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Proposed Counsel for Debtor  
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**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF HAWAII**

In re

HAWAIIAN AIRLINES, INC.  
a Hawaii corporation

Debtor.

**Case No. 03 - \_\_\_\_\_**  
(Chapter 11)

**CONSOLIDATED MEMORANDUM OF LAW  
IN SUPPORT OF DEBTOR'S MOTIONS FOR  
ORDERS AUTHORIZING PAYMENT OF  
CERTAIN PREPETITION CLAIMS**

Date: March 21, 2003  
Time:  
Judge: Hon. Robert J. Faris

Hawaiian Airlines, Inc., as debtor and debtor in possession (the “Debtor”), by and through its undersigned proposed co-counsel, respectfully submits this memorandum of law in support of the following motions (collectively, the “Motions”) filed contemporaneously herewith: (i) Motion for Order (A) Authorizing Payment of Prepetition Wages, Salaries, Reimbursable Employee Expenses, Payment of Prepetition Deductions and Payment Pursuant to Certain Employee Benefits Programs, (B) Directing Banks to Honor Prepetition Checks and (C) Confirming Right of Debtor to Continue Its Employee Programs (the “Employees Motion”); (ii) Motion for Order Authorizing Debtor to Pay or Honor Prepetition Obligations to Certain Foreign Vendors, Service Providers and Governments in the Ordinary Course of Business (the “Foreign Vendors Motion”); (iii) Motion for Order Authorizing Debtor to (A) Continue Debtor’s Workers’ Compensation Programs, Insurance Policies and Agreements Relating Thereto, and (B) Pay all Obligations in Respect Thereof (the “Insurance Motion”); (iv) Motion for Order (A) Authorizing the Debtor to Assume Executory Contracts Relating to Interline Agreements, Clearinghouse Agreements, the ARC Agreements, the BSP Agreements, the UATP Agreement, the Code Share Agreements and the Frequent

Flyer Agreements and (B) Authorizing the Debtor to Honor Prepetition Obligations Related to Code Share Agreements, Global Distribution Systems Agreements, Multi-host Agreements, Travel Agency Agreements, and the ATPCO Agreement in the Ordinary Course of Business (the “Executory Contracts Motion”); (v) Motion for Order Authorizing Debtor to Pay Certain Outside Maintenance Providers, Shippers and Contractors in Satisfaction of Perfected or Potential Mechanics’, Materialmen’s or Similar Liens or Interests, Whether Possessory or Otherwise in the Ordinary Course of Business (the “Maintenance Providers Motion”); (vi) Motion for Order Authorizing (A) Application of Prepetition Payments on Fuel Supply Contracts, Storage Agreements and Fuel Consortia Agreements, (B) Honoring of Other Fuel Supply, Storage, Into-plane Fuel Contracts and Other Fuel Service Arrangements, and (C) Continued Participation in Fuel Consortia (the “Fuel Providers Motion”); (vii) Motion for Order Authorizing Debtor to Honor Prepetition Obligations to Customers and Otherwise Continue Customer Programs and Practices in Ordinary Course of Business (the “Customers Motion”); and (viii) Motion for Order Authorizing Debtor to Pay Prepetition Sales and Use Taxes, Transportation Taxes, Fees, Passenger Facility Charges and Other Similar Government and Airport Charges and for Other Relief (the “Taxes Motion”).

## I. BACKGROUND

As set forth in detail in the Motions, the Debtor seeks the entry of orders authorizing the payment of the following prepetition claims (collectively, the “Prepetition Claims”): (i) certain prepetition claims of its employees, (ii) certain prepetition claims of foreign vendors, (iii) certain prepetition obligations related to the Debtor’s insurance policies and workers’ compensation programs, (iv) certain prepetition obligations relating to the assumption of various executory contracts vital to the operations of the Debtor’s business, (v) certain prepetition obligations related to the Debtor’s outside maintenance providers, (vi) certain prepetition obligations related to the Debtor’s fuel providers, (vii) certain prepetition obligations related to the Debtor’s customers, and (viii) certain prepetition obligations related to sales, use and other taxes.

