UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION

In re:	
PATRIOT COAL CORPORATION, ***et al.*****,**	**Chapter 11** **Case No. 12-51502-659** **(Jointly Administered)**
Debtors.	
	Hearing Date: March 18, 2013 **1:00 p.m.**

UNITED MINE WORKERS' OBJECTION TO DEBTORS' MOTION FOR AN ORDER APPROVING AND AUTHORIZING BONUS PLANS FOR CERTAIN EMPLOYEES

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1. Introduction

The United Mine Workers of America (UMWA) represents over 1700 of the Debtors' employees, comprising 42% of the Debtors' overall workforce (Schroeder Decl. ¶15, Docket #4), and about 60% of Patriot's hourly work force. The Debtors currently seek concessions from the UMWA active and retired members numbering in the billions of dollars. Such concessions will drastically reduce the standard of living for those employees and retirees, in particular their vested entitlement to lifetime guaranteed healthcare. Simultaneously, the Debtors have proposed to grant massive bonuses to corporate insiders (as well as other employees) in two programs, one of which is explicitly a retention bonus, and the other, while nominally an incentive is in reality a thinly-disguised retention bonus. At the last minute, Patriot has also attempted to circumvent §503(c)(1) by re-characterizing retention bonus payments to seven insiders as incentive payments. The combined plans seek to give management almost seven million dollars in bonus payments at a time when Patriot claims it is in dire need of concessions from its miners.

UMWA opposes these plans for several reasons. First, the plans are prohibited by 11 U.S.C. §503(c)(1) because they reward corporate insiders with retention bonus payments, and are not "ordinary course" transactions. Second, Patriot has not shown that either program is necessary—that it faces serious attrition, or that the program targets are sufficiently challenging to be true incentives. Third, Patriot has not justified the personnel selected for bonuses even when not insiders. Finally, given the imminence of a motion seeking to deprive workers and retirees of their livelihood under §§1113 and 1114, the programs are enormously inequitable.

2. The Evidentiary Showing Required To Justify These Plans is Lacking.

The evidentiary showing accompanying the Debtors' motion is tellingly thin. None of the participants in the plans are identified, even by job title. The Motion does not list their

salaries or a description of their duties, or the tenure of the employees sought to be retained or rewarded. The allegation that they are not insiders is purely a conclusion unsupported by any evidence whatsoever.

The alleged compensation benchmarks, while mentioned, are not shown to support the conclusions alleged in the declarations. No information is provided about the "comparable" companies having allegedly similar CERP and AIP plans mentioned in the Bubnovich declaration, even to show that those companies are in extractive industries like coal or in circumstances similar to Patriot's. Again, the conclusions are merely asserted; no actual evidence is provided.

There is moreover no proof that executive flight is a serious risk or an explanation where the fleeing managers would go, given the limited number of mining operations in the eastern United States. There is no analysis of the compensation levels in mining in other parts of the United States, the number of alternative job opportunities in this economy, or the difficulty literally hundreds of Patriot managers would have in trying to find jobs in mining. Because no job titles or duties are given, the Court has no basis to conclude that the managers have transferable skills.

The Court is given almost no information to gauge whether targets in the AIP program are challenging or easily achievable, and no information whatsoever on how any participant's job duties relate to achievement of any target. The targets are not quantified relative to the amount of the bonus, so it is unclear whether the bonuses threaten the Debtors' liquidity rather than act as incentives to foster it.

In short, the Debtors' evidentiary showing is woefully inadequate. This lack of showing is by itself enough to deny the motion. See In re Residential Capital, LLC, 478 B.R. 154, 171-

172 (Bankr. S.D.N.Y. 2012)(finding the "evidence Debtors have submitted supporting their assertion that the KEIP is primarily incentivizing is generally conclusory" and denying the motion); In re Regensteiner Printing Co., 122 B.R. 323 (N.D. Ill. 1990)(representations of counsel on the record, even in the absence of an objection, are insufficient to support bonus program that pays compensation as an expense of administration; evidentiary record is essential, and burden of proof is on employees asserting they are entitled to bonuses); In re Club Dev. & Management Corp., 27 B.R. 610, 613 (9th Cir. BAP 1982)(same).

3. The CERP and AIP Programs Are Illegal Insider Retention Plans

What little can be gleaned from the motion is not reassuring. The Debtors propose two different bonuses covering 274 salaried employees—a Critical Employee Retention Plan (CERP) covering 112 employees and an Annual Incentive Plan (AIP) covering 225 employees, 63 of whom are also in the CERP. The maximum value of the combined bonus plans is $6.9 million. Several proposed CERP and AIP participants participated in the development of the CERP and AIP programs, thus indicating a conflict of interest.

The CERP provides payments totaling approximately $4.5 Million to CERP participants on the condition that they remain with the Debtors in the course of the bankruptcy. The CERP is thus explicitly and entirely retentive in purpose. (See Motion ¶29). The proposed payments total between 11% and 45% of a participant's annual base salary and are payable in three installments—March 31, 2013, September 30, 2013 and after emergence from bankruptcy.

The 112 proposed CERP participants comprise 3% of the Debtors' overall workforce. Even following the debtor's withdrawal of seven insiders from the CERP program, participants remain largely limited to high-level executives, including one senior vice president and twelve other vice presidents. Other participants include Operations and General Managers, including

one General Manager that also serves on the Board of Directors of a subsidiary debtor, and other managerial and salaried employees.[1] Patriot's voluntary withdrawal of a senior counsel from the CERP as an insider is a clear indication that insiders at Patriot are not limited to those holding the title of Vice President or above.

The 225 proposed AIP participants comprise 5.6% of the Debtors' overall workforce. The AIP ostensibly depends on Patriot achieving performance metrics, some defined and some undefined, at a minimum threshold basis. AIP bonuses range from 1.25% to 15% of salary for all but the seven late withdrawals from the CERP; for them, AIP payments range from 43% to 61% of annual salary. AIP participants include a wide variety of employees, ranging from an administrative assistant first employed by the Debtors nine weeks ago to Senior Vice Presidents. The AIP is to be allocated so that the EBITDAP and liquidity components each account for 30% of the overall bonus. Safety, Environmental regulatory compliance, and Mine Safety and Health Administration regulatory compliance goals account for an additional 5% each. The remaining 25% is based upon the achievement of unspecified, individualized goals. As is shown below, this plan is in reality a disguised retention bonus, particularly for the seven late withdrawals who are now receiving the entirety of their formerly proposed CERP payments through the AIP.

The combined programs are designed for the benefit of a very few—the top 35 Officers and General and Operations Managers account for 13% of the participants, but 42% of the CERP payments and 61% of the AIP payments. These people are plainly insiders of the Debtors. As is shown below, the Debtors have failed to meet the heavy evidentiary burden required to justify plans such as these.

[1] At least one General Manager also holds the title of President at a subsidiary mine debtor.

ARGUMENT

I. The Proposed Payments Are, To The Extent Made To Insiders, Prohibited by 11 U.S.C. §503(c)(1).

A. Bonus Programs Are Unsavory And Are Held To A High Standard.

Congress has expressed very strong distaste for bonus programs which result in the personal enrichment of the very executives responsible for leading a company into bankruptcy. Such programs are an enormity in the bankruptcy world, as they impose hardships on employees and small creditors, while rewarding bankruptcy management with bonuses as priority expenses. The court stated in In re US Airways, Inc., 2005 Bankr. LEXIS 1764 (E.D. Va. 2005):

> [Retention bonus programs] have something of a shady reputation. All too often they have been used to lavishly reward—at the expense of the creditor body—the very executives whose bad decisions or lack of foresight were responsible for the debtor's financial plight. But even where external circumstances rather than the executives are to blame, there is something inherently unseemly in the effort to insulate the executives from the financial risks all other stakeholders face in the bankruptcy process.

Id. at *11. Congress essentially outlawed such programs in revised and amended 11 U.S.C. §503 in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA), Pub. L. No. 109-8, § 331, 119 Stat. 23,102-03 (April 20, 2005), except upon very rigorous showings of need. See William Houston Brown, Lawrence Ahern III, *2005 Bankruptcy Reform Legislation with Analysis*, BAPCPA 59 (Westlaw May 2005); In re Global Aviation Holdings Inc., 478 B.R. 142, 147 (Bankr. E.D.N.Y. 2012)(in BAPCPA, Congress erected a "set of challenging standards" and "high hurdles" for the payment of retention bonuses to insiders)(citing In re Global Home Products, LLC, 369 B.R. 778, 784-85 (Bankr. D. Del. 2007)).

Section 503(c)(1) prohibits a debtor from paying a bonus to any insider "for the purpose of inducing a person to remain with the debtor's business," unless the Court finds that "the individual has a bona fide job offer from another business at the same or greater rate of

compensation" and "the services provided by the person are essential to the survival of the business." The transfers are also limited in amount to either 10 times the average amount given to "nonmanagement employees" or 25% of the amount paid to the insider in the previous year. 11 U.S.C. §503(c)(1). Here, the Debtors do not allege that any employee has received a job offer and do not allege the specific necessity of any particular individual plan participant.

