IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

In re:	)	CHAPTER 11
	)	
CEP HOLDINGS, LLC,	)	CASE NO. 06-51848
	)	(Jointly Administered)
Debtors.	)	
	)	BANKRUPTCY JUDGE SHEA-STONUM

OBJECTION OF UNITED STEELWORKERS TO DEBTORS' MOTION FOR AUTHORIZATION TO ADOPT A PERFORMANCE BONUS PLAN AND MAKE PAYMENTS THERUNDER

The United Steel, Paper and Forestry, Rubber, Manufacturing, Energy, Allied Industrial and Service Workers International Union (the "USW") states the following as its objection (the "Objection") to the Motion of Debtors and Debtors in Possession, Pursuant to Sections 105(a), 363(b) and 503(c)(3) of the Bankruptcy Code, for Entry of an Order Authorizing Them to Adopt a Performance Bonus Plan and Make Payments Thereunder (Docket No. 97) (the "Motion"):

INTRODUCTION

1. Pursuant to Section 9(a) of the National Labor Relations Act, 29 U.S.C. §159(a), the USW is the exclusive representative with respect to wages, hours, and other terms and conditions of employment of two bargaining units of employees of Debtor Creative Engineered Polymer Products, LLC (together with its debtor affiliates, the "Debtors"). The first is a production and maintenance unit at the Canton, Ohio plant and comprises approximately 150 employees. The second is a production and maintenance unit at the Crestline, Ohio plant and includes approximately 156 employees. Both bargaining units are covered by extant collective bargaining agreements.

2. The Debtors, on or about September 12, 2006, gave notice to the USW that both the Canton and the Crestline plants will be closing on a permanent basis.

THE MOTION

3. In the Motion, the Debtors seek approval of a purported management Performance Bonus Plan (the "Plan", a copy of which is appended to the Motion as Exhibit A.) As demonstrated below, the program is nothing more than a poorly disguised management retention program that fails to comply with the strictures of new Bankruptcy Code Section 503(c)(1) and (c)(3).

4. The Plan covers all or virtually all of the Debtors' management employees, to the exclusion of their rank and file workforce. (*See* Plan Section 1 and tables attached thereto.) It contemplates two "Bonus Periods"[1] and provides that if an employee voluntarily terminates his or her employment or is terminated for cause prior to the end of a Bonus Period, that employee is ineligible for payment for the period. However, if the Debtors lay off an employee during, but before the end of, a Bonus Period, that employee remains eligible to collect a bonus for that period. (Plan Section 5.)

5. The Plan contemplates two methods for calculating bonus payments. First, for plant-specific positions, *i.e.*, the employees in Tier 4 and the plant managers and the managing director in Mexico, the amount of an employee's bonus is based on the "Plant Earned Bonus Percent" which is keyed to whether that the particular plant at which the employee works "completely achieves and fulfils all of its scheduled releases" on each day of a Bonus Period-- a "Target Achieved Day". Also, if a plant has no scheduled releases on a particular day, that day

[1] The first bonus period (October 1, 2006 to October 15, 2006) has already passed and the second bonus period (October 15, 2006 to October 31, 2006) will be halfway concluded by the time the Motion is heard. The USW questions the "incentivizing" effect of the Plan if it will not go into effect until at the earliest three quarters of the way through the program's time frame. (*See* Plan Section 11: "This Plan shall become effective upon approval of the bankruptcy court… .")

still qualifies as a Target Achieved Day and a bonus that is attributable to that day is payable. (Plan Section 6(a) and (b).) For all other covered employees, *i.e.*, the top management in Tier 1A, non-plant specific managers (the Central Group) in Tier 1B and the support function managers (accounting, purchasing, payables, receivables, information services, *ect.*) in Tiers 2 and 3, the bonus amounts are also exclusively keyed on production at the plant level. Bonus amounts for these employees are based on the Plant Earned Bonus Percent for all of the Debtors' covered plants-- the "General Bonus Percent". The Plant Earned Bonus Percent or the General Bonus Percent, as the case may be, for each employee is then multiplied by the employee's Bonus Period Potential Award, which is determined by management for Tier 4 employees or is listed on tables appended to the Plan, plus amounts forfeited by other covered employees-- the "Redistribution Enhancement". (Plan Sections 5 and 6(d).)

