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My name is Thomas Kochan and I am a professor of management at the MIT Sloan School of Management and Co-Director of the MIT Institute for Work and Employment Research. My comments today are derived from a study of airline labor and employee relations that a group of us has been carrying out over the past eight years under the auspices of the MIT Global Airline Industry Project.[1]

My specific comments relate to the likely effects of the proposed merger between Northwest Airlines and Delta Airlines on labor and employee relations in the merged organization and, in turn, the effects of labor and employee relations on the organization's financial performance, customer service, and employment outcomes. My main point can be summarized succinctly.

If the labor and employee relations issues that will confront the merged organization are not addressed satisfactorily prior to or as part of the merger process, the merged organization will experience intense and prolonged labor management conflict over organizing rights and representation and in negotiations of labor agreements for those occupational groups that choose to be represented. If this happens, our research, and recent experience of merged airlines predict the merged firm will experience low productivity, poor customer service, and significant financial losses that could lead to a return to bankruptcy. If, on the other hand, these issues are addressed successfully prior to the merger, the new organization has the potential for improving these economic outcomes for its shareholders, employees, and the customers and communities it serves. Therefore, I urge the Congress and the Administration to insist that the key labor and employment issues which I will discuss in more detail below be addressed as part of the business plan for the merged organization and that the merger only be approved if all the parties involved demonstrate a commitment to implementing this plan.

Background: The Airline Industry is headed toward a "Perfect Storm"

Between 2001 and 2005 airlines in the U.S. cut over 100,000 jobs and lost $30 billion dollars. Employees lost over $15 billion in wages. Sixteen pension plans covering approximately 240,000 employees were terminated and turned over to the

[1] The full results of our research will be summarized in Greg Bamber, Jody Hoffer Gittell, Thomas Kochan, and Andrew vonNordenflytch, *Up in the Air: How Airlines can Compete by Involving their Workforce.* Cornell University/ILR Press, forthcoming, Fall, 2008.

government's Pension Benefit Guarantee Corporation.[2] Morale plummeted to all time low levels. Customers have endured increased traffic delays and more lost baggage, and customer complaints are rising. The air traffic control system needs a major technological upgrade, airport congestion is stressing the system, and air traffic controllers can't be hired and trained fast enough to replace those retiring. Now, in the face of fuel prices that have risen over 80 percent in the past year, all airlines (with the exception of Southwest, the only company that was able to hedge against fuel price increases) are once again experiencing deep financial losses, employees are experiencing further job cuts, and customers and communities are facing further cuts in service. So on all these dimensions the nation's air transportation system is being stressed and perhaps approaching its limits. The prospect for a perfect storm in which the pressures explode together is growing. The pressures are likely to come to a head when labor contracts covering employees who took the deepest cuts in wages and benefits come due for renegotiations in late 2009 and early 2010.

Labor Relations Challenges/Conflicts Associated with the Delta-Northwest Merger

The pending crisis could come even sooner for Delta and Northwest if their proposed merger is approved and moves forward without attending to the labor and employee relations challenges and likely conflicts that the merged organization will experience. The merged organization will bring together two firms with very different organizational cultures and labor relations traditions and systems. These different cultures will be difficult to integrate without experiencing prolonged conflicts and further declines in passenger service.

Except for its pilots, Delta is largely a non-union company while nearly all eligible Northwest employees are unionized. Historically, relations between Northwest and its employees' unions have been among the most adversarial in the industry. Thus, one of the first issues that employees in the merged organization will need to decide is whether or not they want to be organized and, if so, by which organization. Delta Airlines has a long history of seeking to avoid union representation of its employees. Flight attendants, for example, have mounted several organizing drives at Delta in recent years that met with strong resistance from the company. The top management team from Delta is expected to manage the merged organization and, if past history is an indication, it will be determined to avoid unionization of flight attendants in the merged organization. This will undoubtedly produce another drawn out and highly contested organizing process for flight attendants and other employee groups.

