Marginal Successes, Revised Expectations, Broken Promises
– A Presidency in Review –

Part 3: No New Bankruptcy Protections for Workers and Retirees

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While on the campaign trail, presidential candidate Barack Obama promised to protect the wages, pensions, and benefits of employees and retirees who became creditors of bankrupt employer-corporations.

There were two essential prongs to Obama's campaign promise of corporate bankruptcy reform. First, bankrupt corporations would be prevented from doling out executive bonuses while wages went unpaid and retired worker pensions vaporized. Second, employee-creditors would be permitted to petition the bankruptcy court for a larger portion of their unpaid wages and benefits, giving them greater priority among ranking creditors. The first prong is discussed in this Part 3, while the second prong is discussed in Part 4.

Obama Promised Reform: Protecting Employees and Retirees with Prohibitions on Executive Bonuses from Bankrupt Corporations

A noble cause for the campaign, Obama pledged to change the bankruptcy rules to prevent corporate funds from being diverted in the form of executive bonuses from employee-creditors in the employer's bankruptcy. Specifically, Obama stated his objective:

> *"Protect the jobs and benefits of workers and retirees when corporations file for bankruptcy by telling companies that they cannot issue bonuses for executives during bankruptcy while their workers watch their pensions disappear."*

On the official website of the President-Elect, the Obama-Biden Plan to strengthen retirement savings reiterated the same promised reforms:

> *"Reform Corporate Bankruptcy Laws to Protect Workers and Retirees: Current bankruptcy laws protect banks before workers. Obama and Biden will protect pensions by putting promises to workers higher on the list of debts that companies cannot shed; ensuring that the bankruptcy courts do not demand more sacrifice from workers than*

executives; telling companies that they cannot issue executive bonuses while cutting worker pensions; increasing the amount of unpaid wages and benefits workers can claim in court; and limiting the circumstances under which retiree benefits can be reduced."

Where Is Congress on the Issue of Executive Compensation During Chapter 11 Bankruptcy?

The need for this very type of reform has been with us for at least a decade. In 2002, during the 107th Congress the U.S. Senate failed to pass the *Employee Abuse Prevention Act* which would have protected "employees and retires from corporate practices that deprive them of their earnings and retirement savings when a business files for bankruptcy." The bill was introduced in the previous session of Congress, then reintroduced as S. 2798 by Sen. Richard Durbin (D-IL) on July 25, 2002, with the support of four co-sponsors. S. 2798 died in the Senate after being referred to committee where no report followed.

BAPCPA Changed the Rules Without Stopping Executive Incentive Programs

In 2005, Congress passed the *Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA)*. Pub.L. 109-8, 119 Stat. 23 (2005). BAPCPA curtailed executive compensation during the business bankruptcy, but did not go far enough.

The problem BAPCPA addressed was the Chapter 11 business bankruptcy practice of a debtor in possession's request for a court-approved key employee retention program (KERP). Without a KERP, the bankrupt company would lose its key executives who were essential to a successful outcome in the Chapter 11 case. Not surprisingly, KERP money was typically allocated to the company's senior management and executive officers and included bonuses, severance pay, and lump-sum retention payments. All for the purpose of keeping key executives happy and committed to team bankruptcy. The KERP would help maximize the bankruptcy estate's value for the benefit of creditors, or at least that was the argument. Rational minds in Congress differed, however, on the real purpose of KERPs which rewarded the same insiders who drove the company into the ground in the first place.

BAPCPA amended the U.S. Bankruptcy Code's § 503(c) to require specific evidentiary findings before any corporate bonuses and other incentives for insider executives and officers could be ordered by the bankruptcy court. The use of KERPs was eliminated.

Were KERPs Really Outlawed or Did Corporate Bankrupts Simply Change Their Tune to Get the Same Result?

In application, the BAPCPA has offered little change from the pre-2005 KERP practice. So long as the bonus plan is called something other than a KERP, includes words like "incentivize" and "performance goals," but is not merely an effort to retain personnel or guarantee more than an executive's base salary, then the Chapter 11 judge will likely approve the plan.

House Introduced "Protecting Employees and Retirees in Business Bankruptcies Act of 2007"

The *Protecting Employees and Retirees in Business Bankruptcies Act* sponsored by Rep. John Conyers, Jr., (D-MI) on September 25, 2007, would have done much to restrain executive and insider compensation in anticipation of bankruptcy and during a pending bankruptcy case. But there was no action taken by Congress even though H.R. 3652 had 74 co-sponsors. Instead, H.R. 3652 was referred to U.S. House subcommittee where it died on the vine – no Committee report, no House vote. Of course, because the bill was introduced in a prior session of Congress (110^{th}) no more action can occur on it. That does not mean, however, that a similar bill cannot be introduced to the current 112^{th} Congress in session until January 3, 2013. In keeping with his promise of reform, would President Obama put the power of the Whitehouse behind such legislation?

Broken Promise: No Action to Curtail Executive and Insider Compensation to Protect Workers and Retirees as Creditors

The rank and file employees and retirees of the bankrupt employer are no better off now than they were prior to BAPCPA's change to § 503(c) back in 2005. When it comes to diminishing wages, benefits, and pensions while corporate insiders take as much as possible off the top, the results are the same – employees and retirees continue to lose. The reforms that candidate Obama and President-Elect Obama promised were, and are, still needed to protect the interests of workers and retirees when they become creditors in their employer's bankruptcy.

Sources:

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