6. Under the Plan, the 21 executives and managers in Tiers 1A and 1B may collectively receive up to $656,000, plus the Redistribution Enhancement subject to a cap of 120% of the Bonus period Potential Award. The 20 managers in Tiers 2 and 3 may collectively receive $108,000, plus any uncapped Redistribution Enhancement and the 76 managers in Tier 4 may collectively receive $500,000, plus any uncapped Redistribution Enhancement.

THE OBJECTION

A. LEGAL FRAMEWORK

7. Congress, in enacting new Bankruptcy Code Section 503(c) in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, § 331, 119 Stat. 23 (Apr. 20, 2005) ("BAPCPA"), placed significant limitations on the ability of a corporate debtor to offer retention and severance plans to insiders and prohibits transfers to executives and managers outside of the ordinary course of business that are not justified by the facts and

circumstances of the case. These amendments were the result of Congressional concern and increasing public sentiment against the practice of executives of bankrupt companies generously rewarding themselves during restructuring at the same time that rank and file workers were making tremendous economic sacrifices as a result of the process. *See In re US Airways, Inc.*, 329 B.R. 793, 797 (Bankr. E.D. Va. 2005).

8. Specifically, under Section 503(c)(1), a retention-type payment for the benefit of an insider, as defined by Bankruptcy Code Section 101(31), "shall neither be allowed nor paid" absent findings by the court, based upon evidence in the record, that (1) the individual has a job offer at the same or greater rate of compensation, (2) the services provided by the individual are "essential to the survival of the business," and (3) the payments meet a strict monetary test. 11 U.S.C. §503(c)(1).

9. In addition, Section 503(c)(3) prohibits other transfers or obligations incurred for the benefit of officers, managers and others that are outside of the ordinary course of business and "not justified by the facts and circumstances of the case." 11 U.S.C. §503(c)(3).[2]

10. Because the Plan disproportionately benefits Debtors' insiders in Tiers 1A and 1B, the Court should apply a heightened level of scrutiny in considering Debtors' Motion.[3] *In re Regensteiner Printing Co.*, 122 B.R. 323, 326 (N.D. Ill. 1990) (citing *Pepper v. Litton*, 308 U.S. 295, 306-308 (1962)) (rigorous scrutiny should be applied by a court in reviewing

[2] Although not applicable here, Section 503(c)(2) prohibits severance payments to insiders unless such payments are part of a program generally applicable to the workforce and are limited in amount to no more than ten times the amount of the mean severance pay given to non-management employees during the calendar year in which such payment is made. 11 U.S.C. §503(c)(2).

[3] Debtors' insiders covered by the Plan, at a minimum, include Chairman James Van Tiem, CEO & President Joseph Mallak, Executive Vice President Bruce Fassett, Senior Vice President of Operations David Dick, Chief Financial Officer Warren Knipple, Vice President of Purchasing Robert Poynter and Senior Vice President Quality & Lean George Pucci. 11 U.S.C. §101(31)(B).

employment contracts with insiders absent an independent trustee to ensure fairness).[4] The new provisions buttress the need for rigorous scrutiny of Debtors' Plan given Congress' clear intent that such programs be severely limited.

B. THE PLAN IS A POORLY DISGUISED RETENTION PROGRAM THAT FAILS TO COMPLY WITH BANKRUPTCY CODE SECTION 503(c)(1).

11. Debtors repeatedly characterize the Plan as a performance-based bonus program and urge that the requirements of Bankruptcy Code Section 503(c)(1) do not need to be satisfied. However, there are at least three aspects that dictate that Debtors' "performance" label is misleading. First, a covered employee who quits during a Bonus Period forfeits any bonus earned for that period, but that an employee who is laid off during a bonus period is entitled to a bonus for that period. (Plan Section 5.) Such provisions have no purpose other than encourage employees to remain with the Debtors.