While it is not possible to predict the results of an organizing drive with certainty, the numbers involve predict a close and therefore highly contested election. Delta now employees approximately 13,700 and Northwest employs approximately 8,600 flight attendants. Presumably the same approximate numbers or proportions will be employed in the merged organization. Under rules of the Railway Labor Act and its administrative

[2] Carolina Brionnes and Holly Myers, *Short Changed: How airlines can repay taxpayers for billions of subsidies by improving jobs, security, and services."* Los Angeles Alliance for a New Economy: Working Partnerships USA, p. 12.

agency, the National Mediation Board, to win representation rights a majority of all employees in the unit (11,151) must vote for representation. If national trends among already represented employees carry forward, approximately 80 percent of former Northwest employees (6,880) are likely to favor representation. If the same number of employees vote to be represented as did so in the last election at Delta (32 percent or 4,384), the union will just barely gain a majority of the unit (11,264). This of course is only one possible outcome. The point is not to predict a union victory or loss. The point is all parties will expect the outcome to be uncertain but close. These are exactly the conditions that lead to the most intensive and highly contested campaigns and extended legal appeals by the losing party.

Likely Consequences of Prolonged and Intensive Conflicts

Our research has documented the consequences of a low trust workplace culture and a high or prolonged level of labor management conflict. Using data from 1987 to 2002 we tracked the effects of labor relations on the productivity, service quality, and profits of large US airlines and found that a low trust workplace culture and prolonged conflict in labor negotiations were associated with lower productivity, service quality, and profitability.[3] If, as we expect, the merger produces a similar period of low trust and high conflict, our results predict the same negative economic consequences for the merged organization. Given the fragile economic condition of these two organizations, there is little room for further decline in economic performance.

How this Negative Scenario Might be Avoided

There is an alternative. Our research shows that there are steps that can be taken to build a sustainable airline that addresses the interests of customers, employees, and investors and that contributes to the national interest of having a safe, reliable, and profitable airline industry. Our basic finding, drawn from both quantitative and qualitative research, suggests that to avoid the perfect storm and to achieve a sustainable recovery airlines need to (1) build a positive workplace culture in which the different occupational groups work together in a coordinated fashion, (2) redesign union-management processes for deciding and resolving worker representation issues and contract negotiations to avoid the long delays and protracted conflicts that have come to characterize both processes, (3) agree on a long term compensation plan in which wages of all employee groups (and managers and executives) increase in a steady, predictable fashion in relationship to overall economic trends in cost of living and in the revenues and profitability of the airline.

Given these findings, the federal government should not approve any merger unless the business plan for the merged organization specifies how management and labor leaders will deal with the following issues.

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[3] Jody Hoffer Gittell, Thomas Kochan, and Andrew vonNordenflycht, "Mutual Gains or Zero Sum? Labor Relations and Firm Performance in the Airline Industry, *Industrial and Labor Relations Review*, vol. 57, no. 2, 2004, pp. 163-179.

1. *Management and labor leaders should agree on a process for determining whether and/or which unions or associations will represent different occupational groups in the merged organization that avoids delays, conflicts, and negative/disparaging anti-union or anti-management rhetoric or actions.*

This could be done in a number of ways. A growing number of companies and unions in other industries have negotiated private "rules of conduct" governing behavior and procedures for union elections that eliminate use of disparaging comments by all parties, minimize delays and legal battles, and/or provide for neutrality or other conditions that ensure *employees* can make their own decisions on whether or not to be represented. A similar process and agreed upon rules of behavior could be worked out among the unions and the company and thereby significantly reduce the time, stress, and litigation costs associated with this process.

2. *Management and labor leaders should have a well developed plan for improving the culture of the workplace so that different occupational groups (ground crews, pilots, flight attendants, etc.) work together in a coordinated fashion with their managers to deliver reliable, high quality customer service.*

If the organizing process moves forward in the traditional highly contested and drawn out fashion, the likely outcome (regardless of whether a majority choose union representation or not) is a workplace culture fraught with tension, bitterness in the aftermath of the election ,and a workforce that continues to carry over the traditions and cultural features of the organizations from which they came. This has been the experience at the most recent large merger—i.e., the merger of US Airways and America West. Figure 1 illustrates the result: Nearly two years after the merger, the new US Airways ranked at the bottom of its peer airlines in on time arrivals, baggage losses, and customer complaints. This should serve as a clear object lesson for the new Delta and any other airlines that seek to combine organizations with different organizational cultures.

