SYSTEM BOARD OF ADJUSTMENT
IBT and UAL

In the Matter of the Arbitration Between: INTERNATIONAL BROTHERHOOD OF TEAMSTERS, AIRLINE DIVISION, Union and UNITED AIRLINES, INC. Company.	Outsourced Vendor Audit Grievance: Article II(D)(4) **OPINION AND AWARD**

Hearing Dates: September 20, 2007, October 4, 2007, January 31, 2008, February 2, 2008, June 4, 2008, October 10, 2008

Hearing Location: Burlingame, California
Date of Award: June 2, 2009

BOARD MEMBERS

Union Member: Jim Seitz
Company Member: Richard W. Rosinia
Neutral Member: John B. LaRocco

APPEARANCES

	For the Unions	For the Company
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SYSTEM BOARD OF ADJUSTMENT

INTERNATIONAL BROTHERHOOD OF TEAMSTERS, AIRLINE DIVISION
AND
UNITED AIRLINES, INC.

Outsourced Vendor Audit Grievance

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OPINION OF THE BOARD

I. INTRODUCTION

On April 19, 2007, the Aircraft Mechanics Fraternal Association (AMFA) initiated a grievance charging that United Airlines, Inc. (UAL or United or Company) violated Article II(D)(4) of the applicable collective bargaining agreement. AMFA and the Company stipulated that the grievance is properly before this System Board of Adjustment (SBA or Board) for a decision on its merits. [TR 6-7]

Prior to the hearing herein, AMFA and the Company entered into a July 12, 2007 written stipulation.

The issue presented to the Board is stated in Paragraphs 5.a and 12 of the July 12, 2007 written stipulation with the understanding that Paragraph 12 incorporates the penultimate paragraph of the April 19, 2007 grievance. [TR 6] Paragraphs 5.a and 12 of the July 12, 2007 stipulation read:

> 5.a. The Liability Hearing will be limited to the issue of whether the company has violated Article II-D-4 as alleged in the Subject Grievance.
>
> * * * *
>
> 12. The issue before the SBA in the Liability phase shall be: Did the company violate the contract, as alleged in the Grievance. [Joint Exhibit 2]

The penultimate paragraph of the grievance states: "The Company is in violation of Article II D of the Agreement in that the Company failed to properly calculate the percentage of outsourced maintenance work and exceeded the 20% outsourcing limit." [Joint Exhibit 2]

Paragraph 15 of the July 12, 2007 written stipulation sets forth a comprehensive confidentiality arrangement. The Board not only endorsed the confidentiality arrangement, but also issued a protective order covering all testimonial and documentary evidence. [TR 8] The Board expands the protective order to cover this Opinion and Award. Exceptions to the

protective order may only be accomplished by an order of this Board or a court of competent jurisdiction.

Also in the written stipulation, the parties bifurcated the liability phase and remedy phase. This Opinion and Award concerns the liability phase.

For several decades prior to 2003, the International Association of Machinists and Aerospace Workers (IAM) represented the class and craft of mechanics and related employees on the Company's system. On July 14, 2003, AMFA succeeded the IAM as the representative of the class and craft of mechanics. [TR 30] On April 1, 2008, the National Mediation Board certified the International Brotherhood of Teamsters, Airline Division (IBT or Union) as the exclusive representative of the class and craft of mechanics on this property. [TR 643] Thus, in the midst of the hearing herein, the IBT became the real party in interest.[1] While AMFA negotiated and entered into the July 12, 2007 written stipulation with the Company, the IBT, as the successor labor organization, is bound by the contents of the stipulation.

Paragraph 10 of the July 12, 2007 written stipulation established time limits for post-hearing briefs and rendering this Opinion and Award. The IBT and the Company agreed to extend the 30 day period for filing post-hearing briefs. The Neutral Member of the Board received the post-hearing briefs on or about January 16, 2009 and the matter was deemed submitted. At the Board's request, the IBT and the Company waived the 30 day limitation period for issuing this Opinion and Award.

As contemplated by Paragraph 10 of the July 12, 2007 written stipulation, the Board held two executive sessions after the briefs were filed.

[1] The Union member of the Board was the same individual throughout this arbitration.

II. PERTINENT AGREEMENT PROVISIONS

Article II(D) of the 1994-2000 IAM-UAL Agreement read:

> The Company may contract out up to 20% of all maintenance work annually as measured by the sum of the Maintenance Operations Division's gross annual budget plus those portions of stations' total gross annual budgets attributable to building maintenance and ground equipment maintenance, provided however this percentage may be exceeded in the event the Company has fully utilized its existing equipment or facilities. [Company Exhibit 5] [Emphasis in text]

The underscoring of all language in Article II(D) in the 1994 Agreement meant that the provision was new.[2] Article II(D) was carried forward intact into the 2000-2005 IAM-UAL Agreement which became effective on March 14, 2002. [Company Exhibit 6]

On December 9, 2002, the Company filed for Chapter 11 bankruptcy which triggered labor cost restructuring negotiations pursuant to 29 U.S.C. § 1113(c). [TR 398] As a result of these negotiations, the IAM and the Company entered into a 2003-2009 Agreement.[3] The IAM and the Company amended Article II(D) as follows:

> The Company may contract out the work of heavy maintenance visits (as defined by current Company practices consistent with AOP and MOP guidelines) without restriction. Additionally, the Company may contract out up to 20% of all remaining maintenance work annually as measured by the sum of the Maintenance Operations Division's gross annual budget, excluding the cost of heavy maintenance visits, plus those portions of stations' total gross annual budgets attributable to building maintenance and ground equipment maintenance, provided however this percentage may be exceeded in the event the Company has fully utilized its existing equipment or facilities. [Company Exhibit 7] [Emphasis in text]

While the Company was still in bankruptcy, AMFA and the Company negotiated the 2005-2009 Collective Bargaining Agreement under the auspices of 29 U.S.C. § 1113(c).[4] The

[2] The 1994-2000 Agreement was effective July 12, 1994.

[3] The parties signed the 2003-2009 Agreement on July 11, 2003 and the Agreement was effective retroactive to May 1, 2003.

[4] The Board will refer to the 2005-2009 AMFA-UAL Collective Bargaining Agreement as "the Agreement" or "the current Agreement."

prior Article II(D) language was incorporated, without any changes, into Article II(D)(4). Next, AMFA and the Company added a second paragraph. Article II(D)(4) of the current Agreement, which became effective on January 1, 2005, provides:

> The Company may contract out the work of heavy maintenance visits (as defined by current Company practices consistent with AOP and MOP guidelines) without restriction. Additionally, the Company may contract out up to 20% of all remaining maintenance work annually as measured by the sum of the Maintenance Operations Division's gross annual budget, excluding the cost of heavy maintenance visits, plus those portions of stations' total gross annual budgets attributable to building maintenance and ground equipment maintenance, provided however this percentage may be exceeded in the event the Company has fully utilized its existing equipment or facilities.
>
> Commencing in 2006, the Union shall be permitted to perform an annual audit for the purpose of verifying compliance with the outsourcing limits set forth in the preceding paragraph. Such audits shall begin no later than July 1 following the year to be audited. The Company shall reimburse the Union for the cost of retaining a mutually acceptable outside independent auditor to perform the audit, up to an annual maximum reimbursement by the Company of $75,000. The Company shall provide access to documents reasonably deemed necessary by the auditor for performing the audit. Prior to gaining access to such documents, the auditor shall execute a confidentiality and non-disclosure agreement satisfactory to the Company. Reimbursement shall be made to the Union within 30 days following the Company's receipt of the auditor's final report and proper documentation of the costs incurred in preparing the report. [Joint Exhibit 1] [Emphasis in text]

III. OVERVIEW OF THE DISPUTE

The gravamen of this grievance is what is the proper methodology for calculating the fraction that is described in the first paragraph of Article II(D)(4). The calculation of the denominator of the fraction is not in dispute. The controversy centers on the numerator. The IBT contends that all outsourced maintenance costs constitute the numerator. The Company contends that the numerator excludes outsourced material costs as well as indirect costs and so the figure in the numerator is only outsourced labor expenses. If the IBT is correct, the Company exceeded the 20% outsourcing cap in 2005. If the Company is correct, its 2005 outsourcing complied with the 20% limit.