12. Second, the Plan's root performance target is whether a plant makes all of "its scheduled releases" on a particular day. (Plan Section 6(a).) Normally, an incentive program encourages employees to perform at a level higher than what is ordinarily expected. *See In re Friedman's, Inc.*, 336 B.R. 891, 892 (Bankr. S.D. Ga. 2005) (debtor *raised* its prepetition performance targets for postpetition management incentive plan). In contrast, the Debtors here are proposing to reward just acceptable performance-- meeting a production schedule. There are additional built-in protections that will ensure the recognition of a Target Achieved Day even if there is no production to be shipped on a particular day or a reduction in "Capacity" due to equipment maintenance or other reasons. (Plan Section 6(a) and (c).) Further, members of management, who obviously benefit by a Target Achieved Day being recognized for a plant,

[4] With regard to an independent review of the Plan, the USW understands that the Official Committee of Unsecured Creditors will also be filing an objection to the Motion.

determine its "scheduled releases" and thus have the ability to manipulate the schedule for their benefit. These characteristics make it plainly evident that all the Debtors desire with the Plan is for members of management to show up for work and do just what is expected of them. That clearly is not a performance-based incentive plan.

13. Third, although bonuses under the Plan are keyed to production targets being met at the plant level, many of the covered employees work in support or executive positions at Debtors' headquarters in Akron or support facility in Livonia, Michigan. Debtors fail to explain how an employee such as an accountant or an accounts payable manager is motivated to do his or her job better by being rewarded on the basis what happens on the production floor at a distant plant. In addition, Debtor's executives, although at the top of the production chain of command, have, at best, a tenuous influence on whether a plant meets its production quota on a particular day. Trite expressions of the desirability of teamwork simply do not justify such a broad based group of beneficiaries. The combination of relatively easily met targets and a scope of covered employees that is far wider than the group of employees whose efforts will dictate whether the targets will be met further demonstrates that the Plan is intended to provide each member of management, no matter what function he or she performs, with a bonus so long as the manager does not quit during either of the Bonus Periods. In other words, the Plan is fundamentally a retention program with a spurious incentive aspect.

14. Debtors recognize the obvious retentive qualities of the Plan and urge approval in part because of the benefits obtained from such a program. (Motion ¶¶ 13, 29.) However, they go on to assert that the Plan is first a bonus program and that its "retentive effect" does not bring it within the ambit of Bankruptcy Code Section 503(c)(1) and cite Judge Lifland's recent decision in *In re Dana Corp.*, 2006 Bankr. LEXIS 2181 (Bankr. S.D. N.Y. 2006) (a copy of

which is appended hereto as Appendix A). (Motion ¶ 34.) To the contrary, the court in *Dana* rejected the debtors' characterization of the program before it as an incentive program:

> The Completion Bonus includes an amount payable to the Executives upon the Debtors' emergence from Chapter 11, regardless of the outcome of these cases. Without tying this portion of the bonus to anything other than staying with the company until the Effective Date, this Court cannot categorize a bonus of this size and form as an incentive bonus. Using a familiar fowl analogy, this scheme walks, talks and is a retention bonus.

Id. at *13 (footnote omitted). As demonstrated above, the Plan's retentive qualities clearly dominate any true incentive aspect. As the Plan has the purpose of inducing at least eight insiders to remain with the Debtors' business and makes no attempt to satisfy the requirements of Bankruptcy Code Section 503(c)(1)(A) through (C), the Plan should not be approved by the Court.[5]

C. THE PLAN IS NOT JUSTIFIED BY THE FACTS AND CIRCUMSTANCES OF THE CASE AS REQUIRED BY BANKRUPTCY CODE SECTION 503(c)(3).