The CERP is explicitly a retention program covered by §503(c)(1). While the Debtors have labeled the AIP as an "incentive" rather than a retention bonus, this difference in nomenclature is immaterial. The "firestorm of controversy" surrounding bonuses which led directly to enactment of this provision in BAPCPA was not that executives of bankrupt companies were being paid *the wrong kind of bonus*, but rather that they were being paid any bonuses that would ultimately come from distributions to creditors, lost benefits to retirees, or concessions demanded from rank-and-file employees. [2] In issuing a statement to the Senate Judiciary Committee opposing BAPCPA, the Association of Insolvency and Restructuring Advisors advised Senator Arlen Specter that the amendment "is designed to prevent abuses of the system, where creditors' employees' *and retirees'* monies are unnecessarily expended for the enrichment of management." 151 Cong. Rec. S 2306, S2341 (March 9, 2005)(emphasis added). It is obvious from the phrasing of the issue in this statement of opposition that the opponents

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[2] See Kaplan, "*Executive Compensation Issues Under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005*," Benefits Practice Center, Executive Compensation Library, Journal Reports: Law and Policy (BNA 2005) at n. 28 (collecting contemporary reports of bonus scandals in Enron and other cases). Senator Kennedy, author of the amendment which became the new provisions prohibiting bonus plans in 11 U.S.C. §503, stated repeatedly in the legislative history of BAPCPA that the evil to be remedied was the payment of bonuses to executives in Chapter 11, whether called "incentives," "KERPs," or otherwise, and specifically referred to "incentive payments" as one form of insider payment the amendment was meant to curtail. The Kennedy Amendment was one of several attempts to eliminate such bonuses. Provisions initially contained in the Employer Abuse Prevention Act of 2002, H.R. 5221, 107th Cong., 2d Sess. (2002) and S.2978, 107th Cong., 2d Sess. (2002), and earlier versions of BAPCPA, were designed to address the same abuses. Proponents of this bill did not limit their targets to "retention" bonuses alone, but to all forms of "windfall" and "incentive."

perceived it was the payments to management themselves, not the names given to the payments, that were at stake.

Congress thus made clear that retention bonuses, whether overt or disguised, are disfavored. The language of 11 U.S.C. §503(c)(1) is broad, and condemns all transfers and obligations if any purpose of the transfer is to induce the insider to be employed in the Debtors' business. It is not limited to prohibiting bonuses labeled retention bonuses as such.

Given the legislative history, a "threshold question" is whether the AIP "is a true incentive plan, or instead, a disguised retention plan." In re Hawker Beechcraft, Inc., 479 B.R. 308, 312-313 (Bankr. S.D.N.Y. 2012). The proponent of an incentive plan bears the burden of proving that the plan is not a retention plan governed by §503(c)(1). In re Residential Capital, LLC, 478 B.R. 154, 170 (Bankr. S.D.N.Y. 2012). That is, the proponent must show that the targets in the incentive plan are designed to motivate employees to rise to the challenge, as opposed to paying them a bonus for showing up to work. The Debtors must demonstrate that the payee of the bonus will contribute services necessary to attaining the performance targets only if he receives the promised incentive. Hawker Beechcraft, 479 B.R. at 312-313. Accord Dana Corp., 358 B.R. 567, 576 (Bankr. S.D.N.Y. 2006). As noted above, the Motion comes nowhere close to making this showing.

B. The Debtors Must Show that the Proposed Program Does Not Include Insiders.

The plans are thus illegal for any participant who is an insider. Under 11 U.S.C. §101(31)(B), an "insider" includes any "(i) director of the debtor; (ii) officer of the debtor; [or] (iii) person in control of the debtor." The use of the phrase "nonmanagement employees" in §503(c)(1)(C) to identify non-insiders is also telling: Insiders for purposes of bonuses is meant

to include anyone in the management of the company. The CERP and AIP provide illegal retention payments to at least 35 insiders and perhaps many more.

While the Debtors assert that the program covers only non-insiders, (Hatfield Decl. ¶5), they cannot escape the reach of §503(c)(1)'s severe limitations with a bare assertion. "To avoid the strict requirements of section 503(c)(1), *a debtor must show that the proposed transfers are not to insiders* of a debtor or, if the recipients of the proposed transfers are insiders, that the transfers are not being made for the purpose of retaining those insiders." In re Residential Capital, LLC, 478 B.R. 154, 169 (Bankr. S.D.N.Y. 2012) (emphasis added). The burden is on the debtor to prove that none of the CERP or AIP participants are insiders. A finding that bonus recipients are insiders is fatal to the Motion. See In re Global Aviation, 478 B.R. at 147

The Debtor's CERP proposes retention payments to one Senior Vice President, twelve Vice Presidents (one other Senior Vice President and six other Vice Presidents are not eligible for the CERP, but eligible for the AIP, including the Debtors' corporate secretary and treasurer), its Chief Information Officer, an Assistant Secretary, and several General, Operations and other Managers, all of whom are prohibited insiders pursuant to §503(c)(1), and thus ineligible for a retention payment absent a showing of a competing job offer. Among these proposed participants are at least one Vice President and several unidentified members of management who participated in the formulation of both the CERP and AIP on the Compensation Committee. All of these individuals are properly considered "insiders" as contemplated by Congress in prohibiting retention and similar payments to insiders unless very specific criteria are met.

Because the statutory definition is in the disjunctive, it is sufficient that an insider is either a director, an officer *or* a person-in-control. In re Public Access Technology.com, Inc., 307 B.R. 500, 505 (E.D. Va. 2004). Status as a director or an officer is alone sufficient to establish

the person as an insider. Id. While "control" is an independent additional ground for finding insider status, it is not a feature that officers or directors are required to possess to be deemed insiders. Office of the U.S. Trustee v. Fieldstone Mortgage Co., 2008 U.S. Dist. LEXIS 91479, *18 (D. Md. Nov. 5, 2008). "[T]here is no rational basis under the plain meaning of the relevant words to further limit the definition of officers to those 'in the collective group exercising overall authority regarding the debtor's corporate decisions.'" In re Foothills Texas, Inc., 408 B.R. 573, 581 (Bankr. D. Del. 2009).

"A person holding the title of an officer, including a vice president, is presumptively what he or she appears to be—an officer and, thus, an insider. To overcome that presumption requires the submission of evidence sufficient to establish that the officer does not, in fact, participate in the management of the debtor." Foothills Texas, 408 B.R. at 583. The Debtors' vice presidents and chief information officer are plainly statutory insiders. Not only do they hold titles that suggest officer status, the Debtor's bylaws conclusively establish officer status. Delaware law requires that the officers be stated in the bylaws. 8 Del. Code § 142(a). Patriot Coal Corporation, the lead debtor, is a Delaware Corporation and provides in §3.2 of its bylaws (entitled "Principal Officers") for, among others, "one or more Vice Presidents, a Secretary, a Treasurer and such other additional officers with such titles (including, without limitation, a Chief Operating Officer and a Chief Financial Officer) as the Board of Directors shall from time to time determine, all of whom shall be elected by and shall serve at the pleasure of the Board of Directors." The Bylaws thus conclusively establish insider status for Patriot officers who remain in the CERP.[3]

[3] Even in cases where a court has ruled that a title alone failed to establish "officer" status, bylaws or other corporate paperwork are evidence of officer status, regardless of "control." Cf. Smith v. Ruby (In re Pub. Access Technology.com, Inc.), 307 B.R. 500, 506 (E.D. Va. 2004) ("[t]here are no affidavits, articles of incorporation, corporate minutes, resolutions, or any documents or evidence that show this title makes Smith an officer of the corporation.") Here, there are such documents, and they show insider status.

In at least the case of one affiliated debtor, Newtown Energy, the Authorization is executed by members of the Board of Directors, one of whom is a plan participant. Directors are among the specifically enumerated "insiders" set forth at 11 USC §101(31)(B). Any person that is a director of a corporate debtor is automatically an insider. Public Access Technology.com, Inc., 307 B.R. at 505.

The Debtors' Compensation Committee, in consultation with the Senior Vice President of Law and Administration, the Vice President of Human Resources and other members of management, developed the CERP and AIP and assisted the Debtors' advisors in assembling the bonus programs. Several individuals who assisted in the development of the bonus programs are participants in the CERP, AIP or both. They therefore had input and control over the disposition of the Debtors' assets at least with respect to the proposed bonus programs. Such control renders them insiders pursuant to §503(c)(1), prohibited from receiving such payments. Alternatively, even if such individuals are not "insiders," their participation in developing the CERP and AIP has an element of self-dealing which requires that the Court apply a standard greater than the business judgment standard in evaluating the proposed bonus plans. E.g., Pepper v. Litton, 308 U.S. 295 (1939); Regensteiner, supra. Insider status under the "person-in-control" provision of §101(31)(B)(iii) should be determined, at least in part, by reference to the payment recipient's control of the specific transaction under consideration and the impact of that transaction upon the debtor's creditors. In re CEP Holdings, LLC, 2006 Bankr. LEXIS 3305 (Bankr. N.D. Ohio Nov. 28, 2006).