IV. BACKGROUND AND SUMMARY OF THE FACTS

A. The Negotiating History

During the 1993-1994 negotiations, the IAM retained Tom Roth, a labor economist and President of the Labor Bureau, Inc. [TR 332, 342] Roth testified that the IAM directed him to address economic issues and value various bargaining proposals presented during the negotiations. [TR 344] Roth related that the Company sought substantial pay cuts and, in exchange, the IAM wanted "some job security." [TR 346]

Roth observed that prior labor agreements did not limit the Company's right to outsource maintenance work. [TR 346] During the negotiations, the Union initially proposed prohibiting the Company from outsourcing 90% of its maintenance work. [TR 352] As bargaining ensued, the 90% became 80%. [TR 352] Roth explained that he developed valuation models for the IAM that captured a comparison of all costs between contracting out maintenance work at 90% and contracting out the work at 80%. [TR 357] Roth stated that he and Bruce Ashby, the Company's financial planner, shared information and came "…to an agreement, actually, on what that was valued at." [TR 356] Roth related that the valuation models later expressed the percentage of work that the Company could outsource. [TR 356] Roth testified that he relied on Ashby to project savings to the Company from the incremental change from 10% to 20% of permissible contracting out. [TR 357] Roth was certain that he and Ashby put total outsourcing costs in the numerator. [TR 358] Roth emphasized that the IAM's intent was to permit the Company to contract out 20% of the total maintenance operating division's gross annual budget. [TR 346]

The IAM also retained Roth during subsequent bargaining rounds.

Roth recalled that, in February 2002 and after protracted bargaining, the IAM and the Company entered into the 2000-2005 Agreement. [TR 397, 423] Roth confirmed that Article II(D) did not change. [TR 423-424]

Roth testified that after the Company went into Chapter 11 bankruptcy in December 2002, the IAM and the Company conducted negotiations under Section 1113(c). [TR 398] Roth declared that the parties reached an agreement in April 2003, which amended Article II(D) to exclude heavy maintenance visits (HMV) from the outsourcing prohibition. [TR 398, 401] Roth stated that in his view, the definition of the numerator of the 20% ratio did not change. [TR 402] Peter Kain, the Company's Vice President of Labor and Employee Relations, testified that the amendment to Article II(D) in the 2003-2009 Restructuring Agreement excluded HMV costs from the total costs contained in the denominator of the 20% ratio. [TR 581, 587]

Kain declared that the IAM and the Company jointly created a document to memorialize changes incorporated into the 2003-2009 Agreement. [TR 588] On or about July 11, 2003, the IAM and United issued a restructuring agreement amendment, signed by Scotty Ford, President and General Chairman for the IAM, and Allan Koehler, Managing Director of Labor Relations for the Company, which, according to Kain, set forth a "mutual statement of the parties as to the changes that they are making that are reflected in the actual contract language." [Company Exhibit 10; TR 589] The parties addressed the revisions to Article II(D) on page 7 of the restructuring agreement amendments. The explanation stated:

> "Revise Article II-D (restriction on contracting out no more than 20% of all maintenance work) to provide that (a) the Company may contract out the work of heavy maintenance visits without restriction and (b) the Company may contract out up to 20% of all remaining maintenance work as currently measured by the sum of the annual budget." (Irrelevant footnote omitted) [Company Exhibit 10]

Kain recalled that, after AMFA succeeded the IAM, AMFA and the Company reached a tentative agreement in early 2005 that failed membership ratification. [TR 593] According to

Kain, a second tentative agreement was ratified by the AMFA membership in May 2005 which added the audit paragraph to Article II(D)(4). [TR 593-595] David Frizzell, an AMFA representative, elaborated that since the Company was still in bankruptcy, it sought $96 million per year in pay and pension cuts, as well as maintaining its prerogative to outsource maintenance work. Frizzell testified that because AMFA did not trust the outsourcing numbers in written reports it was receiving from the Company, AMFA proposed the new audit language. [TR 51-53]

B. Early OSV Summaries

Although not required by the 1994-2000 Agreement, the Company, in 1995, began preparing outsourced vendor (OSV) written summaries to report quarterly and annual outsource ratios. The Company furnished the summaries to the IAM. The January-December 1995 OSV summary pegged the Company's outsourcing at 6.22%, which was well below the 20% maximum. To reach that ratio, the numerator contained aggregate outsourcing expenses, while the denominator was total Maintenance Operating Department (MOD) expenditures. [Union Exhibit 15]

Roth testified that he audited the Company's 1995 OSV summary and explained the operation of the 20% ratio to IAM officers. [TR 373] Roth declared that he verified the Company's figures by comparing them to data that the Company reported on Department of Transportation, Bureau of Transportation Statistics Form 41, Schedule P6. [Union Exhibit 14; TR 370, 375] Roth emphasized that the numerator consisted of all dollars of maintenance work outsourced. [TR 377] Roth related that because the IAM reassigned him in 1997, he did not thereafter audit the Company's reported outsourcing ratios. [TR 392-393]

The Company prepared an OSV summary covering January through December 1996, which disclosed an 8% contracting out ratio. [Company Exhibit 13] A description of the

fraction states that the numerator consists of "$ of Maintenance Work Outsourced." [Company Exhibit 13]

The Company reported 11.83% outsourcing from January to December 1997.[5] [Company Exhibit 15]

C. Evidence Surrounding the Company's Change in Calculating the Numerator

Dr. Stephan G. Regulinski, who, in 1997, was the Vice President of Engine Components and Inventory, and Koehler testified about a meeting attended by Regulinski, Koehler, and IAM officers.[6] [TR 511, 535, 885, 888] Regulinski believed the meeting occurred in early 1998. [TR 526] Koehler believed the meeting occurred in late 1997. [TR 888]

Before the meeting, Regulinski concluded that the outsourcing calculation in Article II(D) had material and jobs "all bollixed up" when the purpose of the provision was to concurrently preserve jobs for the IAM and provide the Company with some cost maintenance constraints.[7] [TR 518, 520] Regulinski recognized that while the components in the numerator were from the same pool of costs as the denominator, the Company is the ultimate owner of all materials, even if material originated in a contractor's shop. [TR 520, 543] Regulinkski explained that material is either BFE (buyer [Company] furnished equipment) or SFE (supplier furnished equipment). In either event, Regulinski pointed out that the Company owns or will own all material and so, the Company does not outsource any material. [TR 521-523] Regulinski opined that including material costs in the numerator was "arbitrary." [TR 546] Regulinski declared that he read the word "work" in Article II(D) to be consistent with the notion

[5] The record does not contain the 1997 OSV summary. The 11.83% figure is reported among the historical data in the January-December 1998 OSV summary. [Company Exhibit 15]

[6] At the time of the purported meeting, Koehler was Manager of Labor Relations in the Maintenance Division. [TR 521] Koehler retired in 2008. [TR 885] At the time of the hearing, Regulinski was the President and Chief Executive Officer of Heath Tecna. [TR 507] He left the Company sometime after 1999. [TR 511]

[7] Regulinski related that he had earlier examined data underlying the OSV ratio calculation. [TR 519] At first, he unsuccessfully sought to persuade the IAM to adopt an insourcing/outsourcing offset. [TR 518, 542]

that the Company does not outsource material. [TR 544-545] Therefore, under Regulinski's analysis, Article II(D) capped the amount of labor outsourced. [TR 545-546]