15. Prior to the effectiveness of BAPCPA, management retention and incentive plans were commonly reviewed by bankruptcy courts under the highly deferential 'business judgment rule". *See, e.g. US Airways*, 329 B.R. at 797. With the enactment of new Bankruptcy Code Section 503(c)(3), Congress mandated an additional overlay for a court's analysis. A debtor proposing such a program now has the more exacting burden of demonstrating that the program is justified by the facts and circumstances of the particular case. To maintain that the business judgment rule still applies, as Debtors seem to be doing, would render the additional requirements in Section 503(c)(3) meaningless, which is contrary to a cardinal rule of statutory

[5] The USW expects Debtors to emphasize that the payments to be made under the Plan are being funded in large part or in full by their Participating Customers. Such fact does not take the Plan out of the Bankruptcy Code Section 503(c)(1) analysis. Such payments will be compensation paid by the Debtors from assets of the Estate and, as such, must qualify as administrative expenses. Indeed, the Debtors are seeking authority from this Court to "use… property of the estate" under Bankruptcy Code Section 363(b)(1) to adopt and implement the Plan.

construction. *E.g., TRW, Inc. v. Andrews*, 534 U.S. 19, 31 (2001). In short, the Debtors are not entitled to a presumption regarding the exercise of their business judgment, but as explained above, the Plan should be subject to rigorous scrutiny, particularly because it disproportionately benefits insiders.

16. The Plan is clearly not justified by the facts and circumstances of these cases.[6] As explained in detail above, it simply does not encourage performance "above and beyond" what is normally expected of the plant-level managers, let alone the executives and managerial personnel at the Akron headquarters and the Livonia support facility.

17. To make matters worse, the Debtors fail to take into account the deleterious effects on its rank and file workforce of implementing a generous bonus program for all of management. At a time when most of Debtors' production employees are facing the loss of a good job as a direct result of Debtors' bankruptcy filing and restructuring efforts, the Plan inequitably seeks to soften the blow of the liquidation's consequences on management**.**

18. Indeed, the bright-line exclusion of the rank and file workforce will only serve to breed strong resentment on the part of the production employees whose efforts *directly* determine whether production goals are met. The USW's already difficult task of cooperating during the production wind down at the Canton and Crestline plants will be made even more difficult if the employees view the Chapter 11 process as being tainted by significant bonuses for management while they bear the raw and brutal consequences of the liquidation. *See US Airways*, 329 B.R. at 799 (noting that the "most compelling" objection to bonus and severance program is employees' objection "that it represents a betrayal of the principle of 'shared sacrifice'"). Union support in a most difficult reorganization is an essential element of its

[6] The string citation of unreported slip orders approving management bonus programs are of little help to the Debtors. Not only do such unreported orders have questionable persuasive effect, but a court's analysis should be case and fact specific. *Friedman's*, 336 B.R. at 895.

success, a factor that is directly pertinent to consideration of the Plan. *See id*. at 799-800 (declining to approve a severance program in advance of plan confirmation, and applying a "fair and reasonable" test requiring "careful consideration of" unions' objections); *In re Geneva Steel Co.*, 236 B.R. 770, 773-74 (Bankr. D. Utah 1999) (declining to approve incentive and severance benefits because company had proposed the program without consulting with the USW, and noting evidence that the program would jeopardize employee support for reorganization).

19. Because the Plan as formulated is not justified by the facts and circumstances of this case and because of the clear potential for significant damage to rank and file employee morale, the Plan should not be approved.

CONCLUSION

For the forgoing reasons, the USW respectfully urges the Court to deny the Motion.

Dated:

October 20, 2006
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CERTIFICATE OF SERVICE

I hereby certify that on October 20, 2006, a copy of the foregoing Objection Of United Steelworkers To Debtors' Motion For Authorization To Adopt A Performance Bonus Plan And Make Payments Therunder was sent via the Court's ECF/CM system or e-mail to:

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