Seventeen well compensated General and Operations Managers, some of whom make salaries comparable to the insiders described above, should also be deemed insiders. In addition to specifically identified officers or directors, whether a corporate manager is an "insider" should

be determined on a case-by-case basis on the totality of the circumstances, including the degree of the individual's involvement in a debtor's affairs or control over the disposition of corporate assets. In re Borders Group, Inc., 453 B.R. 459, 469 (Bankr. S.D.N.Y. 2011). The lack of a formal title is irrelevant. See, e.g., Matter of Krehl, 86 F.3d 737, 741 (7th Cir. 1996) (noting that the "definition [of insider] is intended to be illustrative rather than exhaustive")(citation omitted); Boyd v. Petrie (In re Tompkins), 430 B.R. 453, 459 (Bankr. W.D. Mich. 2010)("By using the word 'includes' in the statute, the definition of 'insider' is illustrative and not limiting..").

The intent of §503(c) is widely recognized to be to "limit the scope of 'key employee retention plans' and other programs providing incentives to *management* of the debtor as a means of inducing *management* to remain employed by the debtor." 4 COLLIER ON BANKRUPTCY ¶ 503.17 (15th ed. rev. 2007). "[T]he question is whether a person is taking part in the management of a debtor," and the law neither states nor implies that management of the debtor must be at the most senior level to qualify. Foothills Texas, 408 B.R. 573, 574 n.23. Many proposed CERP participants are high-level managers; the relationship between the Debtors and these managers is more than simply an employer-employee relationship. These individuals manage the subsidiary Debtors' mines and exert substantial control over the day-to-day operations of the respective Debtors in that capacity—they make strategic decisions and commit corporate assets. The Managers are vested with sufficient control so that they should be considered insiders, consistent with the Congressional purpose of section 503(c)(1). See, e.g., Lee's Place v. Hawbaker, 1992 U.S. Dist. LEXIS 10147 (C.D. Ill. 1992)(person who managed debtor and controlled day-to-day operations was insider); In re Standard Stores, Inc., 124 B.R. 318 (Bankr. C.D. Cal. 1991)(general manager was insider); In re National Real Estate Ltd. Partnership II, 87 B.R. 986, 991 (Bankr. E.D. Wis. 1988)(debtor's property manager was an

insider). It is simply impossible to believe that the Debtors' six excluded executives and seven recently excluded CERP participants are the only ones making decisions regarding the Debtors' dozens of mine complexes and mines.

C. Because the Debtors Fail to Meet the Requirements of Section 503(c)(1)(A) and (B), the Motion Must be Denied.

The Debtors did not allege that any single CERP or AIP participant has a bona fide job offer for alternative employment. The Debtors thus failed to meet the requirement of 503(c)(1)(A), strictly prohibiting retention bonuses to insiders who do have job offers in hand for more money. Similarly, the Debtors have not met the burden to show that the services provided by any particular person are essential to the survival of the business, thus failing to meet the requirement of 503(c)(1)(B). In re Hawker Beechcraft, 479 B.R. 308, 313 (Debtors failed to meet burden where they did not identify how managers would contribute services necessary to achieve targets). Either failure alone is sufficient to defeat the Debtors' Motion, which must for this reason be denied at least until the Debtors establish that specific employees are not insiders.

II. The Business Judgment Standard Is Not The Appropriate Standard Here.

A. The Bonuses Are Not Ordinary Course Transactions.

Despite the Debtors' contention that the plans here are "in the ordinary course of business," they plainly are not. Retention programs for the duration of a bankruptcy are by definition not "ordinary course" transactions as they can apply only in the extraordinary case of bankruptcy. The business judgment standard therefore does not apply to any retention program subject to §503(c)(1). In re Dana Corp., 351 B.R. 96, 101 (Bankr. S.D.N.Y. 2006)("business judgment rule does not apply, irrespective of whether a sound business purpose may actually exist"). The Debtors fail to cite a single case holding that a retention plan should be analyzed under the "ordinary course of business standard." One of their citations, In re Global Products,

369 B.R. 778, 786 (Bankr. D. Del. 2007), held that the ordinary course analysis applied precisely because plan was a true incentive, and only accidentally retentive, which is not the case here. The Debtors likewise have not produced any evidence showing that it is within the practice of the coal industry to offer retention plans to employees. The Bubnovich declaration in ¶28, the only authority it cites for this proposition[4], states merely that in his belief the CERP is consistent with market practice, and does not address practice within the coal industry at all.

The vertical test for ordinariness focuses on whether creditors expect and accept similar risks inherent in the transaction when they become creditors. In re Glosser Bros. Inc., 100 B.R. 268, 270 (Bankr. W.D. Pa. 1989). See also Armstrong World Indus. v. James A. Phillips, Inc. (In re James A. Phillips, Inc.), 29 B.R. 391, 394 (S.D.N.Y. 1983) (the touchstone of ordinariness is the interested party's reasonable expectations of what transactions the debtor in possession is likely to enter in the course of its business). Here, the pre-2012 retention plan offered by the Debtors was for its mine-level personnel only, and not its corporate employees. (Hatfield Decl. ¶8) Debtors indeed did not promulgate a corporate-wide retention plan until June 2012, scant weeks before the July 9, 2012 bankruptcy filing. (Hatfield Decl. ¶8). The risk that the Debtor would take money that belongs to its creditors to fund a retention program for insiders and other corporate employees therefore was not one that Patriot's creditors assumed. Patriot's retention program fails both the horizontal and vertical tests, and requires court approval.

B. The Debtors Must Therefore Meet the More Rigorous Scrutiny Standard to Justify Bonuses.

To the extent that section 503(c)(1) applies, the transfer cannot be justified on a debtor's business judgment. Pepper v. Litton, 308 U.S. 295, 306-307 (1939)(involving a key employee

[4] While ¶18 of the Bubnovich Declaration stated that the Debtors' "peer firms" routinely offered incentive based cash payments, it does not address whether it is industry practice to offer retention bonuses. The declaration is also opaque as to whether "peer" means "coal industry" for purposes of the horizontal part of the ordinary course test.

bonus compensation/retention program). Speaking of "officer[s], director[s]" and "stockholder[s]," the Court said "*[t]heir dealings with the corporation are subjected to rigorous scrutiny* and where any of their contracts or engagements with the corporation is challenged the burden is on the director or stockholder not only to prove the good faith of the transaction but also to show its *inherent fairness from the viewpoint of the corporation* and those interested therein." Id. at 306-307 (emphasis added). While Pepper applied this general principle to a case of equitable subordination, the rule remains that courts should protect estates from self-dealing by highly-placed corporate officials who fail to fulfill their fiduciary duties. Courts apply this rigorous standard in any matter where corporate decision-makers are personally interested. E.g., In re Regensteiner Printing Co., 122 B.R. 323 (N.D. Ill. 1990) (bonus program disapproved because standard for reviewing transactions between insiders and debtor is not business judgment, but rigorous scrutiny); In re Borders Group, Inc., 453 B.R. 459, 470-471.

> Given the obvious conflict of interest between a debtor's estate and insiders -- who may themselves have been responsible in whole or part for devising and internally approving the proposed transaction -- the argument underlying application of the business judgment rule (that officers and directors will fulfill their fiduciary responsibilities) lacks its usual weight.

In re Pilgrim's Pride Corp., 401 B.R. 229, 237 (Bankr. N.D. Tex. 2009). "[W]hen a transaction is proposed between a debtor and its insiders, the court cannot simply rely on the debtor's business judgment to ensure creditors and the debtor's estate are being properly cared for." Id.

C. The AIP Is A Disguised Retention Bonus.

While the CERP is clearly prohibited by §503(c)(1), the AIP is ostensibly covered by the business judgment standard under §503(c)(3). The real purpose of the AIP is however more retentive than incentive, and it should be judged under the rigorous standard of §503(c)(1) as well. See Hawker Beechcraft, 479 B.R. 308, 312 ("threshold question" "is whether the [plan] is

a true incentive plan, or instead, a disguised retention plan"). A debtor bears the burden of proving by a preponderance of the evidence that a proposed incentive plan is primarily incentive, not primarily retentive and governed by § 503(c)(1). In re Residential Capital, LLC, 478 B.R. 154, 170 (Bankr. S.D.N.Y. 2012). Attempts to characterize what is essentially a prohibited retention program as an "incentive" program to bypass the requirements of §503(c)(1) are disfavored; the courts consider the underlying circumstances along with the structure of the bonus package to determine whether the plan is subject to §503(c)(1). In re Borders Group, Inc., 453 B.R. at 470.

The payments to the seven high-ranking Patriot officials, recently excluded from the CERP, are clearly retentive in nature. In the face of the United States Trustee's objection that the seven officials are insiders, Patriot simply relabeled the proposed payments as AIP payments rather than CERP payments. In deciding whether a proposed incentive program is in fact a disguised retention program, the Court should analyze whether the plan was designed to achieve specific goals, as well as the circumstances under which the proposal was made. In re Residential Capital, 478 B.R. at 170. Having previously represented to the court that AIP payments of between 5% and 15% were sufficient to motivate the seven insiders to achieve Patriot's operational objectives, Patriot cannot credibly argue that offering the seven insiders an additional bonus of between 35% and 45% is necessary to motivate them to achieve the same operational objectives. Patriot's primary motive in making the additional payments is therefore retentive rather than incentive, so that the additional bonuses should be analyzed under §503(c)(1).