Both Regulinski and Koehler testified that Regulinski consulted with Koehler about a new calculation for the Article II(D) ratio. [TR 521-522, 887] Regulinski posited, "…that we compute the percent outsource as the numerator of this fraction as the value of the labor outsourced." [TR 522] Koehler recalled that Regulinski insisted that including material costs in the numerator was erroneous since the Company farms out labor. [TR 888] According to Koehler, Regulinski asserted that he intended to change the computation of the 20% ratio in Article II(D), and Koehler responded, "Now, well, let's wait a minute. Let me go on down to the union office and see who's there from their leadership group and let me come back to your office and see what they have to say." [TR 889]

Koehler testified that, while he did not remember who, he immediately invited IAM officials located in nearby offices to a meeting 10 or 15 minutes after Regulinski briefed him. [TR 889, 894] Regulinski recalled that the IAM "leadership" that came into his office included Jerry Nelson, Scotty Ford, and Don Crawford. [TR 523-524]

Koehler testified that Regulinski gave the IAM officers a presentation on a whiteboard depicting the 20% calculation with material costs taken out of the numerator. [TR 890] Regulinski concurred that he and an analyst went over the Article II(D) ratio (on a whiteboard) by placing outsourced labor costs in the numerator and all maintenance costs in the denominator. [TR 526-527] Koehler recalled that Regulinski informed the IAM officers that the change in calculating the ratio could potentially result in farming out more work, albeit at the time, the ratio was "a ways away" from 20%. [TR 895-896] Koehler elaborated that, while the difference between the present calculation and Regulinski's calculation was apparent on the whiteboard, the numerical difference in the ratio, with the exclusion of materials, was relatively small. [TR 900-

903] Regulinski stated that he did not tell the IAM representatives about the potential consequences of the change. [TR 547, 556]

Regulinski testified that, at the meeting, the IAM officials did not say no and they did not consent to the calculation change. [TR 528] Koehler recalled that Regulinski did not ask for the IAM's consent. Rather, according to Koehler, Regulinski was informing the IAM about the proper computation of the 20% formula before Regulinski went forward with his application. [TR 897]

Regulinski recounted that immediately after he met with the IAM officers, the Company implemented the new calculation. [TR 558] Regulinski emphasized that the IAM officials did not later challenge the change in the calculation. [TR 531] Koehler stated that he heard nothing from the IAM attendees after the meeting. [TR 891] Both Regulinski and Koehler stressed that the IAM never filed a grievance over the change in the calculation of the numerator. [TR 533, 892]

Jerry Nelson, who was IAM Assistant General Chairman from 1995 to 2000, was certain that he never met with Regulinski. [TR 797, 808] Nelson declared that he would not even recognize Regulinski if he was in a room. [TR 808] Nelson stated that he looked at some records from his tenure as Assistant General Chairman and he did not find any notation of a meeting with Regulinski in 1998. [TR 811] Scotty Ford, who was Secretary of the Local Grievance Committee, asserted that the Regulinski meeting "never occurred," albeit he knew who Regulinski was. [TR 836, 839-840] Both Nelson and Ford stressed that they were never told that the Company changed the OSV ratio calculation. [TR 834, 839]

Roth testified that it is impractical to "dissect" labor costs from non-labor expenses in an outsourcing arrangement. [TR 434, 439] He explained that vendors' labor rates can vary substantially making it difficult, if not impossible, to estimate labor costs, especially since there

is no universal labor to material correlation in any vendor's bid. [TR 438-439] Roth concluded that labor costs cannot be isolated from material costs and profits on vendors' invoices to administer a limitation on an air carrier's capacity to subcontract work out to vendors. [TR 439] Nelson understood that Article II(D) was like a "pie." [TR 805] According to Nelson, Roth told him that the Company can farm out 20% of the entire maintenance budget.[8] [TR 806-807]

Regulinski claimed that the vendors' invoices specified labor charges. [TR 551] Regulinski stated that both vendors and the Company were "very interested" in separating labor from materials. [TR 555] He declared that vendors billed the Company by labor hours since, at the time, the Company was outsourcing tasks that were labor intensive.[9] [TR 553] Regulinski acknowledged that he had never contemplated what would happen if a vendor's invoice did not segregate a charge for labor. [TR 553] Regulinski also acknowledged that the vendor might "bury" some profit in the labor charges. [TR 569] He conceded that this could affect his application of the 20% ratio. [TR 553] Regulinski asserted that, rather than estimating labor expenses outsourced, he would demand that the vendor show labor costs on the vendor's invoice. [TR 553]

Roth understood that any changes in an IAM-UAL collective bargaining agreement had to be approved by the IAM Airline Coordinator at the International and was subject to membership ratification. [TR 400, 427] Roth concomitantly understood that no District IAM officer had the authority to change a substantive term in a collective bargaining agreement. [TR 400] Nelson declared that neither he nor a general chairman had the authority to agree to a substantive change in a labor agreement because an IAM general vice president must sign off on

[8] Nelson recalled that Roth and Ashby agreed to a specific value for Article II(D) that was tied to the employee stock ownership plan. [TR 807]

[9] Regulinski was certain that, at the time, the Company had actual expense data for labor outsourced. [TR 559]

any tentative agreement that the District negotiates.[10] [TR 818] Nelson also stated that the IAM Constitution required membership ratification. [TR 823] Nelson acknowledged that an assistant general chairman can resolve an issue regarding the interpretation of a collective bargaining agreement. [TR 832]

Kain understood that the District Lodge negotiated labor agreements with the Company and that the District officers could speak for the Lodge. [TR 668-669] Kain asserted that an IAM District Lodge official, like the general chairman, could enter into a binding agreement with the Company. [TR 669]

D. OSV Summaries From 1998 Through 2005

The 1998 first quarter OSV summary reported outsourcing at 10.77%. In this report, the Company started calculating the numerator as labor expenses only with a couple of minor, immaterial exceptions. In this summary, the fraction is shown numerically instead of a description. The OSV spending pie chart has the phrase "includes capital & expense" in parenthesis.[11] A footnote at the bottom of the OSV capital spending summary spreadsheet indicates that material purchases were excluded. [Company Exhibit 14] Similarly, the OSV expense spending summary shows a 66% deduction on the amount paid to General Electric for the cost of materials. For January to December 1998, the OSV summary showed a 9.14% outsourcing ratio. Next to two major vendors, the words "labour only" appear in parenthesis.

The Company adhered to the labor expense only formula for computing the numerator of the 20% ratio from 1998 through 2006. The following table depicts the OSV percentages (ratios) from 1998 through 2005, except for 2001 and 2002.

[10] During the period 1998 to 2000, Ken Thiede was General Chairman of the applicable IAM District Lodge. [TR 833]

[11] The pie chart illustrates the percentage of outsourcing in various maintenance categories with engine expense (53%) being the largest. [Company Exhibit 14]

ANNUAL OSV PERCENTAGES AS THEY APPEAR IN COMPANY OSV SUMMARIES

YEAR	PERCENTAGE
1998	9.14%
1999	12.19%
2000	11.25%
2001	Not submitted
2002	Not submitted
2003	10.18%[12]
2004	14.43%
2005	16.14%

[Company Exhibits 15, 18, 22, 32, and 36] This dispute focuses on the 16.14% result for 2005. The record contains a stipulation that "…if AMFA is correct in that contention such that other costs are properly included in the numerator – material costs and other outsource maintenance costs – that the ratio under Article II(D) for 2005 would have exceeded 20%." [TR 454-455]

The Company prepared and distributed quarterly and annual OSV reports to a wide range of recipients, including several IAM officers. For example, the January to December 1999 OSV summary was sent to Jerry Nelson and Ken Thiede. [Company Exhibit 18]

