



Memorandum

TO: City Council

FROM: Mayor Chuck Reed
Vice Mayor Judy Chirco
Councilmember Nancy Pyle
Councilmember Rose Herrera

SUBJECT: Airport Living Wage Ordinance

DATE: December 2, 2010

APPROVED: *Chuck Reed* **DATE:** *12/2/10*

Judy Chirco Nancy Pyle Rose Herrera

RECOMMENDATIONS: *PH*

Approve an ordinance including staff recommendations A, B, C and H with the following modifications to be effective January 1, 2011, and bring back to the City Council for a second reading on December 14, 2010:

- A. Complaint-based enforcement of compensation provisions to be bolstered with annual reporting and a system of audits so that every business is audited at least every two years.
- B. Violations of minimum compensation requirements to be dealt with as follows:
 - i. 30-day opportunity to cure for first violation of minimum compensation requirements in any 3-year period; and
 - ii. In any 3-year period, subsequent violations may be assessed a fine payable to the City in an amount equal to any underpayment.
- C. Modify section 25.11.520 to read:

25.11.520 ~~Temporary exemption for passenger airlines.~~

- A. The minimum compensation requirements of this part shall not apply to any covered employee of an ~~passenger airline~~ airport business, only if the sum of the hourly wage, the employer's direct hourly contribution for the covered employee's health and medical care insurance, if any, and the employer's direct hourly contribution for the covered employee's retirement benefits, if any, is no less than the greater of:
 - 1. Twelve dollars and eighty-three cents (\$12.83) per hour; or
 - 2. The then-current minimum compensation rate with minimum health benefits provided, as adjusted on an annual basis under this part.
- B. The employer's direct hourly contribution shall be the rate of contribution irrevocably made by the employer to a trustee or to a third person pursuant to a fund, plan or program for the benefit of employees.

~~C. Any exemption under this section shall expire on December 31, 2010.~~

C. If an employee is offered health insurance or retirement benefits in good faith, but voluntarily declines to receive them, the benefits shall be deemed to have been provided to the employee. Staff is directed to monitor and report back to City Council as necessary but no later than January 2012 if businesses are abusing this provision.

BACKGROUND

On March 8, 2010, staff presented information at a City Council study session regarding the Airport's need, ability, and constraints to successfully compete for air service. This included a review of the state of the airline industry; Bay Area air service trends and the competitive marketplace; cost challenges facing the Airport; policy issues that constrain the Airport's competitive position; and options for addressing those challenges.

At the study session, Council directed staff to develop a work plan for developing a strategic plan that will keep the Airport competitive.

On May 12, 2010, the City Council approved eight Strategic Principles for Airport Competitiveness to guide staff and Council decisions on individual components of the Airport Competitive Strategic Plan. Two of those principles are particularly relevant to this item.

3. The Airport will **continue to be cost-competitive for airlines and seek opportunities to reduce costs** allocated to airlines through greater efficiencies, benchmark with the airport industry best practices, and identify the most cost-effective alternative service delivery methods in all areas of service.

5. The Airport will **continue to aggressively seek to increase air service** in partnership with the community to gain more routes, frequencies, and carriers that meet the needs of Silicon Valley businesses and residents. To increase passenger traffic, the Airport needs more flights. This will require active marketing to airlines and the development of more effective community and business engagement to help achieve this goal.

As part of an effort to maintain existing flights and to gain new air service, the Mayor has been meeting with airline CEOs to ask them what they need from our airport to be successful and what would be necessary for them to consider adding new services.

The CEOs from Southwest, Alaska/Horizon, and Virgin America have confirmed that the cost of operations is a critical component of their decision making and is more than just Cost per Enplaned Passenger. The cost of operations includes many other factors, such as the cost of compliance with our living wage ordinance.

The living wage ordinance is of particular concern to Southwest, which provides over 50% of our air service, and is vital to the success of the airport and the City's ability to make debt service payments. Southwest has operated under a temporary exemption for passenger airlines that

CITY COUNCIL

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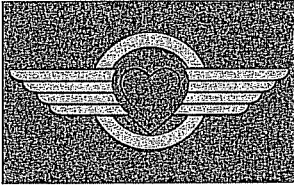
Subject: AIRPORT LIVING WAGE ORDINANCE

Page 3

expires on December 31, 2010 and has requested that we modify the living wage ordinance. The CEO of Southwest sent a letter dated November 9, 2010 describing their interests and requesting a modification of the ordinance. A copy of that letter is attached.

This memorandum recommends important revisions to the Airport Living Wage Ordinance that will help support the Council's immediate goal to place the airport in a more competitive position. One of the proposed revisions will resolve the issues that Southwest currently views as a disincentive to expanding service in San Jose. That's an important first step. Other revisions that we have recommended will help to relieve regulatory and administrative burdens and costs to the City and Airport employers, while at the same time encouraging compliance with the Airport Living Wage Ordinance. We don't believe that modifications to the minimum amounts of wages and benefits are necessary at this time since San Jose is in the middle of the range of comparison airports. Staff recommendations not addressed in this memorandum which could lead our airport to being more competitive with other regional airports will need to be further evaluated and addressed at some point in the future.