The Debtor and each subsidiary Debtor also granted "Authorized Officers" the authority to commence bankruptcy proceedings on their behalf in Written Consents filed with the

voluntary petitions. The "Written Consent" for the vast majority of the Debtors in these cases was signed by the Corporate Vice President and Treasurer who is a Participant in the disguised CERP. "Authorized Officers" in the lead case were vested with significant authority to dispose of and commit the filing debtor's assets, including the powers to execute and file pleadings in the chapter 11 case, to retain legal and financial advisers, "and to take and perform any and all further acts and deeds that any such Authorized Officer deems necessary or desirable in connection with the Company's chapter 11 case." (Case No. 12-51502, Doc. 1, p. 15-18) Authorized Officers were also "empowered to enter into the Credit Agreement and each of the other Loan Documents, to borrow under the Credit Facilities at such times and in such amounts as any Authorized Officer shall deem necessary or advisable." The Debtors in each of the connected cases filed nearly identical authorizations, except they define "Authorized Officer" as "the President, Treasurer, Secretary and Assistant Secretary," and vest those individuals with the same far-reaching authority. (See, e.g., Newtown Energy, Inc., Case No. 12-52091, Doc. 1, pp. 15-18). Authorized Officers exercise significant control over the Debtors; they are insiders. The Debtors have similarly declared that other recipients of the disguised CERP payments are responsible for managing its operations.[5]

Patriot's originally proposed AIP payments are similarly retentive in nature. The payments are not made unless the employees remains employed through the target payment dates, a hallmark of a retention program. The target and threshold liquidity and EBITDAP figures are derived directly from Patriot's five year plan, i.e., targets that Patriot was projected to

[5] For example, one bonus plan participant is a senior vice president about whom the debtors declared in a press release: He "has a wealth of experience overseeing top-notch mining operations. We look forward to his contributions as we continue to enhance the production and safety performance of our underground mines. Further, as coal markets rebound and Patriot returns its focus to growth, [his] broad expertise in designing and developing new mines and in evaluating acquisitions will add valuable insight to our team." The subject individual in the same release was said to "have management oversight responsibility for the Panther and Federal longwall mines, as well as Patriot's Valley Operations including the Big Mountain, Wells, Rocklick and Harris complexes." It beggars credulity that such a highly placed executive is not an insider of the Debtors.

reach. These targets constitute 60% of the bonus formula; thus the majority of the bonus is likely to be paid. Liquidity forecasts alone account for 30% of the target metric and the Debtors are ahead of forecast in this category.[6] Given that the Debtors need to achieve the liquidity targets to avoid violating their liquidity covenant and remain on track for a successful reorganization, 60% of the AIP payments are a reward simply for keeping the debtors on track to reorganize and emerge from bankruptcy (even if the debtors are ultimately unsuccessful), which is not a challenging target. In re Residential Capital, 478 B.R. at 172-172 (Payments based on successful reorganization or emergence from bankruptcy are retentive, even if substantial increased effort by participants would be required to achieve a successful reorganization). The removal of pension expenses from EBITDA obviously makes the target even easier to achieve. Achievement of at least some of the Safety, Environmental regulatory compliance, and Mine Safety and Health Administration regulatory compliance goals is virtually guaranteed.

The retentive focus of the AIP is further illustrated by the individual performance metric of the program. The AIP program pays out partial bonuses if some but not other metrics are achieved. The Debtors have not provided the Court with any explanation of what the individual performance metrics will be or how the individual performance metrics will be set. Because the Debtors seek to set individual performance metrics and pay bonuses essentially in secret, there is no assurance the metrics are not retentive in nature. Courts have refused to give debtors similar blank checks to pay discretionary bonuses. In re Dewey & Leboeuf LLP, 2012 Bankr. Lexis 3484 *14-15 (Bankr. S.D.N.Y. 2012)(without better articulated criteria for awarding bonuses, court cannot be sure they will not be discriminatory).

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[6] UMWA cannot disclose to the Court just how far ahead; by agreement with Patriot, much of the information in this opposition is protect by confidentiality agreements so as not jeopardize its competitive position. The point remains however that the Court has no information to support the allegation that the targets are "aggressive" when some of them have already been achieved and others are virtually in the participants' grasp.

The AIP program, while nominally an incentive, is thus in reality a retention bonus, or simply a pay increase to management. See, e.g., In re Hawker Beechcraft, supra, 479 B.R. at 313 (debtor failed to show that plan was not retentive because, although it included targets, the lowest levels were well within reach and a payout was inevitable). There is no evidence here of independent oversight establishing that any of the targets set by the Debtors were sufficiently challenging and incentivizing to be a part of a legitimate incentive program. The bonuses therefore are a given for showing up at work and maintaining the status quo at a previously-projected level of performance—a classic retention, rather than incentive, plan.

As noted above, about 40 participants in the AIP program are insiders within the meaning of §503(c)(1). The Debtor's disguised retention payments to these insiders pursuant to the AIP are therefore subject to the rigorous scrutiny of §503(c)(1). In re Residential Capital, 478 B.R. at 164. Because the Debtors have failed to demonstrate that any of the insiders have received a bona fide job offer, it cannot justify the retention bonus, disguised as incentive payments, to any of its insiders. "If the Court determines that an employee is an insider, then the Debtors must meet the strict requirements of section 503(c)(1)." In re Velo Holdings, Inc., 472 B.R. 201, 208 (Bankr. S.D.N.Y. 2012). The Debtors failed to meet the burden, and because the AIP is retentive and includes payments to insiders, the Debtors should be prohibited from implementing the AIP for the same reason they cannot justify the CERP.

III. The Debtor Has Failed To Demonstrate That Its Retention Bonus Proposal Is Necessary To Its Reorganization.

Even assuming that §503(c)(1) does not apply, the standard for determining whether a bonus outside the ordinary course is justified in a given case is whether--

- the plan has a reasonable relationship to the results to be obtained;
- the cost is reasonable in light of the debtor's assets, liabilities, and earnings potential;

• the scope of the plan is fair and reasonable or discriminates unfairly;

• the plan comports with industry standards;

• the debtor undertook due diligence in investigating the need for a plan, the employees that should be incentivized, market standards; and

• the debtor received independent counsel in performing due diligence in creating and authorizing the incentive compensation.

In re Global Aviation Holdings Inc., 478 B.R. 142, 150 (Bankr. E.D.N.Y. 2012). The Debtors' CERP proposal fails at least the first five criteria.

A. The Debtors Have Failed to Demonstrate They Have an Attrition Problem.

The proposed retention bonuses can only be approved if they are justified by the facts and circumstances of the case, i.e., if the Court is satisfied that the payments will advance the interests of the creditors and the estate. In re Global Aviation Holdings Inc., 478 B.R. at 150; In re Pilgrims' Pride Corp., 2009 Bankr. LEXIS 264 * 17 (Bankr. N.D. Tex. 2009). The proposed retention programs were devised by Patriot officials including the Vice President of Human Resources and other management officials. (Hatfield Decl. ¶19) The VP of HR, not surprisingly, is slated to receive the maximum 45% retention bonus, as well as a 10% "incentive" bonus. Given that the development of the retention programs constitute dealing between the Patriot's insiders and Patriot as the debtor-in-possession, the Court should closely scrutinize the program to ensure that it is fair to the estate and creditors. In re Regensteiner Printing Co., 122 B.R. 323, 326 (N.D. Ill. 1990).

At a minimum, to justify the retention program the Debtors must demonstrate to the Court that the employees will not render the required services to the estate without the bonus and that the employees cannot be replaced at less cost. Id. at 326. The CERP has no reasonable relationship with the result sought unless Patriot has an actual employee retention problem, such

that the bonus payments are truly necessary to retain employees. At a minimum, this showing requires proof that the employees desire to leave, and that they have somewhere to go. Pension Transfer Corp. v. Beneficiaries, 444 F. 3d 203, 215 (3d Cir. 2006) (bonus payments constituted fraudulent transfers in part because in an industry with few other job opportunities, the program offered amounts that exceeded amounts necessary to retain employees).

The Debtors therefore must show to the Court that they are at risk of suffering greater than normal voluntary employee attrition absent the retention bonuses. The Debtors cannot rely upon either of the metrics they employ for this showing, i.e., the departure of employees since the filing of the bankruptcy petition, and the comparison of employee wages with wages earned by employees at other companies. Hand in hand with the conclusion that the Debtors failed to demonstrate the need for the CERP is that the Debtors also failed to perform reasonable due diligence to determine that the CERP is necessary, as required by the fifth criteria of the Global Aviation test.

The metrics used by the Debtors are insufficient for several reasons. While the Debtors claim that more than 25 allegedly critically important employees have departed since June 2012, they fail to inform the Court how many of them constitute normal retirements, rather than the employee leaving for another employment opportunity. Variation in voluntary departure rates may be based on reasons other than bankruptcy. The Debtors cannot demonstrate a statistically significant link between the filing of the bankruptcy and the rate of termination of its employees, especially given Hatfield's statement that there has been 11% attrition in Patriot's corporate headcount since 2011, i.e., since long before the bankruptcy filing. (Hatfield Decl. ¶14).