Kain emphasized that all the OSV summaries from 1998 onward disclosed that materials were excluded from the numerator. He pointed out that the January to December 1999 OSV summary showed a 66% deduction for materials from the charges of vendors GE and LH and an 85% reduction for material costs from vendor PW's charges. [Company Exhibit 18; TR 649] Kain also pointed out that the OSV vendor detail in the January to March 2000 quarterly OSV summary had a column entitled "Spending Adjusted for Materials." [Company Exhibit 19; TR 652] Most, if not all, of the reports had similar spending adjustment for materials notations under the OSV vendor detail. Kain further stated that the reports specified "Labour Only" and

[12] The Company submitted an OSV summary covering May through December 2003 reporting outsourcing at 10.18%. [Company Exhibit 26] The reports no longer restated historical data because, according to the Company, HMV costs were now fully excluded. [TR 744]

would show a percentage deduction for material costs from the amounts charged by the largest engine and air frame vendors. [TR 650-658]

Douglas Henry, Manager of Financial Planning for the Company's Maintenance Division, began preparing the OSV summaries in 2001. [TR 679, 681] He testified that the pie chart, with the heading, "OSV Spending By Work Type," in the OSV summaries was revised sometime between the January-December 2000 OSV summary and the May-June 2003 OSV summary. [TR 744-745] Henry stated that at least through 2000, the pie chart included material costs and labor costs in its depiction of the numerator. Below the heading of the pie chart in the January-December 2000 OSV summary (and prior reports), the following phrase appears in parenthesis: "includes material expense." [Company Exhibit 22] The May to June 2003 OSV summary has the pie chart with the heading unchanged, but the parenthetical expression is deleted. [Company Exhibit 23] Henry stated that the pie chart in the May-June 2003 OSV summary included only labor costs in the numerator. [TR 745] Kain indicated that the pie charts that included material expense in the numerator might lead him to believe that materials were used in calculating OSV spending. [TR 675-676]

Henry declared that to determine the numerator, the "focus program pulls data out of the Company's ledger system and the program extracts data for labor only from specific CAB accounts." [TR 688-689] Henry further declared that analysts look at vendors' invoices to discern how much of the charged amount was labor and if this is not possible, then the analysts arrive at an estimate for the labor expense.[13] [TR 697]

[13] Henry stated that the Company does not estimate labor for certain small outsourcing accounts, such as outside building maintenance, plumbing, and moving. [TR 765]

On January 13, 2004, Henry met with Jim Seitz, AMFA Contract Administrator and Coordinator, to go over the OSV quarterly summaries in more detail.[14] [Company Exhibit 24; TR 698] Henry testified that he "walked through" the OSV reports with Seitz. [TR 703]

According to a March 12, 2004 e-mail message, Kevin McCormick and Koehler met the previous Tuesday (March 9) to review the May-December 2003 OSV summary.[15] [Company Exhibit 26] In the March 12 e-mail message, McCormick asked Koehler for additional information regarding the "Review of supporting calculations used to determine the percentages used by UAL in splitting of OSV invoices between labor and materials." [Company Exhibit 26]

Henry testified that on June 2 and 3, 2004, he met with McCormick, his colleague Nicole Wilder, and Seitz to extensively explain all calculations in the 2004 first quarter OSV report. [TR 717] Henry was certain that he went through the methodologies of computing the numerator with McCormick, including the calculation for splitting labor costs from material costs. [TR 712-713, 718, 720] Henry elaborated that he showed McCormick the "labor vs. non-labor assumption for …OSV expense." Henry asserted that he also showed McCormick how the Company derived the estimated labor expense; that is, the Company estimated the labor percentage for engine OSV work based on internal Company work and expenditures. [TR 720, 754-755] Henry recalled that McCormick remarked that the calculations were "acceptable to him." [TR 721] Minutes of the June 2-3, 2004 meeting indicate that the attendees reviewed the first quarter 2004 OSV summary with supporting data. According to the minutes, both McCormick and Seitz appeared to understand the calculations and were "confident about

[14] To reiterate, AMFA succeeded the IAM as the representative of mechanics and related crafts on July 14, 2003. [TR 30]

[15] Frizzell characterized McCormick as AMFA's "number cruncher." [TR 72] In a January 31, 2005 declaration filed with the United States Bankruptcy Court, McCormick described himself as the Founder and President of the McCormick Advisory Group, which is a financial and administrative service provider. McCormick attested that he served as the National Administrator for AMFA and that his primary focus is "…the analysis of the financial aspects arising within the context of collective bargaining…." [Company Exhibit 11] McCormick was not called as a witness during the hearing.

results." [Company Exhibit 27] The minutes reflect that the AMFA participants asked for data underlying the labor and materials split calculation on engine outsourcing in the power by the hour arrangement to fully understand the calculation. [Company Exhibit 27; TR 732] Henry remembered that, after the meeting, he provided McCormick with the requested data, as well as other data, concerning CAB accounts, OSV vendor identification, labor and material cost splits and HMV expenses. [Company Exhibit 29; TR 725-726] Henry acknowledged that during these discussions with AMFA, he never informed the AMFA representatives that, at some point in the past, non-labor costs had been included in the numerator because he was unaware of any such previous inclusion.[16] [TR 748]

E. The Moss Adams Engagement, Work, and Report

Since the second paragraph of Article II(D)(4) of the current Agreement granted AMFA the right to perform an annual audit, beginning in 2005, to verify the Company's compliance with the 20% outsourcing limit, Frizzell developed a request for proposal which AMFA sent to approximately 20 auditors. [TR 57] After studying responses from several auditors, the AMFA representatives voted to retain Moss Adams, LLP.[17] [TR 58] Moss Adams is an independent, certified public accounting firm. [Union Exhibit 5]

The October 4, 2006 Moss Adams engagement letter and the attached Professional Services Agreement provided that Moss Adams was working jointly for AMFA and the Company to perform Agreed-Upon Procedures. The October 4, 2006 letter stated that the engagement is solely to assist AMFA and the Company "…in the audit of aircraft maintenance outsourcing cost percentage as submitted by United for compliance with the Collective Bargaining Agreement (CBA) between United and AMFA." [Union Exhibit 7] The engagement

[16] Henry related that he learned, in 2007, that non-labor costs were included in the numerator in the mid-1990s after one of his analysts went through prior OSV summaries. [TR 760]

[17] Moss Adams is also performing the 2006 OSV audit. [TR 219]

letter also stated that Moss Adams would apply "…the agreed-upon procedures listed in the attached Schedule A to the outsourced maintenance cost percentage of United as of December 31, 2005…" [Union Exhibit 7] A draft of this sentence had the word "determine" before the phrase "the outsourced maintenance cost percentage." A "comment" on the draft document indicates that the word "determine" was removed. A Company analyst had previously asked for this change because, according to the analyst, the Company, not Moss Adams, determines the rate. [Union Exhibit 7; Company Exhibits 1A, 1B]

Curtis P. Matthews, the Moss Adams Managing Partner in charge of the engagement and a Certified Public Accountant, emphasized that Moss Adams had no prior professional relationship with either AMFA or the Company. [TR 118, 136] He stated that the purpose of Moss Adams' audit was to follow the Agreed-Upon Procedures which had been developed by the parties and incorporated into the Professional Services Agreement. [TR 148] Matthews declared that Moss Adams was not charged with rendering an opinion on the sufficiency of the Agreed-Upon Procedures. [TR 142-143] Matthews asserted that Moss Adams followed the Agreed-Upon Procedures. [TR 155]

Matthews related that the Company supplied the information and data for Moss Adams' final report. [TR 157] Matthews further related that he and his associates performed field work, conducted interviews, attended meetings, and reviewed extensive documentation. [TR 156] Matthews testified that, at some point during the engagement, Frizzell gave him the 1996 OSV summary.[18] Matthews declared that he found subsequent reports more "unenlightening" than the 1996 report, albeit the 1996 report was not as important as the 2005 report, which was the subject of the audit. [Union Exhibit 8; TR 169, 263, 265-266]

[18] Matthews acknowledged that the Agreed-Upon Procedures did not call for AMFA to provide any pre-2005 OSV summaries. [TR 263]