Attachment



SOUTHWEST AIRLINES CO.

Gary C. Kelly
Chairman of the Board, President &
Chief Executive Officer

2702 Love Field Drive
P.O. Box 36611
Dallas, TX 75235-1611
(214) 792-4363

November 9, 2010

Honorable Mayor Chuck Reed
Mayor of the City of San José
200 East Santa Clara Street, 18th Floor
San José, CA 95113

Re: San José Municipal Code Chapter 25.11
Airport Living Wage and Labor Standards

Dear Mayor Reed:

I want to thank you and the entire San José community for creating an environment where Southwest Airlines has been able to grow and prosper. Southwest initiated service at the Norman Y. Mineta San José International Airport (the Airport) in 1993 with nonstops to Burbank and Las Vegas. We now offer nonstop service to 13 cities including our most recent addition of nonstop service between San José and Austin, Texas, which began this past Sunday, November 7. In addition, on November 12, Southwest will start accepting reservations for international service between San José and various destinations in Mexico through our international connection with Volaris. We are very pleased with our current service and future prospects at the Airport and are sincerely delighted to be a part of the San José community.

I am also writing to respectfully request your and the City Council's consideration of a limited amendment tailored to address a particularly challenging aspect of the Airport Living Wage and Labor Standards found in San José Municipal Code Chapter 25.11 (the Living Wage Policy). In doing so, I wish to emphasize that Southwest Airlines fully supports the objectives and purpose of the Living Wage Policy. The limited amendment is intended to accomplish that purpose while at the same time recognizing the protections that the collective bargaining process offers to employees whose labor agreements are governed by the Railway Labor Act.

Summary of The Living Wage Policy

The Living Wage Policy currently requires employers at the Airport to pay wages of no less than (i) \$14.19 per hour, or (ii) \$12.94 per hour, if the employer pays at least 50% of the cost of its employees' health insurance plan.

There are two exemptions to this requirement. The first (the Collective Bargaining Exemption) exempts employees covered by a collective bargaining agreement that "expressly provides that the terms of the collective bargaining agreement shall supersede . . . the Living Wage Policy." The second (the Temporary Exemption) establishes the lower minimum compensation rate (currently, \$12.94 per hour) as the rate applicable to passenger airlines and permits passenger airlines to include the cost of employer-paid health and medical care insurance and retirement benefits in the computation of wages. The Temporary Exemption is scheduled to expire on December 31, 2010.

Benefits Valued at \$3.79/Hour

Southwest Airlines provides its Employees an outstanding benefits package consisting of very generous retirement, health, and welfare benefits that provide significant value to Employees. In fact, for an

Employee earning \$12.94 per hour, Southwest's benefits have an annual potential value of \$7,882 (or \$3.79 per hour) *over and above* the minimum health benefits that must be provided to qualify for the \$12.94 minimum compensation rate under the Living Wage Policy. These benefits include the following:

- Company 401(k) match of \$1 for every \$1 contributed by the Employee, up to 8.3% of the Employee's compensation (valued at up to \$1.07/hour),¹
- Company ProfitSharing contribution which, over the past 5 years, has averaged 5.24% of each Employee's compensation (valued at up to \$0.68/hour),
- Company payment of 89.5% of the cost of the medical and dental healthcare plans, which is 39.5% more than is required to qualify for the lower minimum compensation rate under the Living Wage Policy (this excess amount is valued at \$2.00/hour), and
- Company payment of the cost of basic life insurance, basic AD&D insurance, long-term disability, employee assistance program, and work/life benefits (valued at \$0.04/hour).

Exhibit A provides additional details on the value of Southwest's generous benefits package.

Approximately 87% of Southwest's workforce is covered by a collective bargaining agreement—one of the highest such percentages in the domestic airline industry.² These collective bargaining agreements address all aspects of hours, rates of pay, benefits, rules and working conditions and, in Southwest's case, have resulted in a total compensation package that is rich in benefits.

Benefits Not Recognized after December 31, 2010

The current Living Wage Policy gives consideration to Southwest's valuable benefits through the Temporary Exemption. However, the Temporary Exemption is scheduled to expire on December 31, 2010 at which time Southwest's benefit package will no longer be recognized under the Living Wage Policy even though it represents substantial value and even though it is the direct result of collective bargaining.

As an air carrier, Southwest is unable to negotiate a local labor agreement to transfer value from benefits to wages for its San José Employees. Southwest's labor agreements are governed by the Railway Labor Act (RLA) rather than the more common National Labor Relations Act (NLRA). The RLA applies to air carriers and railroads and, unlike the NLRA, mandates a single national collective bargaining agreement for all locations (for example, all of Southwest's Customer Service Agents are governed by a single collective bargaining agreement whether they work in San José, Kansas City, Orlando, Boston, or any of Southwest's 65+ other locations). As a result, Southwest is required to provide its San José Employees with the package of pay and benefits that are collectively bargained on a nationwide basis.