In terms of employees who actually are or would have been eligible for inclusion in the CERP and therefore might be affected by the CERP's approval, Patriot lost five eligible

employees in the third quarter of 2012, two in the fourth quarter of 2012 (including one retirement), and three in the first quarter of 2013, out of a management of approximately 900. Key employee departures at Patriot have therefore slowed down since the initial shock of the bankruptcy filing. Each of the departed CERP participants in the fourth quarter of 2012 and the first quarter of 2013 have already been replaced, in all but one case by employees receiving a lower salary. Patriot has not articulated any negative consequences derived from the replacements. There is also no evidence from Patriot's submissions, anecdotal or otherwise, that any employees decided to remain at Patriot because of the prospect of receiving retention payments. Rather, the company is relying upon self-created expectations from having announced a bonus plan on the eve of bankruptcy.

Patriot's criteria for determining whom to include in the employee retention programs failed to take into account the employees' likelihood of leaving, such as a survey of employee satisfaction, whether the employees have received increased telephone calls from headhunters, whether the employees have actively solicited or received job offers, the extent that the employee's skills are transferable to other industries, and the current availability of job opportunities for the employee. Patriot designed its employee retention programs without any attempt to target them to those most at risk of leaving. Patriot's own managers met to select participants in the retention programs, with no "independent" evaluation whether Patriot's selection of participants was reasonable. Consequently, while Patriot claims that it considered the critical knowledge, experience, difficulty of replacement, and performance record of its selected participants, the CERP and AIP programs include 43 participants who were very recently hired (in 2011, 2012 or even in 2013); one has been with the company only nine weeks, and two who have been with the company only eight weeks. It beggars credulity to say they

accumulated a trove of irreplaceable experience in so short a time, or that an incentive is require to keep them in jobs so they recently chose, especially for employees who signed on after Patriot filed for bankruptcy. Patriot's program therefore appears to be a reward for management, rather than a program genuinely needed for employee retention. Cf. In re Allied Holdings, 337 B.R. 716, 723-724 (Bankr. N.D. Ga. 2005) (purpose of KERP must be to retain employees, not to reward them).

While Patriot claims its employees are paid at 25% less on average when compared to their "peers" in other industries and the coal industry, there is no explanation in Patriot's submissions of how much of its benchmarking analysis was based on comparables in the coal industry rather than other industries. Given the disparity of duties and compensation in the covered employees—from senior VPs making $340,000 to low-level technicians and administrative assistances making $30,000—the average of 25% is meaningless. To the extent Patriot's survey is based on information gathered in other industries, without knowing the industries and positions included in the survey it is impossible to determine whether the skills of Patriot's employees are in fact transferable to the other positions to which they are being compared, i.e., whether Patriot's employees are truly at risk of changing jobs.

Even to the extent that Patriot's data is based on a coal industry survey, the Court has no way of validating that the benchmark positions selected by Patriot are truly comparative in educational requirements, job duties, and responsibilities. There is no showing that Patriot has taken into account either the cost of living at the locations where the holders of comparison positions work, or the seniority of the employees holding the comparison positions. The Court has no way of knowing how much of the alleged discrepancy in compensation is due to other factors rather than actual differences in compensation practices between coal companies.

Because Patriot provided the Court with the average compensation only, the Court cannot evaluate whether, when the CERP payments are included, total compensation for some Patriot executives may be higher than for comparable positions. Patriot may be offering bonuses to employees who are receiving the same or more than their counterparts elsewhere when adjusted for experience, work experience, and local cost of living.

Patriot has failed to produce any evidence showing that other companies are actively recruiting its employees following the bankruptcy at levels beyond normal and historical experience. Patriot has failed to demonstrate how many, if any, of its identified CERP participants have transferable skills, and are likely to be hired at other firms. There is no showing for example that underground mine managers, mining environmental engineers, geologists, and mine superintendants have significant opportunities in other fields. The depressed state of the coal industry which formed one reason for Patriot's Chapter 11 filing must be having the same effect on Patriot's competitors. No reason is given why non-bankrupt mines would rush to hire management personnel who steered Patriot into bankruptcy.

Patriot's argument that its employees are receiving below market wages is logically and internally inconsistent as well. On the one hand it claims employees are likely to leave because of allegedly lower compensation offered by Patriot; on the other, it is also claiming that its employees are departing for jobs with greater security, even though those jobs offer lower pay or rank. (Hatfield Decl. ¶15) Indeed, the only evidence that any employees are likely to leave in the future because of lower wages in Patriot's submissions is the anecdotal claim that several managers *and foremen* have stated that they are considering offers by local rival companies, because they did not receive their 2012 incentives. (Hatfield Decl. ¶17) Patriot however *did not include a single foreman* in their list of CERP/AIP participants, and there is no evidence that the

managers who expressed concern with their 2012 incentives were included in the CERP/AIP. Patriot cannot justify offering its CERP program to a wide range of participants, many of whom may have received no employment solicitations and have no plans to leave Patriot, when it cannot point to a single departed employee who would have changed his or her mind if Patriot offered an employee retention program in 2012. Patriot's program is clearly one aimed to reward certain managerial employees, rather than one aimed to convince employees genuinely at risk of leaving to stay instead.

Bolstering this conclusion is the front-loading of the bonuses. If the goal of Patriot's program is genuinely to retain its employees, there is no reason to pay up to half of the retention bonus to employees who leave *prior to* Patriot's emergence from bankruptcy. There is additionally no justification for paying employees one-quarter of the retention bonus by the end of March 2013, only one month after the earlier possible approval date for the CERP, unless the payment is a reward for work done to date, i.e. largely before the approval of the CERP. AIP bonuses are likewise tied to the employee remaining through the target dates only.

The evidence that Patriot has presented is a far cry from cases where management demonstrated a genuine need to pay retention bonuses. For example, in In re US Airways, Inc., 2005 Bankr. LEXIS 1764, *13-14 (E.D. Va. 2005), the court granted the debtor's motion for severance and bonus payments (but only to non-officer management employees) based in part on the evidence that there were 340 vacancies in its managerial hierarchy, and that an additional 20 to 40 management employees had voluntarily left each month during the 8 months since the company filed Chapter 11. The exodus in US Airways was almost 20% of its management. The "exodus" at Patriot is not even 10% of its CERP participants. There is a real paucity of evidence to support Hatfield's apparent fear of an exodus of Patriot management personnel.

B. Patriot's Bonus Programs Are At Odds With Its Claims of a Liquidity Crisis.

Throughout its bankruptcy, Patriot has been subject to a liquidity covenant that required it to have $100 million in liquidity on and after January 1, 2013 for the duration of the loan. (Doc. 29-1, Sec. 7.13) A breach of the covenant constitutes a default of the loan agreement; which results in the unpaid principal and all other amounts due on the loan becoming immediately due and payable. (Id., Sec. 8.02). Patriot has used its liquidity "crisis" as a primary reason for its demand for concessions from UMWA. Paying an additional $6.9 million in bonuses to Patriot management, on top of its already substantial compensation, would place Patriot in further jeopardy of violating the liquidity covenant; thus jeopardizing its prospects of reorganization. In re Channel Master Holdings Inc., 309 B.R. 855, 862 (Bankr. D. Del. 2004) (KERP amount should be reduced to free up additional working capital to allow the debtor to survive, thus enhancing the recovery for all creditors).

C. Patriot's Bonus Proposals Do Not Comport With Industry Standards.

Patriot's argument that its CERP proposal comports with industry standards is based upon its flawed assumption that the period of retention under the CERP is 21 months. The duration of retention pursuant to the CERP should be measured from the date that the program is approved by the Court. In In re Allied Holdings, supra, because of a delay in approval of a retention bonus program, the first payment under the program became due two weeks after approval of the program. The Court held this early payment was unreasonable despite the employees' expectations of receiving a bonus payment at the end of the year. 337 B.R. at 726. Similarly, in the case at bar the duration of the CERP program should be measured from the date of the program's approval, which cannot be earlier than February 26, 2013. Given that the CERP is projected to end when the Debtors emerge from bankruptcy at the beginning of March

2014, the duration of the CERP program is 12 months, rather than 21 months as claimed by the Debtors, even assuming the Debtors push the date of emergence from bankruptcy from 2013 to the end of the first quarter of 2014. The yearly cost of the CERP program therefore is unreasonably high, given the liquidity covenant and prospects of default facing the Debtors.

Given that the Debtors have failed to provide the Court with any information on either how the comparisons were selected, or the extent of participants included in the comparisons, the Court lacks sufficient data to conclude that the comparison of retention bonus programs are apple-to-apple comparisons, as required by the Global Aviation test. The range of payments in the proposed CERP is between approximately $10,000 and more than $100,000, so the reasonableness of these payments depends on the types of positions included in the CERP, as well as the base salaries of participants in the program. Patriot has not provided the Court with any analysis of who is included in the allegedly comparable retention bonus plans or their salaries. The Court is instead presented solely with a "cost per participant" statistic that has little meaning given the wide range of positions and base salaries that may be included in a CERP program. The Court is not, for example, presented with any information showing that paying 45% of base salary to a CERP participant in a 12-month program is reasonable and comports with industry standards.