Although the Debtor recognizes that the relief requested in the Motions should be granted in only limited circumstances, the Debtor submits that the payment of the Prepetition Claims is more than justified in this case. The relief requested in the Motions is critical to the Debtor’s survival in the immediate postpetition period and to its ability to reorganize successfully in the months that follow. The Debtor believes that the immediate payment of the Prepetition Claims is thus essential to its continuing business operations and that its very survival hinges upon making such payments in the ordinary course of its business. In

critical situations of the type described in the Motions, applicable law permits the Court to authorize the Debtor to make payments for prepetition claims.

Accordingly, for the reasons set forth in the Motions and this memorandum of law, the Debtor respectfully requests that this Court grant the relief requested in the Motions in their entirety.

## II. ARGUMENT

### A. **Courts Have Recognized a Debtor's Authority to Make Postpetition Payments of Critical Prepetition Claims Under the "Necessity of Payment" Doctrine**

This Court has ample authority to permit the payment of the Prepetition Claims discussed in the Motions. In a long line of cases dating back to the late 1800s, federal courts have consistently permitted postpetition payment of prepetition claims when necessary to preserve or enhance the value of a debtor's estate for the benefit of all creditors. *See, e.g., Miltenberger v. Logansport Ry. Co.*, 106 U.S. 286 (1882) (payment of pre-receivership claim prior to reorganizations permitted to prevent "stoppage of ... [crucial] business relations"); *Gregg v. Metropolitan Trust Co.*, 197 U.S. 183 (1905) ("the payment of the employees of the [rail]road is more certain to be necessary in order to keep it running than payment of any other class of previously incurred debt"); *In re Chateaugay Corp.*, 80 B.R. 279 (S.D.N.Y. 1987) (approving lower court order authorizing debtor prior to plan to pay prepetition wages, salaries, expenses and

benefits), *appeal dismissed*, 838 F.2d 59 (2d Cir. 1988); *In re Ionosphere Clubs, Inc.*, 98 B.R. 174, 175-76 (Bankr. S.D.N.Y. 1989) (courts have the power “to authorize a debtor in a reorganization case to pay prepetition claims where such payment is essential to the continued operation of the debtor”); *In re Gulf Air, Inc.*, 112 B.R. 152, 153 (Bankr. W.D. La. 1989) (payment of prepetition wages, benefits and expenses permitted to “safeguard against loss of going-concern values”).

The postpetition payment of prepetition claims has generally been allowed under the “doctrine of necessity,” also referred to as the “necessity of payment” principle. The statutory basis of the “doctrine of necessity” is section 105 of title 11 of the United States Code (the “Bankruptcy Code”), which provides as follows:

The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.

11 U.S.C. §105(a).

The purpose of section 105(a) of the Bankruptcy Code, which codifies the bankruptcy courts’ inherent equitable powers, is to “assure the bankruptcy courts power to take whatever action is appropriate or necessary in aid of the exercise of their jurisdiction.” 2 Collier on Bankruptcy ¶ 105.01[1] (15th ed. 2002).

Based on the bankruptcy courts' equitable powers, the "doctrine of necessity" principle has been explained as "permit[ting] immediate payment of claims of creditors where those creditors will not supply services or material essential to the conduct of the business until their pre-reorganization claims shall have been paid"). *In re Penn Central Transportation Co.*, 467 F.2d 100 at 102 (3d Cir. 1972). Under this doctrine, the immediate payment of prepetition claims may be authorized where the payments are essential to the debtor's continued business operations. *See, e.g., In re Columbia Gas System Inc.*, 171 B.R. 189, 191-92 (Bankr. D. Del. 1994); *In re SIS Corp.*, 108 B.R. 608, 609-10 (Bankr. N.D. Ohio 1989) (recognizing that payments on account of prepetition claims may be authorized by a court "premised upon overriding practical and policy reasons"). For example, in discussing the "necessity of payment" principle in *In re Lehigh & N.E.R. Co.*, 657 F.2d 570 (3d Cir. 1981), the Court stated:

[T]he "necessity of payment" doctrine ... teaches no more than, if payment of a claim which arose prior to reorganization is essential to the continued operation of the railroad during reorganization, payment may be authorized even if it is made out of corpus. [Citations omitted.]

*Id.* at 581.