Moss Adams' report entitled, "Independent Accountant's Report on Applying Agreed-Upon Procedures" is dated March 23, 2007. [Joint Exhibit 4] Moss Adams reported two OSV percentages. The first calculation resulted in 16.07% and the second calculation resulted in 30.28%. [Joint Exhibit 4; TR 201] The 16.07% was slightly under the 16.14% reported by the Company on its January-December 2005 OSV summary. [Joint Exhibit 4; Company Exhibit 36] Matthews claimed that the lower rate was the "United rate" while the higher rate was the result of the procedures. [TR 128] Matthews elaborated that 16.07% is the starting rate and 30.28% is the ending rate under Agreed-Upon Procedure 5(j). Matthews further explained that he started with the Company's calculation and then he looked for costs that were not included in the pool. [TR 312-313] However, he acknowledged that an ending rate and starting rate are not found in any Agreed-Upon Procedure. [TR 314] Matthews also acknowledged that it was not part of the engagement for Moss Adams to determine if the Company complied with the current Agreement. [TR 319]

The Moss Adams report included the following results of relevant Agreed-Upon Procedures:

> Agreed-Upon Procedure 3(c) provided:
>
> > The outsourced maintenance rate is calculated as the ratio of direct labor outsourced maintenance expense (the numerator), divided by the sum of all maintenance expense (the denominator). Expenses for heavy maintenance visits (airframe) are excluded from both the numerator and denominator, consistent with the CBA. The source for the expenses utilized in the calculation is the Organizational Expense Report (OER). [Joint Exhibit 4]

Moss Adams reported the results of Agreed-Upon Procedure 3(c) as follows:

> The outsourced maintenance rate is calculated as the ratio of direct labor outsourced maintenance expense (the numerator), divided by the sum of all maintenance expense (the denominator). Expenses for heavy maintenance visits (airframe) are excluded from both the numerator and denominator consistent with the CBA. The source for the expenses utilized in the calculation is the Organizational Expense Report (OER). [Joint Exhibit 4]

As part of the results of Agreed-Upon Procedure 5(a), Moss Adams reported that "We validated the mathematical accuracy of the outsourced maintenance rate calculation performed by United by comparing amounts used to compute the rate to the source schedules provided by United supporting the amounts used in the computation."

The results of 5(a) concluded with: "We were able to apply United's methods to recalculate the OSV rate." [Joint Exhibit 4]

Agreed-Upon Procedure 5(j) read:

> Compare domestic outsourced maintenance supplier charges as disclosed by United, identified on the United General Ledger and OER and/or included in the rate base to the outsourced maintenance rate pool charges and summarize amounts not included in the outsourced maintenance cost pool. [Joint Exhibit 4]

Moss Adams reported the following results to Agreed-Upon Procedure 5(j):

> Using the data provided by United in the worksheet titled OER Data (Purchased Mtce and Purchased Serv.) for "OSV OER" Tab undated, and the worksheet titled OSV CAPITAL SPENDING MOD Jan-Dec dated 11/6/2006, we identified amounts applicable to Outsource Vendors that were not included in the computation of the OSV ratio. Specifically, we identified $263,929,936 of OSV OER costs and $6,817,154 in Capital OSV costs that were not included in the pool in the outsourced service supplier report provided by United in the report titled, Outsource Maintenance and Outside Services Jan-Dec, 2005. We identified the costs applicable to the outsourced vendors and recomputed the ratio using total payments. To compute the total payments we used the amounts reported by United as total vendor payments from United's OSV rate calculation supporting documentation. We relied on United to identify accounts, which represented outsourced service supplier costs. We also relied on United to provide the detailed listing of activity within these accounts. A summary of procedure details is provided in Exhibit A. [Joint Exhibit 4] [Emphasis added]

Agreed-Upon Procedure 5(l) provided:

> Summarize the potential impact of any findings on the outsourced maintenance rate and validate facts surrounding audit finding through discussion with AMFA and United personnel. [Joint Exhibit 4]

Moss Adams reported the following results to Agreed-Upon Procedure 5(l):

> We confirmed through discussion with United Management that United used only estimated outsourced labor costs in the pool used to calculate the rate. We

> recalculated the rate using total outsource vendor payments. This calculation is shown in Exhibit A. [Joint Exhibit 4]

Matthews declared that Agreed-Upon Procedures 5(j) and 5(l) required Moss Adams to report both the 16.07 and 30.28 percentages with a difference of 14.21%. [TR 201, 313]

Note 1 of Exhibit A of the Moss Adams report stated:

> The indicated 16.07% OS comes from the OSV percentage and computation provided by United for the application of the agreed upon procedures. United reported a rate of 16.14% to AMFA. United did not use budgeted data to calculate this rate and did not provide budget data in sufficient detail to enable us to recompute this rate based on budgeted costs. [Joint Exhibit 4]

Note 2, pertaining to Capital MOD and MOD spending, provided the dollar amount "Represents the difference between total payments to outside vendors and the amounts used by United, which were based on estimated labor cost only (see comments in 5c and 5j in the report body)." [Joint Exhibit 4] Note 6 stated, "The total OSV Payments Column includes adjustments resulting from procedures 5c and 5j as indicated in Note 2 above." [Joint Exhibit 4] In Note 4, Moss Adams acknowledged that the Company "…defines outsourced maintenance work as the labor portion of total OSV cost." [Joint Exhibit 4]

Matthews held what he called an "exit" meeting with AMFA representatives and Company officials on March 27, 2007. [TR 158] Matthews related that he pointed out to the Company's Senior Vice President, Bill Norman, that in the past, material costs had been included in the numerator. According to Matthews, Norman replied that that was not correct. [TR 65, 177] Matthews then produced the 1996 OSV report to support his assertion. [TR 175-176] Frizzell declared that Norman seemed surprised by the 1996 OSV report. [TR 67] Frizzell also recalled that the Company contended that the 30.28% calculation was unauthorized. [TR 66]

Matthews testified that subsequent to entering into the AMFA-UAL engagement, Moss Adams performed other work for AMFA under a separate engagement. [TR 214, 216]

Matthews related that Moss Adams did not disclose the additional work to the Company, but he claimed that the added work did not undermine Moss Adams' independence when it conducted the audit of 2005 outsourcing. [TR 217-218]

Frizzell testified that after the Moss Adams report was issued, he had a conversation with Koehler wherein he learned that the Company had changed the numerator calculation to exclude material costs. Frizzell further testified that Koehler told him that the change had been shown to the IAM. Frizzell remembered that he responded to Koehler by saying that the IAM would never agree to such a change. [TR 55-56]

V. THE POSITIONS OF THE PARTIES

A. The IBT's Position

The record conclusively demonstrates that when the IAM and the Company negotiated Article II(D), they agreed to a formula that included all elements of the maintenance budget in both the numerator and the denominator. Ashby, a Company financial officer, and Roth, on behalf of the IAM, negotiated the 20% ratio. They mutually understood that the IAM was receiving job security in exchange for concessions. During negotiations, Roth and Ashby exchanged valuation examples and so they concurred on the method of the calculation. Indeed, it makes sense that Roth and the IAM would be careful not to understate OSV spending to protect IAM members from substantial Company outsourcing.

The clear language in Article II(D) confirms the Ashby-Roth understanding. The common connotation of the term "maintenance work" encompasses all of the Company's expenditures on outsourced maintenance without any exclusions.

Roth gave an expert opinion that restricting the numerator to labor costs is unworkable since there is not any universally recognized standard to dissect labor costs from the total cost of outsourced work and, thus, the Company could easily manipulate the figure placed in the

numerator. On the other hand, total outsourced maintenance costs are subject to exact verification. Roth also opined that estimating labor costs is impractical since rates can vary from vendor to vendor or be buried in vendors' profits.