IV. The Bonus Programs Are Not Fair and Equitable.

"[It] is well settled that bankruptcy courts are courts of equity, empowered to invoke equitable principles to achieve fairness and justice in the reorganization process." In re Momentum Mfg. Corp., 25 F.3d 1132, 1135 (2d Cir. 1994). Before approving Patriot's proposed bonus plans the court must weigh the equities in a Chapter 11 case. In re Lionel Corp., 722 F. 2d at 1063, 1071 (2d Cir. 1983). See also In re America West Airlines, 171 B.R. 674, 678 (Bankr.

D. Ariz. 1994) (even under the business judgment test, a proposed retention bonus must be reasonable and fair under the circumstances).

Patriot has claimed throughout the bankruptcy that its ability to reorganize is dependent on receiving relief through the §1113 and §1114 processes. Relief under both §1113 and §1114 is only available when there is equitable sacrifice among the debtor's employees, management, and other creditors. In re Delta Airlines, 359 B.R. 468, 486 (Bankr. S.D.N.Y. 2006); In re Pierce Terminal Warehouse Inc., 133 B.R. 639, 647-648 (Bankr. N.D. Iowa 1991) (debtor cannot require union employees to take pay cuts when non-union employees are not asked to take similar pay cuts, even though union employees received a more costly package of benefits). See In re Northwest Airlines, 346 B.R. 307, 326 (Bankr. S.D.N.Y. 2006) (concessions deemed fair precisely because debtor made no attempt to institute management bonus program).

The Debtors currently propose massive reductions to the pensions, lifetime guaranteed healthcare, and wages for unionized workers and retirees represented by the UMWA in sums numbering in the billions of dollars. At the same time that Patriot is rewarding its own executives with bonuses, so that many of them may receive in 2013 the highest yearly total compensation that they have ever received from Patriot, it is seeking to pay for these bonuses by asking its unionized employees to accept substantial, life-altering changes in compensation through the §1113 and §1114 process. Patriot's CERP and AIP proposals therefore are clearly inequitable. They are funded at least in part by cutting the wages and the lifetime healthcare guarantees of miners who will (if the wage cuts are implemented) make wages of $40,000 to $55,000 per year—the low end of the bonus program scale.

The UMWA is bargaining with Patriot on the premise of equality of sacrifice and upon the express stipulation that no bonuses be paid to Patriot's salaried and managerial employees

unless justified by a bona fide job offer. Granting the bonuses will set the Debtors and the union upon a collision course.

Under §§1113 and 1114, UMWA members and retirees have no legal obligation to negotiate a reduction in their wages and benefits if Patriot's executives and managers are not similarly making sacrifices toward its emergence from bankruptcy. The court in In re Northwest Airlines Corp., 2006 Bankr. LEXIS 1159 at *39 (Bankr. S.D.N.Y. 2006) noted in granting an application to reject a collective bargaining agreement that employees were *not* being asked to bear a disproportionate burden of the sacrifice of reorganization precisely *because* management in that case did not even seek a bonus plan.

Indeed, the legislative history of §1113, as well as its plain language, commands that all parties, not just rank-and-file employees, make a contributing sacrifice to the reorganization. Congress expects courts to deny rejection applications when managers get bonuses; indeed, it expects bankruptcy courts on their own initiative to cut management's pay. E.g., 30 Cong. Rec. S8898 (daily ed. June 29, 1984)(Remarks of Sen. Packwood)("[T]he focus for cost cutting must not be directed exclusively at unionized workers. Rather the burden of sacrifices in the reorganization process will be spread among all affected parties"); 130 Cong. Rec. H7489, H7491, H7494 7496 (daily ed. June 29, 1984) (Remarks of Reps. Rodino, Moorehead, Lungren, and Morrison)("This section would ensure that...employees do not bear the entire financial burden of making the reorganization work or a disproportionate share of that burden, but only their fair and equitable share of the necessary sacrifices"); In re Blue Ribbon Transportation Co., 30 B.R. 783, 113 LRRM 3505 (Bankr. D.R.I. 1983)(cited in congressional record as an example of the correct approach by a court). The court in Blue Ribbon required that management salaries

be reduced by 25%, that perks be eliminated, and that other concessions be made by management officials.

The equity requirement was enacted to "spread the burdens of saving the company to every constituency while ensuring that all sacrifice to a similar degree." In re Century Brass Products, Inc., 795 F.2d 265, 273 (2d Cir.), cert. denied, 479 U.S. 949 (1986)(emphasis added). Top management must shoulder their share of the burden of reorganization. See, e.g., In re Indiana Grocery Co., 136 B.R. 182 (Bankr. S.D. Ind. 1990). While it is often difficult to compare sacrifices, an appropriate consideration is that of "equity under the circumstances," that is, considering each employee's contribution. Id. at 194. In other words, the intention of Congress and the actual practice of bankruptcy courts was not to conjoin rewards for executives with demands for sacrifices upon the rank-and-file. Bonus plans knock the underpinnings from demands for §1113 and §1114 concessions; they jeopardize Patriot's chance to receive the very labor cost savings that it has claimed throughout the bankruptcy it needs to comply with its liquidity covenant and reorganize successfully.

As noted above, the lack of supporting detail to the bonus plans means there is no assurance that once the CERP and AIP payments are included, the total package of compensation received by at least some of the participants will not be the highest yearly total package of compensation that they have ever received at Patriot. Patriot claims that the 2013 total compensation that it offers to its CERP/AIP participants will average approximately 20% less than the equivalent positions received in 2010-2011 (Hatfield Decl. ¶10), but the CERP And AIP programs combined would provide payments to participants up to 60% of their base salary; with the highest payments going to employees who are already receiving the highest salaries from

Patriot. It is likely that its highest-paid managers will receive total compensation still higher than they ever received from Patriot before if the CERP/AIP programs are approved by the Court.

To grant bonuses of this magnitude in the face of the §§1113 and 1114 demands is inequitable. As the letters sent by Patriot retirees to the Court have tragically recounted, retirees face the prospect of spending a large portion of their fixed incomes on health insurance and health care costs at the same time that Patriot is arguing to the Court, with little concrete supporting evidence, that lavish salaries, some in excess of $340,000 per year, will not keep its senior executives and managers in their current positions. Especially given Patriot's liquidity covenant, every dollar paid to Patriot's top executives in the CERP program would likely need to be recouped from its other employees and retirees, who are likely far less able to afford the reductions in pay and benefits. Equity principles therefore strongly counsel against approving Patriot's bonus proposal. Because the union's support and participation in bankruptcy is critical, it should not be jeopardized by the proposed incentive program. In re Geneva Steel Co., 236 B.R. 770, 773 (Bankr. D. Utah 1999). The motion should be denied.

The bonus plans are inequitable and unreasonable because they will *de facto* be funded by significant benefit and wage reductions to rank and file employees, who will bear unfairly the whole burden of cost-savings of reorganizing this estate. Approval of the motion will impede the Debtors= ability to reorganize, because it steers the estate inexorably toward an unnecessary confrontation between labor and management.[7]

[7] The Court would not have the power to intervene in such a dispute. Briggs Transportation Co. v. Teamsters, 739 F.2d 341 (8th Cir.) cert. denied, 469 U.S. 917 (1984)(strike to force employer to adhere to rejected agreement could not be enjoined by bankruptcy court).

V. The Debtors' Bonuses Cannot Pass Muster Even Under the Business Judgment Test.

Under the more generous business judgment test, there still must be an independent conclusion by the Court that the bonus is "reasonable and fair under the circumstances." In re America West Airlines, 171 B.R. 674, 678 (Bankr. D. Ariz. 1994). There are two reasons why the Debtors' proposed programs are not reasonable even under the business judgment test: First, the program seeks to reward employees before any results have been achieved. Second, the program rewards employees even though they cannot make any concrete contributions toward attaining the metrics.

Incentive programs should not pay performance incentives before any results have been attained. In In re US Airways, Inc., the court refused to approve new employment agreements for the top 23 corporate officers until plan confirmation, 2005 Bankr. LEXIS 1764 at *13-14, and insisted upon other safeguards, such as a mitigation provision reducing severance pay if terminated managers found other employment and a cap on the maximum administrative expense exposure to the estate. Id. at *18-23. See In re Geneva Steel Co., 236 B.R. 770 (Bankr. D. Utah 1999)(ordering similar mitigation provision in severance pay). In America West, supra, the court permitted bonuses only retrospectively, that is, for proven performance after a successful conclusion to the bankruptcy.

In America West, executives actually took pay cuts of 10% for *three years* during the bankruptcy and prior to being awarded bonuses, which were received only after a successful reorganization paying a substantial dividend to unsecured creditors. The bonuses were largely in the form of equity, i.e., the managers reaped the reward of managing the company well. See In re Geneva Steel Co., 236 B.R. 770 (Bankr. D. Utah 1999) (ordering that proposed bonuses for executives not be paid in cash, but rather in stock). Similarly, it is not fair and reasonable for

Patriot to reward its employees for continuing their current level of performance; so that the employees would receive the payments regardless of whether the reorganization is ultimately successful, and regardless of contributions, if any, they made toward a successful reorganization.