Although the Ninth Circuit has in one instance (and only in dicta) read the necessity of payment rule narrowly in *In re B & W Enters., Inc.*, 713 F.2d 534, 537 (9th Cir. 1983) (stating, in dicta, that the necessity of payment rule relates only to

railroad reorganization cases), that Court and other courts in this Circuit have since acknowledged that unequal treatment of prepetition debt is permitted in order to preserve a debtor's potential for rehabilitation and has approved the payment of prepetition claims when such payment is vital to a debtor's continued operations. Indeed, in *In re Adams Apple, Inc.*, 829 F.2d 1484, 1490 (9th Cir. 1987), the Court of Appeals for the Ninth Circuit subsequently recognized that the policy of equal treatment of creditors may be superseded when it conflicts with the policy of rehabilitation of a debtor. This Court stated that:

Cases have permitted unequal treatment of pre-petition debts when necessary for rehabilitation, in such contexts as (i) prepetition wages to key employees; (ii) hospital malpractice premiums incurred prior to filing; (iii) debts to providers of unique and irreplaceable supplies; and (iv) peripheral benefits under labor contracts.

*Id.* at 1490.

The relief that the Debtor seeks through the Motions is fully justified under the “doctrine of necessity,” as further described below, since the Debtor’s prompt payment of the Prepetition Claims is crucial to the preservation and protection of its assets and business, and ultimately to its successful reorganization.

**B. The Debtor Requests Authority to Make Postpetition Payments of Prepetition Claims Essential to Its Ongoing Business Operations And to the Success of Its Reorganization Efforts**

Below is a description of the various categories of Prepetition Claims which the Debtor is seeking authorization to pay pursuant to the Motions.

1. Employees' Prepetition Claims

This Court should allow the Debtor to pay prepetition employees' claims as requested in the Employees Motion because: (i) the bulk of such payments are entitled to priority pursuant to sections 507(a)(3) and 507(a)(4) of the Bankruptcy Code and will be paid eventually under any plan of reorganization, (ii) the continued allegiance and effort of the Debtor's employees is pivotal to the success of the Debtor's reorganization, and (iii) the Debtor may otherwise be deemed in violation of section 1113(f) of the Bankruptcy Code.

Section 507(a)(3) of the Bankruptcy Code<sup>1</sup> creates third-tier priority for precisely the type of employee's compensation the Debtor seeks to pay and section 507(a)(4) of the Bankruptcy Code<sup>2</sup> grants fourth-tier priority to unsecured claims for contributions to employee's benefit plans. The Debtor submits that the majority of the prepetition compensation and benefit payments that the Debtor

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<sup>1</sup> Section 507(a)(3) of the Bankruptcy Code provides, in part, that: "the following expenses and claims have priority in the following order: ... (3) Third, allowed unsecured claims, but only to the extent of \$4,650 for each individual . . . earned within 90 days before the date of the filing of the petition . . . for— (A) wages, salaries, or commissions, including vacation, severance, and sick leave pay earned by an individual." 11 U.S.C. §507(a)(3).

<sup>2</sup> Section 507(a)(4) of the Bankruptcy Code provides, in part, that: "the following expenses and claims have priority in the following order: ... (4) Fourth, allowed unsecured claims for contributions to an employee benefit plan — (A) arising from services rendered within 180 days before the date of the filing of the petition . . . ; but only (B) for each such plan, to the extent of — (i) the number of employees covered by each such plan multiplied by \$4,650; less (ii) the aggregate amount paid to such employees under paragraph (3) of this section, plus the aggregate amount paid by the estate of such employees to any other employee benefit plan." 11 U.S.C. §507(a)(4).

seeks to make pursuant to the Employees Motion are granted priority pursuant to sections 507(a)(3) and 507(a)(4) of the Bankruptcy Code and thus will be paid under any plan of reorganization. *See* 11 U.S.C. § 1129(a)(9)(B). Given the importance of the employees' retention and support to the reorganization of the Debtor's business, and since the Debtor will pay such Prepetition Claims eventually, the Debtor submits that this Court should authorize the immediate payment of such claims.