The IBT also proved that the Company applied the Article II(D) formula the way it had been developed by Ashby and Roth. The first OSV summary that the Company issued included all outsourcing costs in the numerator. Roth audited the Company's 1995 figures for both the numerator and the denominator and he determined that the numbers were accurate. Thus, the bargain that the IAM and the Company struck in 1994 is uncontroverted.

The record does not contain any evidence demonstrating that any labor organization waived the bargained-for method of calculating the 20% ratio in Article II(D). The Company presented flimsy evidence of an alleged meeting with several IAM officials whereby Regulinski purportedly presented a change in the formula to which the IAM officials ostensibly consented. However, two IAM officers specifically contradicted Regulinski. No such meeting occurred. Thus, the Company's evidence of the alleged 1998 meeting between Regulinski, Koehler, Nelson, and Ford is disputed and unreliable. Moreover, Regulinski admitted that no agreement was reached at the meeting. The language in Article II(D) did not change. Koehler conceded that Regulinski unilaterally changed the method of calculating the numerator. Even if the meeting occurred, the IAM officials attending the meeting lacked the authority to change a provision in the collective bargaining agreement. Their silence did not constitute ratification of Regulinski's change in the Article II(D) formula. Also, Regulinski did not obtain the consent of any IAM official at the International.

Next, when AMFA succeeded the IAM as representative of the mechanics and related crafts, the Company deliberately concealed from AMFA that, prior to 1998, it had calculated the 20% ratio significantly different from the manner it was calculating the ratio in 2003, 2004, and

2005. Therefore, the Company's evidence merely demonstrates that it quietly changed the OSV formula without the consent of the IAM and without the knowledge of AMFA.

The Company must prove waiver by clear and convincing evidence. Neither the IAM nor AMFA intentionally relinquished a known right. From 1998 to the present, no labor organization was aware that the Company had trampled over the protection afforded by Article II(D). Without knowledge about the change in calculating the numerator, the IAM and AMFA could not surrender any right. A waiver must also be voluntary. As stated above, Regulinski went forward with revising the numerator of the formula on his own, regardless of the views of the IAM (even if they had a modicum of knowledge about what Regulinski did). Put simply, the Company did not prove any waiver of the Article II(D) formula negotiated in 1994.

The post-1997 OSV reports noted the change in the formula with obscure language and small print references. The Company never explained the contents of the OSV summaries to the IAM subsequent to 1997. The prominent portions of each summary remained unchanged which would lead a reader to believe that the post-1997 reports were the same as the 1996 and 1997 reports. More specifically, the pie chart had the same elements in the numerator in the post-1997 OSV summaries as it had in the numerator in the summaries issued prior to 1997. Only when AMFA became the representative of the class and craft of mechanics did the Company change the format for the pie charts. For the first time, the Company deleted the parenthetical expression specifying that material expenses were included in the numerator. Thus, given that the OSV reports remained substantially the same, the IAM did not waive the Article II(D) formula agreed to in 1994 .

The Company cannot rely on a past practice since AMFA was unaware of what the Company and the IAM negotiated in 1994. AMFA was furnished with, and provided explanations about, reports after the Company had already changed the numerator. AMFA had

no reason to suspect that any practice might have arisen. More significantly, once AMFA discovered that the formula had been applied differently before 1998, it promptly challenged the Company's violation of Article II(D) through the Moss Adams audit. To reiterate, since AMFA was unaware of the pre-1998 practice of applying Article II(D), AMFA could not waive the original, bargained-for application of the 20% ratio.

Finally, the Company cannot prevail on the rationale that no labor organization filed a grievance until the instant case. Without evidence that the Company exceeded the 20% limit under the IBT's construction of the 20% formula prior to 2005, no damages were incurred. A labor organization cannot pursue a grievance over a hypothetical mathematical process.

The parties stipulated that if the IBT's position is correct, the Company exceeded the 20% limitation in 1995. The IBT urges the Board to order the IBT and the Company to proceed to fashion the appropriate remedy.

B. The Company's Position

The IBT did not satisfy its burden of proving that the numerator of the OSV 20% maintenance outsourcing ratio should include costs other than labor costs.

At the onset, the plain and unambiguous language of Article II(D) refers to "20% of …maintenance work." The words "maintenance work" do not mean 20% of the total MOD gross annual budget. The terms "work" and "budget" are not synonymous. When the IAM and the Company excluded HMV from the 20% formula in 2003, they again adopted the term "work". The amendment to Article II(D) clearly stated that the "work of heavy maintenance visits" would be factored out of the numerator of the ratio. Simultaneously, the parties adjusted the denominator to exclude "the cost of heavy maintenance visits." The use of the word "work" for the numerator and the term "cost" for the denominator manifested the parties' intent that the two figures contain different expenses.

Including materials in the numerator leads to an unreasonable result. The Company either provides materials to vendors or purchases the materials from the vendors. In either BFE or SFE, the Company is the owner of the material. Whether the Company opts to purchase materials from vendors or provides the materials to the contractors, the material cost does not influence the amount of labor which is being outsourced. The origin of the materials is irrelevant and totally unrelated to job security since the Company does not outsource materials. The objective of Article II(D), preserving jobs, is unconcerned with the source from which the Company purchases materials. Roth confirmed that the purpose of the 20% ratio was to limit contracting out to preserve jobs. Therefore, the numerator was not conceived as an intended restriction on the Company's sources of purchasing materials.

Although Roth contends that the numerator must include all expenses, the negotiators could easily have written in Article II(D) that the entire outsource maintenance budget or all contracting out expenses associated with the maintenance operation should be in the numerator of the ratio; but instead, they used the words "maintenance work." In the 1994 Agreement, the word "work" appears numerous times. All of the references contemplate the ordinary meaning of "work," which is labor. The Union has not cited any provision elsewhere in the 1994 Agreement where the word "work" is inflated to include non-labor components such as material and indirect costs.

Both the bargaining history and the past practice leave no doubt that maintenance work did not include material or other non-labor factors. Only the first few OSV summaries support the IBT's interpretation of Article II(D). The 1998 summary and subsequent summaries plainly excluded materials from the numerator. Kain and Henry pointed out numerous report references that excluded material costs from amounts paid to individual vendors. The reports contain phrases like "labour only." These OSV summaries were furnished to IAM officers, including the

general chairmen. The practice was unbroken from 1998 through 2005. The IBT cannot repudiate the past practice. As the successor labor organization, it is bound by the Agreement language, the interpretations thereof, and practices. In 2007, Frizzell and Matthews boldly announced that the 1996 OSV summary was the only relevant report to determine the propriety of the methodology of applying the 20% ratio in Article II(D). They conveniently ignored the succession of consistent reports over the next decade which excluded material costs from the numerator. The post-1997 OSV summaries established an uninterrupted, unequivocal past practice which was readily ascertainable by the IAM and AMFA.

Regulinski and Koehler discussed the change to the numerator with IAM officers before making the change. Later, when AMFA became the representative of the mechanics and related employees, Henry provided AMFA's financial people with detailed data concerning the manner in which the 20% ratio was calculated. Henry held extensive briefings with Seitz and McCormick, who seemed satisfied with the calculation. The fact that neither Seitz nor McCormick was called as a witness speaks volumes about AMFA's knowledge. The Board should draw an adverse inference from the failure of Seitz and McCormick to take the witness stand.

During the 2003 restructuring negotiations, the IAM and the Company agreed that the OSV ratio would continue "as currently measured." If the IAM had been concerned that the numerator of the OSV ratio excluded material costs, the IAM should have raised its concerns at the bargaining table instead of affirming how it was being applied.