The Collective Bargaining Exemption is not an alternative for an air carrier like Southwest due to the requirement that the collective bargaining agreement "expressly provide[] that the terms of the collective bargaining agreement shall supersede . . . the Living Wage Policy." RLA agreements are national in coverage and focus while NLRA agreements are distinctively local—both in coverage and nature. As a result, NLRA agreements are well suited to address unique local requirements like the Living Wage Policy. RLA agreements, on the other hand, must address hours, rates of pay, benefits, rules and working conditions of employees in multiple locations nationwide and must be voted on and ratified by Employees across the

¹The maximum match varies by labor agreement between 7.3%-9.3% of compensation but is currently at 8.3% of compensation for all Employees at the Airport. On January 1, 2011, the maximum match for Customer Service Agents and Noncontract Employees (including those at the Airport) will increase to 9.3% of compensation.

² Southwest Airlines Employees are represented by the following Unions: Southwest Airlines Pilots' Association (Pilots), Transport Workers Union (Flight Attendants; Ramp, Operations, Provisioning, and Freight Agents; Dispatchers; and Professional Flight Instructors), International Association of Machinists (Customer Service Agents and Customer Representatives), International Brotherhood of Teamsters (Stock Clerks and Flight Simulator Technicians), and the Aircraft Mechanics Fraternal Association (Mechanics and Aircraft Appearance Technicians).

country. These differences make waivers of local living wage requirements under an RLA agreement unattainable as a practical matter. In essence, RLA employers do not have the same ability as NLRA employers to access the Collective Bargaining Exemption.

Limited Amendment

We respectfully request your and the City Council's consideration of a limited amendment to the Collective Bargaining Exemption so as to no longer require an express waiver of the Living Wage Policy for collective bargaining agreements governed by the Railway Labor Act. Such an amendment would:

- be supported by the differences between RLA and NLRA labor agreements,
- only apply to air carriers and railroads whose employees are afforded the protections of nationwide collective bargaining under the Railway Labor Act (as opposed to the Temporary Exemption that applies to all passenger airlines regardless of collective bargaining), and
- relieve the regulatory and administrative burden and cost to the City and employers alike that has been experienced under the Temporary Exemption and that would continue under any other approach that requires employers to report, and the City to verify, the value of benefits offered employees.

I thank you for the opportunity to share Southwest Airlines' views on this important issue. We stand ready to answer any questions and provide any assistance that you or the City Council may find helpful in considering this matter. If so, you can contact Gregg Thorsen, Sr. Director Employee Benefits, directly at gregg.thorsen@wnco.com or 214-792-3947.

Very truly yours,


Gary C. Kelly

Exhibit A
Southwest Airlines Co.
Benefits Fact Sheet

Southwest Airlines Co. Benefit	Benefit Description	Annual Potential Value	Recognized under the Living Wage Policy after Dec 31, 2010?
401(k) Company Match	\$1 for \$1 up to 8.3% of annual compensation	\$2,234	No
ProfitSharing Contribution	Variable depending on profitability. 5-Year Average = 5.24% of annual compensation	\$1,410	No
Health Plans (Medical and Dental)	Multiple plans to choose from	\$4,153	No
Welfare Plans	Life, AD&D, LTD and Work/Life Benefits	\$85	No
Total Annual Potential Value		\$7,882	No
Hourly Equivalent		\$3.79/hr	No

Notes:

General

- Annual potential values are based on an Employee making \$12.94/hour and paid for 2,080 hours per year.
- 87% of Southwest Airline's workforce is covered by a collective bargaining agreement. The benefits shown above are addressed in and subject to those agreements.

Retirement

- 401(k) company match will increase to 9.3% beginning January 1, 2011 for Customer Service Agents and Noncontract Employees. For these Employees, the annual potential value of the 401(k) company match will be \$2,503.
- According to a 2008 survey by the ProfitSharing Council of America, the average company 401(k) match is approximately 3%.
- Annual potential value of the ProfitSharing contribution is calculated by multiplying the 5-year average contribution of 5.24% by \$26,915.20 (2,080 hours at \$12.94/hour).

Health & Welfare

- Southwest Airlines pays 89.5% of the cost of its Health Plans, which is 39.5% more than what is required under the Living Wage Policy to qualify for the reduced minimum compensation rate. The annual potential value of the Health Plans shown above is the annual cost of this additional 39.5% value provided to Employees.
- Southwest offers four health plans, two of which are free to Employees. Overall, Employees pay 10.5% of the cost of Southwest's Health Plans.
- Annual potential value of the Welfare Plans is the annual cost per Employee of the following benefits provided free to Employees by Southwest Airlines: Basic Life, Basic AD&D, LTD, EAP and Work/Life Benefits.