To the limited extent that the prepetition payments the Debtor seeks to make pursuant to the Employees Motion are not covered by sections 507(a)(3) or 507(a)(4) of the Bankruptcy Code, this Court should nonetheless allow the Debtor to make those payments pursuant to the doctrine of necessity. As specifically stated by the Court of Appeals for the Ninth Circuit in *Adams Apple*, "cases have permitted unequal treatment of prepetition debts when necessary for rehabilitation, in such contexts as (i) prepetition wages to key employees . . . and (iv) peripheral benefits under labor contracts."

Further, bankruptcy courts within the Ninth Circuit have routinely granted the relief requested in the Employees Motion. *See, e.g., In re Washington Group International, Inc.*, Case No. 01-31627 (GWZ) (Bankr. D. Nev. May 14, 2001); *In re Liberty House, Inc.*, Case No. 98-01039 (LK) (Bankr. Haw. Mar. 20, 1998); *In re Pacific Gas and Electric Company*, Case No. 01-30923 (DM) (Bankr. N.D. Cal.

Apr. 16, 2001); *In re Fountain View, Inc.*, Case No. 01-39678 (BB) (Bankr. C.D. Cal. Oct. 3, 2001); *In re Health Plans of the Redwoods*, Case No. 02-11358 (AJ) (Bankr. N.D. Cal. Jul. 5, 2002); *In re AgriBioTech, Inc.*, Case No. 00-10533 (LBR) (Bankr. D. Nev. Jan. 26, 2000); *In re National Airlines, Inc.*, Case No. 00-19258 (LBR) (Bankr. D. Nev. Dec. 6, 2000); *In re Crown Vantage, Inc.*, Case No. 00-41584 (RJN) (Bankr. N.D. Cal. Mar. 16, 2000).

Numerous courts in other circuits have also recognized a bankruptcy court's ability to allow payment of prepetition wages and benefits, irrespective of statutory priorities, where such payments are in the best interests of the estate. *See, e.g., In re Crafts Precision Indus., Inc.*, 244 B.R. 178, 183 (1st Cir. B.A.P. 2000) (vacation payments that did not qualify under section 507 of the Bankruptcy Code "approved pursuant to section 105, irrespective of them being non-priority obligations" because there existed a "substantial risk" of employee defection absent payment); *In re Miller Mining, Inc.*, 219 B.R. 219, 223 (Bankr. N.D. Ohio 1998) ("This Court often permits the payment of prepetition wages so that the debtor-in-possession may maintain an effective work force"); *In re Sharon Steel Corp.*, 159 B.R. 730, 736-37 (Bankr. W.D. Pa. 1993) (upholding authorization of prepetition wages where necessary to avert serious threat to chapter 11 process); *In re Chateaugay Corp.*, 80 B.R. 279, 287 (Bankr. S.D.N.Y. 1987) (allowing payment of certain prepetition workers' compensation claims; "[a] rigid application of the priorities of

section 507 would be inconsistent with the fundamental purpose of reorganization and of the Act's grant of equity powers to bankruptcy courts, which is to create a flexible mechanism that will permit the greatest likelihood of survival of the debtor and payment of creditors.”

If prepetition wages, salaries and contributions to the employees' benefit plans are not made, the Debtor's employees will suffer personal hardship, which will devastate the Debtor's ability to efficiently reorganize since the Debtor's business is principally people-oriented. Further, if the Debtor fails to pay to its employees all amounts owed in connection with such employees' salary, wage and benefits, the Debtor will be in breach of its collective bargaining agreements with the various unions representing the Debtor's employees.<sup>3</sup> Some courts have held that the failure by a debtor to pay its obligations under its collective bargaining agreements amounted to a modification of such agreements in violation of section 1113(f) of the Bankruptcy Code. *See In re Unimet Corp.*, 842 F.2d 879 (6<sup>th</sup> Cir. 1988). In light of the foregoing, this Court should allow the Debtor to pay certain prepetition wages, expenses and benefit obligations in accordance with the policies, plans and programs that were in place before the Debtor filed for Bankruptcy, as further described in the Employees Motion.