Second, an incentive plan must be calculated to achieve the desired performance. Dana Corp., supra, 358 B.R. 567 at 576. The Debtors must show the payees contribute services necessary to achieve the targets of the incentive program. Hawker Beechcraft, supra, 479 B.R. at 313. One non sequitur in Patriot's AIP is the payment of bonuses for attaining safety and environmental goals to office employees, its Chief Information Officer, as well as employees in departments such as tax, purchase, and computer sciences who would make no apparent contributions toward improving Patriot's health and safety record. More generally, Patriot's AIP includes administrative assistants and even an associate I in the mailroom, employees who are not in a position to make a significant impact upon its attainment of its financial, safety, or environmental metrics. Patriot's AIP is thus further revealed as a mere reward, rather than a genuine effort to motivate the employees whose improved work performance is needed to achieve performance metrics and enhance Patriot's prospects of a successful reorganization.

Conclusion

For the foregoing reasons, and for reasons to be developed at the evidentiary hearing in this matter, the Court should deny the Motion.

Dated this 8th day of March, 2013.

s/ Frederick Perillo
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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a copy of the foregoing document was filed on March 8, 2013 using the Court's CM/ECF system and that service will be accomplished upon all counsel of record by operation of that system.

s/ Frederick Perillo

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF MISSOURI
EASTERN DIVISION

In re: **PATRIOT COAL CORPORATION, *et al.*,** **Debtors.**	**Chapter 11** **Case No. 12-51502-659** **(Jointly Administered)**

DECLARATION OF FREDERICK PERILLO

I, Frederick Perillo, being duly sworn and under oath, states as follows:

1. My name is Frederick Perillo. I am one of the attorneys representing the United Mine Workers of America in relation to the above-captioned matter. I have firsthand knowledge of, and am competent to testify as to all information contained in this declaration.

2. I have attached a true and complete copy of the Bylaws of Debtor Patriot Coal Corporation ("Patriot") as exhibit A to my declaration. Section 3.2 of the Bylaws defines "Principal Officers."

Pursuant to 28 U.S.C. s. 1746, I declare under penalty of perjury that the foregoing is true and correct to the best of my knowledge and belief.

Executed this 8th day of March, 2013.

s/ Frederick Perillo

Exhibit A

FORM OF
AMENDED AND RESTATED
BY-LAWS
OF
PATRIOT COAL CORPORATION

ARTICLE I

MEETING OF STOCKHOLDERS

Section 1.1. Place of Meeting. Meetings of the stockholders of the Corporation shall be held at such place either within or without the State of Delaware as the Board of Directors may determine.

Section 1.2. Annual Meetings. (A) Annual meetings of stockholders shall be held, at a date, time and place fixed by the Board of Directors and stated in the notice of meeting, to elect a Board of Directors and to transact such other business as may properly come before the meeting.

(B) Nominations of persons for election to the Board of Directors of the Corporation and the proposal of business to be considered by the stockholders may be made at an annual meeting of stockholders (1) pursuant to the Corporation's notice of meeting delivered pursuant to Article 1, Section 4 of these By-Laws, (2) by or at the direction of the Chairman of the Board or (3) by any stockholder of the Corporation who is entitled to vote at the meeting, who complied with the notice procedures set forth in subparagraphs (B) and (C) of this Section 2 and who was a stockholder of record at the time such notice is delivered to the Secretary of the Corporation.

(C) For nominations or other business to be properly brought before an annual meeting by a stockholder pursuant to clause (3) of paragraph (B) of these By-Laws, the stockholder must have given timely notice thereof in writing to the Secretary of the Corporation, and, in the case of business other than nominations, such other business must be a proper matter for stockholder action. To be timely, a stockholder's notice shall be delivered to the Secretary at the principal executive offices of the Corporation not less than ninety (90) days nor more than one hundred and twenty (120) days prior to the first anniversary of the preceding year's annual meeting; provided, however, that in the event that the date of the annual meeting is advanced by more than twenty (20) days, or delayed by more than seventy (70) days, from such anniversary date, notice by the stockholder to be timely must be so delivered not earlier than one hundred and twenty (120) days prior to such annual meeting and not later than the close of business on the later of the ninetieth (90th) day prior to such annual meeting or the tenth (10th) day following the day on which public announcement of the date of such meeting is first made. Such stockholder's notice shall set forth (1) as to each person whom the stockholder proposes to nominate for election or re-election as a director all information relating to such person that is required to be disclosed in solicitations of proxies for election of directors, or is otherwise required, in each case pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), including such person's written consent to being named in the proxy statement as a nominee and to serving as a director if elected; (2) as to any other business that the stockholder proposes to bring before the meeting, a brief description of the business desired to be brought before the meeting, the reasons for conducting such business at the meeting and any

material interest in such business of such stockholder and the beneficial owner, if any, on whose behalf the proposal is made; and (3) as to the stockholder giving the notice and the beneficial owner, if any, on whose behalf the nomination or proposal is made (a) the name and address of such stockholder, as they appear on the Corporation's books, and of such beneficial owner and (b) the class and number of shares of the Corporation which are owned beneficially and of record by such stockholder and such beneficial owner.

(D) Notwithstanding anything in the second sentence of paragraph (C) of these By-Laws to the contrary, in the event that the number of directors to be elected to the Board of Directors of the Corporation is increased and there is no public announcement naming all of the nominees for director or specifying the size of the increased Board of Directors made by the Corporation at least eighty days prior to the first anniversary of the preceding year's annual meeting, a stockholder's notice required by this By-Law shall also be considered timely, but only with respect to nominees for any new positions created by such increase, if it shall be delivered to the Secretary at the principal executive offices of the Corporation not later than the close of business on the tenth (10th) day following the day on which such public announcement is first made by the Corporation.

Section 1.3. Special Meetings. (A) Except as otherwise required by law, special meetings of the stockholders may be called pursuant to the provisions of the Amended and Restated Certificate of Incorporation of the Corporation, filed with the Delaware Secretary of State on October 22, 2007 (as amended from time to time, the "Charter").

(B) Only such business shall be conducted at a special meeting of stockholders as shall have been brought before the meeting pursuant to the Corporation's notice of meeting pursuant to Article I, Section 4 of these By-Laws. Nominations of persons for election to the Board of Directors may be made at a special meeting of stockholders at which directors are to be elected pursuant to the Corporation's notice of meeting (1) by or at the direction of the Board of Directors or (2) by any stockholder of the Corporation who is entitled to vote at the meeting, who complies with the notice procedures set forth in these By-Laws and who is a stockholder of record at the time such notice is delivered to the Secretary of the Corporation. Nominations by stockholders of persons for election to the Board of Directors may be made at such a special meeting of stockholders if the stockholder's notice as required by paragraph (C) of Section 2 shall be delivered to the Secretary at the principal executive offices of the Corporation not earlier than the ninetieth (90th) day prior to such special meeting and not later than the close of business on the later of the seventieth (70th) day prior to such special meeting or the tenth (10th) day following the day on which public announcement is first made of the date of the special meeting and of the nominees proposed by the Board of Directors to be elected at such meeting.

Section 1.4. Notice. Except as otherwise provided by law, at least ten (10) and not more than sixty (60) days before each meeting of stockholders, written notice of the time, date and place of the meeting, and, in the case of a special meeting, the purpose or purposes for which the meeting is called, shall be given to each stockholder.

Section 1.5. Quorum. At any meeting of stockholders, the holders of record, present in person or by proxy, of a majority of the Corporation's issued and outstanding capital stock shall constitute a quorum for the transaction of business, except as otherwise provided by law. In the

absence of a quorum, any officer entitled to preside at or to act as secretary of the meeting shall have power to adjourn the meeting from time to time until a quorum is present.

Section 1.6. Voting. Except as otherwise provided by law or by the Charter, (a) all matters submitted to a meeting of stockholders, other than the election of directors, shall be decided by vote of the holders of record of a majority of the shares of the Corporation's issued and outstanding capital stock present in person or represented by proxy at the meeting and entitled to vote on the matter, and (b) directors shall be elected by a plurality of the votes of the shares of the Corporation's issued and outstanding capital stock present in person or represented by proxy at the meeting and entitled to vote on the election of directors.

Section 1.7. General. (A) Only persons who are nominated in accordance with the procedures set forth in these By-Laws shall be eligible to serve as directors and only such business shall be conducted at a meeting of stockholders as shall have been brought before the meeting in accordance with the procedures set forth in these By-Laws. Except as otherwise provided by law, the Charter or these By-Laws, the Chairman of the meeting shall have the power and duty to determine whether a nomination or any business proposed to be brought before the meeting was made in accordance with the procedures set forth in this By-Law and, if any proposed nomination or business is not in compliance with these By-Laws, to declare that such defective nomination shall be disregarded or that such proposed business shall not be transacted.

(B) For purposes of these By-Laws, "public announcement" shall mean disclosure in a press release reported by the Dow Jones News Service, Associated Press or comparable national news service or disclosure in a document publicly filed by the Corporation with the Securities and Exchange Commission pursuant to Section 13, 14 or 15(d) of the Exchange Act.

