama administration move forward quickly with plans to reform our broken health care system, and to put in place programs that will guarantee health insurance coverage for all Americans, contain costs, ensure quality of care, and establish more equitable financing mechanisms. In particular, we believe any health care reform initiative should include proposals to address the challenges associated with providing health care to the pre-Medicare population aged 55-65.

There can be no doubt that one of the major financial challenges facing the Detroit-based auto companies in future years is the cost of providing health care to almost a million retirees. Although the 2005 and 2007 contracts greatly reduced the companies' retiree health care liabilities, they are still enormous and a major problem that hinders the ability of the companies to obtain financing from private lenders.

All of the other major auto producing nations have national health care systems that spread the costs of providing health care across their societies. As a result, the automakers in these countries are not burdened by retiree health care legacy costs. Accordingly, the UAW is hopeful that the enactment of national health care reform in the United States would help to establish a level playing field among all employers, and alleviate the retiree health care legacy costs facing the Detroit-based auto companies.

Third, during the coming year Congress and the Obama administration are likely to consider major new initiatives dealing with energy security and climate change. The UAW strongly supports prompt action in both of these vital areas. Specifically, besides requiring automakers to comply with the tougher new fuel economy standards that were enacted in 2007, we believe Congress and the Obama administration should take steps to ensure that fuel economy improvements continue in the years following 2020, and that the companies move expeditiously to introduce advanced technology vehicles. In particular, we support an aggressive program to increase domestic production of plug-in hybrids and their key components, and to expand the infrastructure that will be needed to support these vehicles. To help achieve these objectives, Congress and the Obama administration should make sure that the Section 136 Advanced Technology Vehicles Manufacturing Incentive Program (ATVMIP) continues to be fully funded, and that additional resources are provided to ensure that production of advanced, more fuel efficient vehicles and their key components is ramped up quickly. In addition, the UAW strongly supports the enactment of an economy-wide cap-and-trade program to aggressively reduce emissions of greenhouse gases that are causing climate change.

Although these initiatives pose challenges for the auto industry, the UAW also believes they can provide great opportunities. Properly structured, these initiatives can not only ensure that our nation reduces its consumption of oil and emissions of greenhouse gas emissions. They also can ensure that the more fuel efficient vehicles of the future and their key components are built in the United States by the domestic auto companies and American workers. In effect, these initiatives can be an important part of the restructuring that is necessary to ensure the future viability of the domestic auto companies.

Fourth, Congress and the Obama administration must make sure that our nation's trade policies promote fair trade, not so-called "free trade" that fails to provide a level playing field and instead places our domestic automakers at a significant competitive disadvantage. In particular, prompt action needs to be taken to eliminate unfair currency manipulation by China and Japan. In addition, Congress and the Obama administration should insist that the U.S.-Korea free trade agreement must be renegotiated to require that Korea dismantle the non-tariff barriers that have kept its market closed to U.S.-built automotive products, before it is granted any further access to the U.S. market.

By pursuing all of these policies, Congress and the Obama administration can benefit our entire country. The UAW also believes that these policies can provide a basis under which a restructured domestic auto industry can remain viable and strong in the coming years.

In conclusion, the UAW appreciates the opportunity to testify before this Committee on industry plans to stabilize the financial condition of the American automobile industry. We strongly urge this Committee and the entire Congress to act promptly to approve an emergency bridge loan to the Detroit-based auto companies to enable them to continue operations and to avoid the disastrous consequences that their liquidation would involve for millions of workers and retirees and for our entire nation.

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Pre-Packaged Bankruptcy Is Not the Path to Revitalize the Domestic Auto Companies

Some commentators have suggested a pre-packaged bankruptcy as an alternative to (or as part of) government-backed relief for the domestic auto companies. But the promoters have not explained how pre-packaged bankruptcy procedures can be successfully brought to bear in a case with the complexity and scope of one or all of the Detroit-based auto companies. Indeed, bankruptcy experts are skeptical that pre-packaged bankruptcy can work. As one noted business writer who has consulted with bankruptcy experts has concluded, "it makes no sense."[1]

In a pre-packaged bankruptcy, a company negotiates a financial restructuring with its major creditors outside of bankruptcy, lines up all or most of its major creditors in support of the proposed debt restructuring, and then uses the bankruptcy process to achieve a quick, consensual approval of its repayment plan. Any minority, dissenting creditors are out-voted by the pre-arranged majority support for the plan. Bankruptcy law permits pre-packaged deals as an efficient form of business restructuring.