## 2. Foreign Vendors Prepetition Claims

In connection with (i) its flight service in foreign locations such as Pago Pago, American Samoa and Papeete, Tahiti, and (ii) several sales agents of the Debtor established in Tokyo, Japan, the Debtor makes certain payments to various foreign vendors and service providers in the ordinary course of its business. The prompt payment of the Debtor's prepetition obligations to such foreign creditors is absolutely crucial to the preservation and protection of the Debtor's estate, and ultimately to its successful reorganization, since the Debtor's foreign operations represent a significant part of its business. The payment to the foreign creditors will contribute significantly to the Debtor's revenue-generating capability by enabling the Debtor to provide a high level of service and to retain the confidence and goodwill of its customers and foreign suppliers. Without continued services in foreign locations, the Debtor's international operations may shut down, thus jeopardizing the Debtor's efforts to successfully reorganize and emerge from chapter 11 expeditiously.

Further, if the Debtor's prepetition obligations to foreign creditors are not satisfied, such creditors could take actions that could severely disrupt the Debtor's operations. For example, the foreign creditors may argue that they are not subject to the jurisdiction of this Court and thus not subject to the automatic stay imposed

<sup>3</sup> In this chapter 11 case, more than 86% of the Debtor's employees are unionized.

by section 362(a) of the Bankruptcy Code. The foreign creditors also may sue the Debtor in foreign courts, obtain judgments against the Debtor, and thereafter seek to enforce such judgments against the Debtor's foreign assets. Based on the foregoing, the Debtor submits that the consequences of not paying its foreign creditors, as described in detail in the Foreign Vendors Motion, would be devastating to its business.

Courts in this Circuit have routinely granted authority to a debtor to pay prepetition claims of foreign vendors under the doctrine of necessity. *See, e.g., In re Lindemann Produce LLC*, Case No. 00-32672 (GWZ) (Bankr. D. Nev. Sep. 15, 2000); *In re Air Transport, LLC*, Case No. 98-30248 (GWZ) (Bankr. D. Nev. Feb. 9, 1998); *In re National Airlines, Inc.*, Case No. 00-19258 (LBR) (Bankr. D. Nev. Dec. 6, 2000).

As stated above, certain foreign entities provide vital services to the Debtor's operations and payment of such foreign entities is necessary for the Debtor to operate abroad. Accordingly, the Debtor respectfully submits that payment to its foreign vendors, as described in the Foreign Vendors Motion, is necessary and in the best interests of the Debtor's estate and creditors and, therefore, should be allowed by this Court under the "doctrine of necessity."

### 3. Prepetition Payments for Insurance and Workers' Compensation Programs

It is essential to the continued operation of the Debtor's business and its efforts to reorganize that all its insurance policies be maintained on an ongoing and uninterrupted basis. Any failure to pay insurance premiums when due may affect the Debtor's ability to renew its insurance policies. If such insurance policies are allowed to lapse, the Debtor could be exposed to substantial liability for damages resulting to persons and property of the Debtor and others, which exposure could have an extremely negative impact on the Debtor's ability to reorganize successfully. The maintenance of the Debtor's workers' compensation programs is also vital to the Debtor, as applicable state law mandates such coverage. Further, the risk that claimants under the Debtor's workers' compensation programs will not receive timely payments with respect to employment-related injuries could have a devastating effect on the financial well-being and morale of the Debtor's employees and their willingness to remain in the Debtor's employ and support its reorganization. Therefore, it is critical that the Debtor continue to maintain its insurance policies and its workers' compensation programs and be permitted to pay any obligations in the ordinary course of business in accordance with its prepetition practices.

Bankruptcy courts in this Circuit have routinely granted the relief requested in the Insurance Motion to other debtors in major chapter 11 cases. *See, e.g., In re Crown Vantage, Inc.*, Case No. 00-41584 (RJN) (Bankr. N.D. Cal. Mar. 16, 2000);

*In re AgriBioTech, Inc.*, Case No. 00-10533 (LBR) (Bankr. D. Nev. Jan. 26, 2000); *In re National Airlines, Inc.*, Case No. 00-19258 (LBR) (Bankr. D. Nev. Dec. 7, 2000); *In re Pacific Gas & Electric Co.*, Case No. 01-30923 (DM) (Bankr. N.D. Cal. Apr. 6, 2001); *In re Washington Group International, Inc.*, Case No. 01-31627 (GWZ) (Bankr. D. Nev. May 14, 2001).