It is not impossible to avoid this same outcome. Continental Airlines demonstrated how it is possible to turn around an extremely negative and bitter workplace culture and labor relations environment after a new management team took over and brought the company out of bankruptcy in 1994. Our research shows that it was successful in doing by communicating extensively with its employees, negotiating fair but efficient labor agreements in a timely fashion, and introducing incentives and rewards for meeting on time performance and other goals that affected both the company's bottom line and the quality of customer service. The record speaks for itself. So a clear plan for learning from the Continental experience should be required.

3. *Management and labor leaders should negotiate long term labor agreements that gradually restore workers wage and benefits and secure the pension plans that remain in place by linking compensation*

adjustments to increases in the cost of living, management and executive compensation increases, and the financial performance of the firm. The parties should also be required to develop a process for assuring future agreements are negotiated in a timely fashion without resort to work stoppages.

If the different employee groups band together to demand their wage and benefits be restored to pre-concession levels, the prospect for a strike that will significantly disrupt passenger service is very high and will create strong pressure for government officials to turn to a Public Review Board and/or some other form of government intervention to resolve the dispute. Thus, waiting to deal with these issues, or dealing with them in the traditional manner, will put the company at risk and risk disrupting airline service to major cities such as Detroit, Atlanta, Minneapolis-St. Paul, and a number of smaller cities in which Delta and Northwest are now the major service providers. Steps to avoid this need to be taken now.

There are ways to reduce these risks. An increasing number of labor and management negotiators around the country have turned to state of the art "interest based" negotiations processes to resolve their conflicts and search for innovative, mutual gain solutions to their problems. Indeed, several years ago, an airline industry labor-management task force developed a set of consensus recommendations on how to improve negotiations in this industry.[4] Adapting and implementing these consensus recommendations and state of the art practices from other industries would be a practical way of achieving the type of commitment called for here.

The approach taken by the pilot unions from Delta and Northwest may serve as a model for other groups. Their respective unions, in conjunction with company representatives, have negotiated a joint agreement that restores some of the wages and benefits given up in recent years. Moreover, the unions have agreed on a process for integrating their seniority lists that provides for binding arbitration if the union representatives cannot reach an agreement on their own. By taking these proactive steps the parties have ensured that pilot labor relations will not impede the merger transaction nor risk a long drawn out representation or negotiations process after the transaction is consummated.

In summary, I believe we are facing a pivotal moment in the history of American aviation. Simply approving the merger and letting past patterns play out as expected will likely produce a financial crisis for the merged company and put more jobs, pensions, and services at risk. These consequences can be avoided by taking actions now to put in place practices that have demonstrated their value in airlines and in other industries. How government, management, and labor leaders handle this opportunity will determine whether we avert or speed up the arrival of the perfect storm looming on the horizon.

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[4] See, *Options for Improving Negotiations and Dispute Resolution: A Report of the Working Group on Airline Labor Relations,* March, 2004.

Figure 1

Service Quality Comparisons Across US Airlines

	Consumer Complaints	On Time Arrivals	Mishandled Baggage
Southwest	0.3	80.4	6.0
Alaska	0.8	71.5	6.6
JetBlue	0.8	69.3	5.8
Continental	1.1	74.7	5.7
Northwest	1.5	69.7	5.1
American	1.8	69.5	7.4
Delta	1.9	76.9	7.7
United	2.3	71.8	6.0
US Airways	3.4	68.0	8.8

Customer Complaints = complaints per 1,000 passengers, January-September, 2007
On Time Arrivals = Percent total on time arrivals, November 2006-October 2007
Mishandled Baggage = Reports per 1,000 passengers, January-September, 2007.

Sources: Transportation Department and Bloomberg Financial Markets. Reprinted from Jeff Bailey, "Fliers Fed Up? The Employees Feel the Same, *New York Times*, December 22, 2007, p. A16.