It is true that the Company agreed to the Moss Adams audit which led to the 30.28% calculation. However, Moss Adams also found 16.07% outsourcing, which is almost precisely what the Company computed. Matthews and AMFA trumpeted the 30.28% ratio as if it was some newly discovered computation when, in fact, the Company had been open about how it

applied the OSV calculation since 1998. At the exit meeting, Matthews waved the 1996 OSV report as if the Company had kept the document a secret. Matthews' conduct was analogous to the feigned indignation of the police captain who was "shocked, shocked" that there was gambling in Casablanca. Moss Adams' preoccupation with the 30.28% figure was part of the firm's strategy to satisfy AMFA so that Moss Adams could generate additional work (which it already has) from AMFA. However, Moss Adams' entanglement with AMFA impaired its independence in conducting the audit of 2005 outsourcing. Also, a close perusal of the Agreed-Upon Procedures demonstrates that Moss Adams did not have any authority to reach the 30.28% calculation. All of the Agreed-Upon Procedures refer solely to direct labor costs in the numerator. The Moss Adams engagement letter was amended to make it clear that the Company, not Moss Adams, determines the rate. Without authority, Moss Adams determined a 30.28% rate.

The Union's arguments are either unsupported by the evidence or they fail to help the IBT reach its burden of proof. While Nelson and Ford denied attending a meeting with Regulinski, both Regulinksi and Koehler were certain that the meeting occurred. Regulinski and Koehler are no longer with the Company and so, they did not have any motive to lie. Regulinski and Koehler were not entirely clear about who attended the meeting or when the meeting occurred (due to the passage of many years), but the meeting must have been held because future OSV summaries contained Regulinski's interpretation of the Article II(D) 20% ratio. The IBT also claims that only the IAM International had authority to renegotiate an agreement. However, the Company and the IAM did not bargain over Article II(D) at the Regulinski meeting. How to calculate the 20% ratio was a routine interpretation or application of existing agreement language. IAM General Chairmen and their assistants regularly interpret and apply provisions of labor agreements. Changing the method of calculation did not amend Article II(D).

Furthermore, before excluding material costs from the numerator, the parties had previously made another adjustment to the 20% ratio without changing the terminology of Article II(D). Shortly after the 1994 Agreement became effective, the Company and IAM changed the composition of the denominator. Article II(D) states the denominator consists of the gross annual maintenance budget. The parties interpreted this language to mean it was permissible to use actual MOD expenses.

In summary, material costs are not attributable to outsourcing since they are incurred whether the work is performed in-house or by an outside contractor. Therefore, it is completely irrational to now place them into the numerator of the 20% ratio.

The Company urges the Board to deny the grievance.

VI. DISCUSSION

As a product of the IAM-Company 1994 negotiations, the two parties constructed a fraction to place a 20% cap on the Company's annual outsourcing of "all maintenance work." Article II(D) described the denominator in far more detail than it described the numerator.

The denominator was composed of the MOD's "gross annual budget plus" the portion of budgets for outlying stations devoted to building and equipment maintenance. The method of calculating the denominator is clear. Yet, the IAM and the Company never adhered to this clear and unambiguous computation. Instead, they mutually applied actual, aggregate MOD and other maintenance expenses. This joint deviation from the clear language by the IAM and the Company strongly suggests that the Article II(D) fraction was more equivocal or flexible than the IBT and the Company now argue.

Turning to the numerator, "all maintenance work annually" is a broad term that is reasonably susceptible to several different definitions. As the Company argues, the term "work" can connote "labor." However, if the exclusive focus of the IAM and the Company, back in

1994, was labor expenses, they could have easily restricted the 20% ratio to outsourced labor expenses in the numerator and the sum of in-house and outsourced labor expenses in the denominator. However, the IAM and the Company included all MOD budgeted expenditures in the denominator. Since all maintenance expenses, including materials (whether BFE or SFE) constituted the denominator, the IBT's interpretation of Article II(D) is also reasonable. Therefore, when the phrase "all maintenance work" is placed in the context of the remaining language (the denominator) of Article II(D), the phrase becomes vague and ambiguous.

In addition, if, as the Company argues, the term "work" patently means "labor," the Company itself is responsible for creating an ambiguity based on how it calculated the 20% ratio in the early OSV summaries. The Company reported the numerator as all outsourced spending in 1995, 1996, and 1997. It included both material costs and labor expenses. Roth's testimony that he and Ashby mutually arrived at models to apply the 20% ratio was uncontroverted. Roth's audit of the 1995 numerator and denominator figures found that the numbers accurately reflected the computations in the models developed by Roth and Ashby. The application of Article II(D) by the Company and IAM in 1995, 1996, and 1997 conforms to the interpretation advanced by the IBT in this case.

Therefore, this Board concludes that this dispute cannot be resolved simply by interpreting the ordinary meaning of the language set forth in Article II(D) of the 1994-2000 Agreement. The language adopted by the negotiators is vague and ambiguous with respect to the numerator, coupled with the mutual deviation from the seemingly clear language regarding the denominator. In conclusion, the parties constructed a fraction that can be reasonably calculated at least two different ways.

The two different calculations were followed at different times. From 1995 through 1997, the 20% ratio was calculated in accord with the IBT's interpretation of Article II(D). From

1998 through 2006, the 20% ratio was calculated in accord with the Company's interpretation of Article II(D). The evidence demonstrates that the Company changed the calculation in 1998 to exclude material and indirect costs from the numerator.

Beginning in 1998, the Company modified the calculation for the numerator without the express consent of the IAM. Regulinski's testimony demonstrates that he intended to effect the calculation change with or without the permission of the IAM. Regulinski was adamant that the fraction had been misapplied since 1995 because, in his view, the Company never outsources material regardless of whether the materials are BFE or SFE. Regulinski firmly believed that the 1995-1997 method of calculating the numerator was erroneous because it did not reflect the true purpose (preserving jobs) of Article II(D). Consequently, Regulinski changed the composition of the numerator.

The major dispute in the record is whether or not Regulinski and Koehler provided IAM officials with advance notice of the Company's intent to change the calculation of the Article II(D) numerator. Regulinski and Koehler recalled meeting with IAM officers to illustrate the changed calculation on the whiteboard, and to entertain any reaction from the IAM officials. The testimonies of Regulinski and Koehler are directly contradicted by Nelson and Ford, who were not only certain that they never met with Regulinski about the OSV ratio calculation, but also that they were never informed about any change to the calculation. However, there is some circumstantial evidence that raises a reasonable inference that the Company imparted some notice of the numerator calculation change to local or system IAM officers. First, the fact that Regulinski sought advice from Koehler, the Labor Relations Specialist for Maintenance, before making the change, implies that Regulinski was aware that the IAM may have something to say about his contemplated change in the calculation of the numerator. Second, it logically follows that Koehler would advise Regulinski to show the IAM any change in the 20% calculation to

assess whether a disagreement could trigger a grievance. As will be discussed in the following paragraphs, it would be difficult for Regulinski to surreptitiously implement the change. The change would be obvious. Third, it is plausible that Ford and Nelson did not remember the meeting because, at the time, the calculation change did not result in a substantial modification to the ratio. When Regulinski placed the new formula on the whiteboard, the resultant ratio, without material costs in the numerator, did not vary much from the existing ratio, with material costs in the numerator, inasmuch as the Company was outsourcing labor intensive projects at the time. Fourth, Koehler's rendition was, at least, partially corroborated. When Moss Adams released its final report, Frizzell related that Koehler spontaneously remarked that the IAM had been shown the new calculation when the change was implemented. These circumstances are of sufficient probative value to permit the Board to infer that IAM officials received notice of the impending change to the composition of the numerator of the Article II(D) fraction. Nevertheless, even if the testimonies of Nelson and Ford are fully credited, the ensuing OSV summaries placed the IAM on actual notice that the Company had changed the calculation of the numerator to restrict the figure to labor expenses. The written reports, which were widely disseminated to Company and IAM personnel, are of far greater probative value than the memories of Regulinski, Nelson, Koehler, and Ford.