Pre-packs can work with **financial** restructurings, i.e., those that do *not* involve substantial operational issues. Where a company must restructure its balance sheet, but the business is otherwise sound, large creditors holding secured and unsecured debt are more likely to agree on the business fundamentals, and therefore more likely to reach a negotiated agreement on restructuring terms -- for example, swapping debt for equity or extending debt maturities. But the domestic automobile manufacturers are in the midst of a much broader restructuring which is, to a large degree, operational. They are shifting their product mix; they are developing new-technology vehicles; and they are revamping their production locations. None of these issues can realistically be addressed in a pre-packaged bankruptcy, which is aimed at obtaining the consent of creditors to renegotiated terms on their financial debt instruments. Pre-packs were not intended for operational restructuring scenarios.

In fact, no one has explained how the basic elements of a pre-packaged bankruptcy can be achieved in the case of the domestic auto companies. Who are the debt holders, and can enough of them agree on negotiated terms? The *New York Times* reports that the domestic automakers owe more than $100 billion to banks and bondholders. The originating banks have probably syndicated, or sold off, pieces of the debt to others. Some $56 billion in new debt securities was reportedly issued to investors such as pension funds, insurance

[1] Joe Nocera, "Road Ahead is Long for G.M.," *The New York Times*, November 22, 2008.

companies and hedge funds.[2] For a pre-packaged bankruptcy to work – or even get organized - the lion's share of the outstanding debt holders need to be identified, agree to come to the table, and then agree on restructuring terms. This process would be a lengthy and expensive one, undertaken in an uncertain and weak economic environment.

The same types of problems would exist for other claimants. The various creditors engaged in the process would likely want to see a business plan before negotiating restructured terms. Thus, the pre-packaged bankruptcy would be the proverbial tail wagging the dog. Assumptions made by some proponents of a pre-pack about whether stakeholders will participate in a pre-packaged effort and what the likely outcomes would be are unsupported supposition. Also unanswered are questions about how a bankruptcy filing would deal with GMAC and the other auto finance entities or the companies' overseas operations.

A pre-packaged bankruptcy could disintegrate into a regular, contested bankruptcy proceeding. First, the likelihood of obtaining the requisite consents is already challenged by the size, potential scope, and lack of transparency of the debt holders. Second, pre-packs must follow solicitation rules which are governed by securities laws, not bankruptcy law. The company would have to put together a solicitation that successfully navigates these rules. And, once in bankruptcy court, the efficient nature of the approval process would depend on sufficient compliance with the solicitation rules, and a sufficient supporting majority, to overcome challenges by dissenting creditors or others. If the approval process became prolonged, then the advantages of speed and efficiency would be lost.

Pre-packaged bankruptcy would not eliminate the risks associated with a bankruptcy filing. It would not eliminate the threat of systemic risk resulting from the effects of a bankruptcy by one or all of the domestic automakers on the financial markets.[3] Moreover, a pre-packaged bankruptcy is still a bankruptcy as far as customers are concerned. The promoters have not explained how pre-packaged bankruptcy would allay the concerns of the majority of consumers who have said they would not buy an automobile from a company in bankruptcy. Given this consumer reaction, a bankruptcy filing by any one of the domestic automakers in the current environment is a dangerous "bet the economy" proposition.

None of the elements of an auto industry restructuring *require* a bankruptcy proceeding. Restructuring milestones, repayment terms, taxpayer protections and other conditions of a loan can be established through legislation. Moreover, legislation can establish a process under which the actual restructuring of the

[2] Zachary Kouwe and Louse Story, "Big Three's Troubles May Touch Financial Sector," *The New York Times*, November 24, 2008
[3] Zachary Kouwe and Louse Story, "Big Three's Troubles May Touch Financial Sector," *The New York Times*, November 24, 2008

domestic auto companies is supervised by the next administration. This can ensure that all stakeholders come to the table and share in the sacrifices that will be required, and that the domestic auto companies will be viable businesses after the restructuring is completed. In contrast, putting the fate of an auto industry restructuring in the hands of a bankruptcy court, even if a pre-packaged plan were realistically possible, would put narrow creditor interests ahead of all other stakeholders and ahead of important national concerns, including health care and pension policy, energy and transportation policy, and the negative effects of the economic downturn. These are interests that must be addressed and balanced by our elected government.

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