(C) For purposes of this By-Law, no adjournment nor notice of adjournment of any meeting shall be deemed to constitute a new notice of such meeting for purposes of this Article, and in order for any notification required to be delivered by a stockholder pursuant to this Article to be timely, such notification must be delivered within the periods set forth above with respect to the originally scheduled meeting. Subject to applicable law, the Board of Directors may elect to postpone any previously scheduled meeting of stockholders.

(D) Notwithstanding the foregoing provisions of this Article, a stockholder shall also comply with all applicable requirements of the Exchange Act and the rules and regulations thereunder with respect to the matters set forth in these By-Laws. Nothing in these By-Laws shall be deemed to affect any rights of stockholders to request inclusion of proposals in the Corporation's proxy statement pursuant to Rule 14a-8 under the Exchange Act.

ARTICLE II

DIRECTORS

Section 2.1. Number, Election and Removal of Directors. The number of Directors that shall constitute the Board of Directors shall be not less than three nor more than 15. Within the limits specified in the Charter, the number of Directors shall be determined by the Board of

Directors or by the stockholders. The Directors shall be elected by the stockholders at their annual meeting in the manner set forth in the Charter. Vacancies and newly created directorships resulting from any increase in the number of Directors may be filled pursuant to the terms of the Charter. Directors may be removed only for cause, and only by the affirmative vote of at least 75 percent in voting power of all shares of the Corporation entitled to vote generally in the election of directors, voting as a single class.

Section 2.2. Meetings. Regular meetings of the Board of Directors shall be held at such times and places as may from time to time be fixed by the Board of Directors or as may be specified in a notice of meeting. Special meetings of the Board of Directors may be held at any time upon the call of the Chairman or President and shall be called by the President or Secretary if directed by a majority of the Directors. Telegraphic or written notice of each special meeting of the Board of Directors shall be sent to each Director not less than two days before such meeting. A meeting of the Board of Directors may be held without notice immediately after the annual meeting of the stockholders. Notice need not be given of regular meetings of the Board of Directors.

Section 2.3. Quorum. One-third of the entire Board of Directors shall constitute a quorum for the transaction of business. If a quorum is not present at any meeting of the Board of Directors, the Directors present may adjourn the meeting from time to time, without notice other than announcement at the meeting, until such a quorum is present. Except as otherwise provided by law, the Charter, these By-Laws or any contract or agreement to which the Corporation is a party, the act of a majority of the Directors present at any meeting at which there is a quorum shall be the act of the Board of Directors.

Section 2.4. Committees of Directors. The Board of Directors may, by resolution adopted by a majority of the entire Board, designate one or more committees, including without limitation an Executive Committee, to have and exercise such power and authority as the Board of Directors shall specify. In the absence or disqualification of a member of a committee, the member or members thereof present at any meeting and not disqualified from voting, whether or not he or they constitute a quorum, may unanimously appoint another Director to act at the meeting in place of any such absent or disqualified member.

Section 2.5. Actions without a Meetings. Any action required or permitted to be taken at any meeting of the Board of Directors or a committee thereof may be taken without a meeting if all the members of the board or of such committee, as the case may be, consent thereto in writing or by electronic transmission, and such writing or writings or electronic transmission or transmissions are filed with the records of the meetings of the board or of such committee. Such consent shall be treated for all purposes as the act of the board or of such committee, as the case may be.

Section 2.6. Participation in Meetings by Conference Telephone. Members of the Board of Directors, or any committee designated by the Board of Directors, may participate in a meeting of such board or committee by means of conference telephone or other communications equipment by means of which all persons participating in the meeting can hear each other or by any other means permitted by law. Such participation shall constitute presence in person at such meeting.

Section 2.7. Compensation. In the discretion of the Board of Directors, each director may be paid such fees for his or her services as director (including as a member of one or more committees of the Board of Directors) and be reimbursed for his or her reasonable expenses incurred in the performance of his or her duties as director as the board of directors from time to time may determine. Nothing contained in this section shall be construed to preclude any director from serving the Corporation in any other capacity and receiving reasonable compensation therefor.

Section 2.8. Reliance Upon Books and Records. A member of the Board of Directors, or a member of any committee designated by the Board of Directors shall, in the performance of his or her duties, be fully protected in relying in good faith upon the records of the Corporation and upon such information, opinions, reports or statements presented to the Corporation by any of the Corporation's officers, employees, agents, committees, or by any other person as to matters the member reasonably believes are within such other person's or persons' professional or expert competence, and who has been selected with reasonable care by or on behalf of the Corporation.

ARTICLE III

CHAIRMAN OF THE BOARD AND OFFICERS

Section 3.1. Chairman of the Board. The Board of Directors shall elect from time to time one of its own members as the Chairman of the Board of Directors (the "Chairman"). The Chairman may also be the Chief Executive Officer or other officer of the Corporation. The Chairman shall preside at the meetings of the Board and may call meetings of the Board and any committee thereof, whenever he deems necessary, and he shall call to order and preside at all meetings of the stockholders of the Corporation. In addition, he shall have such other powers and duties as the Board shall designate from time to time.

Section 3.2. Principal Officers. The principal officers of the Corporation shall consist of a Chief Executive Officer, a President, one or more Vice Presidents, a Secretary, a Treasurer and such other additional officers with such titles (including, without limitation, a Chief Operating Officer and a Chief Financial Officer) as the Board of Directors shall from time to time determine, all of whom shall be elected by and shall serve at the pleasure of the Board of Directors. Subject to applicable law, an officer may hold more than one office, if so elected by the Board of Directors. Such officers shall have the usual powers and shall perform all the usual duties incident to their respective offices. Such officers shall also have such powers and duties as from time to time may be conferred by the Board of Directors. All officers shall be subject to the supervision and direction of the Board of Directors. The Board of Directors may from time to time elect, or the Chief Executive Officer or President may appoint, such other officers (including one or more Assistant Vice Presidents, Assistant Secretaries, Assistant Treasurers, and Assistant Controllers) and such agents, as may be necessary or desirable for the conduct of the business of the Corporation. Such other officers and agents shall have such duties and shall hold their offices for such terms as may be prescribed by the Board of Directors or by the Chief Executive Officer or President, as the case may be. The officers of the Corporation need not be stockholders of the Corporation nor need such officers be directors of the Corporation.

Section 3.3. Election and Term of Office. The officers of the Corporation shall be elected annually by the Board of Directors at the regular meeting of the Board of Directors held after the annual meeting of stockholders. If the election of officers shall not be held at such meeting, such election shall be held as soon thereafter as convenient. Each officer shall hold office until his successor shall have been duly elected and shall have qualified or until his death or until he shall resign, but any officer may be removed from office at any time as provided in Section 3.4.

Section 3.4. Removal. Any officer elected, or agent appointed, by the Board of Directors may be removed by the affirmative vote of a majority of the entire Board of Directors whenever, in their judgment, the best interests of the Corporation would be served thereby. Any officer or agent appointed by the Chief Executive Officer or the President may be removed by the Chief Executive Officer or the President, as the case may be, whenever, in such officer's judgment, the best interests of the Corporation would be served thereby. Such removal shall be without prejudice to the contractual rights, if any, of the person so removed; provided that no elected officer shall have any contractual rights against the Corporation for compensation beyond the date of the election of his successor, his death, his resignation or his removal, whichever event shall first occur, except as otherwise provided in an employment contract or under an employee deferred compensation plan.

Section 3.5. Vacancies. A newly created elected office and a vacancy in any elected office because of death, resignation, or removal may be filled by the Board of Directors for the unexpired portion of the term at any meeting of the Board of Directors. Any vacancy in an office appointed by the Chief Executive Officer or the President because of death, resignation, or removal may be filled by the Chief Executive Officer or the President.

ARTICLE IV

INDEMNIFICATION

To the fullest extent permitted by the Delaware General Corporation Law, the Corporation shall indemnify any current or former Director or officer of the Corporation and may, at the discretion of the Board of Directors, indemnify any current or former employee or agent of the Corporation against all expenses, judgments, fines and amounts paid in settlement actually and reasonably incurred by him in connection with any threatened, pending or completed action, suit or proceeding brought by or in the right of the Corporation or otherwise, to which he was or is a party or is threatened to be made a party by reason of his current or former position with the Corporation or by reason of the fact that he is or was serving, at the request of the Corporation, as a director, officer, partner, trustee, employee or agent of another corporation, partnership, joint venture, trust or other enterprise.

ARTICLE V

GENERAL PROVISIONS

Section 5.1. Notices. Whenever any statute, the Charter or these By-Laws require notice to be given to any Director or stockholder, such notice may be given in writing by mail,

addressed to such Director or stockholder at his address as it appears on the records of the Corporation, with postage thereon prepaid. Such notice shall be deemed to have been given when it is deposited in the United States mail. Notice to Directors may also be given by telefax or e-mail.

Section 5.2. Fiscal Year. The fiscal year of the Corporation shall be fixed by the Board of Directors.

Section 5.3. Amendment. Except as otherwise provided in the Charter, these By-Laws may be adopted, amended or repealed by resolution of the Board of Directors or by vote of a majority of the voting power of the stock outstanding and entitled to vote.