The 1998 first quarter and annual OSV summaries had several conspicuous references which plainly communicated to the reader that material costs had been removed from the computation of the figure in the numerator. A statement that material purchases were excluded appears at the end of the OSV capital summary. The expense summary specified a deduction for the cost of materials in the GE outsourcing arrangement. The 1998 annual report had the words "labour only" in parenthesis next to two significant vendors. These two words "labour only" appear numerous times throughout virtually all the post-1998 OSV summaries. Later reports,

such as the 1999 annual OSV summary, had a percentage deduction from the outsourcing expenditures made to three major vendors. The first quarter 2000 report had notations such as "spending adjusted for materials." It is true, as the IBT points out, that the pie chart remained the same in the post-1998 OSV summaries until the chart was amended some time between 2000 and 2003. In its depiction of the numerator, the pie chart contained all outsourcing expenses. However, this was the only information that contradicted all other data in the OSV summaries. Given the many references to excluding materials, the paradox between the pie chart and the remainder of the OSV data was readily apparent. Therefore, if IAM officers who received the report (and many did) were concerned about the contents of the pie chart, they undoubtedly would have voiced such concerns. Stated differently, the contradiction between the pie chart and the remainder of the numbers in the summaries must have been inconsequential since no IAM officer inquired about it. More significantly, there is not any evidence that any IAM officer took exception to any OSV summary between 1998 and 2003. Thus, while the OSV reports do not highlight the numerator calculation change in large, neon lights, the pervasive references to the calculation change were sufficiently conspicuous so that the IAM had actual knowledge that the Company was computing the OSV ratio, beginning in 1998, differently from the 1995 to 1997 methodology.

The changed numerator calculation matured into a past practice. The exclusion of materials from the numerator was a notorious, consistent, and uninterrupted practice. *City of Kansas City, Kansas*, 94 Lab. Arb. (BNA) 191, 194-95 (1989) (Berger, Arb.). To reiterate, the OSV summaries made no secret of the change. Since IAM officials routinely received the OSV summaries, the IAM acquiesced to the change in the calculation. *Lau Industries*, 114 Lab. Arb. (BNA) 462, 466 (2000) (Imundo, Arb.). It is highly implausible that the IAM would not have contested or grieved (or mentioned during the protracted 2000-2002 bargaining) the change to

the application of a critical contract provision like Article II(D) had they did not acquiesced to it. *Sylvania City School District,* 116 Lab. Arb. (BNA) 449 (2001) (Oberdank, Arb.).

In addition, the past practice can comport with the express language in Article II(D). If the exclusion of material costs from the numerator was truly contrary to the terminology of Article II(D), AMFA would have protested as soon as it learned that the Company used only labor expenses to determine the numerator of the 20% ratio.[19] When AMFA assumed representation of the mechanics and related employees, it rightly sought to understand if the Company was properly computing the fraction described in Article II(D). Henry testified, without any refutation, that he demonstrated the derivation of the OSV ratio reported in the OSV summaries to Seitz, McCormick, and his associate. Henry furnished Seitz and McCormick with underlying, hard data revealing the source of all figures used to calculate both the numerator and the denominator. The minutes of the June 2-3, 2004 meeting and the March 12, 2004 email message from McCormick demonstrate that AMFA's financial people were fully aware not only that the numerator included labor costs only, but that in many instances, some vendor labor expenses were estimated. McCormick reviewed and analyzed specific information about how the Company made the material/labor expense split, as well as how the Company estimated outsourced labor expenses. The record does not contain any evidence that McCormick objected to how the Company calculated the numerator. Thus, AMFA's financial expert understood that placing labor expenses only in the numerator of the OSV fraction was not a violation of the express language of Article II(D).[20] Even when AMFA learned about the pre-1998 calculation, there is not any evidence that it immediately protested the Company's exclusion of material costs

[19] It is axiomatic in interpreting collective bargaining agreements that any past practice cannot vary or alter the clear and unambiguous terms of an agreement.

[20] Inasmuch as McCormick did not testify, there is no evidence contesting Henry's testimony that AMFA representatives were satisfied with the methodology the Company used to compute the numerator. *Amoco Oil Co.*, 87 Lab. Arb. (BNA) 493, 500 (1986) (Goldstein, Arb.)

from the denominator. Instead, Frizzell tendered the 1996 OSV summary to Matthews.[21] The record does not disclose exactly when AMFA learned about the pre-1998 calculation. As the IBT argues, AMFA could not acquiesce to any past practice when it first became the representative of mechanics and related employees. Nevertheless, McCormick's acceptance of the calculation means that the exclusion of materials from the numerator is a reasonable interpretation of "all maintenance work." Most importantly, whether AMFA was aware of any past practice had been rendered moot by the 2003 restructuring agreement amendment.

On July 11, 2003, the IAM and the Company codified the past practice. Kain explained that the two parties entered into the July 11, 2003 restructuring agreement amendment to set forth a mutual statement of the parties' intent with regard to the actual contract language. When the IAM and the Company amended Article II(D) to exclude HMV expenses, they agreed in the restructuring agreement amendment that the Company "…may contract out up to 20% of all remaining maintenance work as currently measured by the sum of the annual budget." (Emphasis added) Since the main change to Article II(D) was the removal of HMV costs from the fraction, the above quoted clause would have been wholly unnecessary unless the parties wanted to be absolutely certain that the 20% ratio would continue to be measured exactly as it was being measured in 2003. The pivotal terminology "as currently measured" would be rendered superfluous under the IBT's interpretation of Article II(D). Since the IAM had actual notice of the change in the calculation of the numerator via the many OSV summaries, it agreed to formally adopt the change with the words "as currently measured." In addition, the parties modified the Article II(D) fraction by excluding HMV. In doing so, the IAM and the Company changed both the numerator and the denominator of the fraction. The "cost" of HMV was

[21] It is somewhat incongruous that Frizzell would forward the summary to Matthews rather than demanding an explanation for the change in the calculation directly from the Company.

removed from the denominator, while the "work" of HMV was removed from the numerator. If total outsourced HMV cost had been included in the numerator, the IAM and the Company would have used "cost" to describe the reduction in the numerator as well as the denominator. As the Company persuasively argues, the differentiation between "work" and "cost" for HMV in the restructuring amendment was precisely parallel with the way the Article II(D) ratio was "currently measured." Therefore, the plain language of the July 11, 2003 restructuring agreement amendment demonstrates that the parties codified the past practice (since 1998) of determining the computation of the numerator in the Article II(D) fraction.[22]

Due to the express language in the July 11, 2003 restructuring agreement amendment, the IBT did not satisfy its burden of proving that the Company violated Article II(D)(4).[23]

The Moss Adams audit was immaterial inasmuch as Moss Adams was not charged with determining whether its 30.28% outsourcing conclusion constituted a misapplication of Article II(D)(4) of the current Agreement. Moss Adams' contention that the Agreed-Upon Procedures compelled the auditor to report the 30.28% outsourcing ratio is also irrelevant because of this Board's determination that the Company properly computed the Article II(D)(4) fraction at 16.14% for 2005. Since the Board finds that the Moss Adams audit is not pertinent to the disposition of this case, the Board need not address the Company's allegation that Moss Adams' other business dealings with AMFA subverted the integrity of its 2005 OSV audit.

In conclusion, the Board holds that the Company did not violate Article II(D)(4) as alleged in the grievance.

[22] As a consequence, the IAM's Constitution concerning the approval and ratification of amendments to collective bargaining agreement provisions is irrelevant.

[23] The IBT bears the burden of proving an agreement violation. *Browning-Ferris*, 114 Lab. Arb. (BNA) 1424, 1427 (2000) (Briggs, Arb.).

AWARD AND ORDER

The grievance is denied.

Dated: June 2, 2009

____ I concur / ____ I dissent

_____
Jim Seitz
Union Member

____ I concur / ____ I dissent

_____
Richard W. Rosinia
Company Member

_____
John B. LaRocco
Neutral Member
Arbitrator