Accordingly, the Debtor submits that payment under the insurance policies and the workers' compensation programs, as described in the Insurance Motion, should be allowed by this Court under the "doctrine of necessity."

4. Prepetition Payments for Executory Contracts

The Debtor is party to numerous code share agreements, global distribution systems agreements, multi-host agreements, travel agency agreements and ATPCO agreements, as more fully described in the Executory Contracts Motion. Each of these agreements is essential to the Debtor's business. If the Debtor were to lose the relationships established and governed by these agreements, its revenue would suffer and its ability to continue to operate within the airline industry and, thus, reorganize, would be in jeopardy. The Debtor believes that if it does not have the ability to pay prepetition obligations relating to these agreements in the ordinary course of business, the counterparties to such agreement may not have any incentive to continue to provide services to the Debtor or may attempt unilateral self-help measures to protect their interests. Regardless of whether such actions

are legally proper, any disruption in the Debtor's business, even for a short time, could be catastrophic.

Similar relief as requested herein has been granted in this Circuit and other Circuits in other airline cases. *See, e.g., In re U.S. Airways Group, Inc.*, Case No. 02-83984 (SSM) (Bankr. E.D. Va. Aug. 12, 2002 and Sep. 5, 2002); *In re Trans World Airlines, Inc.*, Case No. 01-00056 (PJW) (Bankr. D. Del. Jan. 10, 2001); *In re Trans World Airlines, Inc.*, Case No. 92-115 (Bankr. D. Del. Jan. 31, 1992); *In re America West Airlines, Inc.*, Case No. 91-07505-PHXRGM (Bankr. D. Ariz. Jun. 27, 1991); *In re Pan Am Corp.*, Case Nos. 91 B 10080-10087 (Bankr. S.D.N.Y. Jan. 29, 1991); *In re Continental Airlines, Inc.*, Case Nos. 90-932-980 (Bankr. D. Del. Dec. 28, 1990).

Accordingly, it is essential that the Debtor be given authority by this Court to pay its prepetition obligations in connection with the agreements described in the Executory Contracts Motion in the ordinary course of business.

#### 5. Outside Maintenance Providers Prepetition Claims

It is essential that the Debtor pay certain prepetition obligations to its outside maintenance providers, as further described in the Maintenance Providers Motion, to ensure that they will provide the required maintenance and overhauls for the Debtor's fleet of aircraft and aircraft components, which will enable the Debtor to satisfy its paramount concern – the safety of its passengers. Only by maintaining

the highest levels of safety can the Debtor provide a high level of service and retain the confidence, support, and goodwill of the flying public. Moreover, it is essential that the Debtor pay such prepetition claims to ensure that the Debtor's fleet is maintained and serviced in a timely fashion. Planned maintenance for aircraft is scheduled months ahead of time both internally at the Debtor's facilities and with certain of outside maintenance providers. It is important to the Debtor's successful operations that this planned maintenance schedule not be disrupted. Any disruption could impair the Debtor's operation and lower confidence in the Debtor's safety record. Furthermore, any disruption could also impair the Debtor's ability to comply with FAA maintenance regulations, with which the Debtor is required to comply as a debtor in possession.

Unless the Debtor's outside maintenance providers and shippers are paid promptly, they may refuse to redeliver the Debtor's aircraft, engines, and other equipment vital to its operations. In addition, if certain of the Debtor's contractors' prepetition claims, as described in the Maintenance Providers Motion, are not paid, such contractors may refuse to continue their maintenance of the Debtor's facilities or complete work on ongoing projects. Finally, "on-call" outside maintenance providers who provide services at the Debtor's destination cities also must be paid to avoid a disruption in repair and maintenance services needed to continue the Debtor's operations safely and successfully.

Similar relief has been granted by courts in this Circuit and other Circuits. *In re Liberty House, Inc.*, Case No. 98-01039 (Bankr. D. Haw. Mar. 20, 1998) (order authorizing payment of prepetition claims of certain service providers including shipping service providers); *In re America West Airlines, Inc.*, Case No. 91-07505-PHXRGGM (Bankr. D. Ariz. Jun. 27, 1991) (interim order authorizing payment or honoring of approximately \$18 million of prepetition claims of outside mechanics and repairmen); *In re UAL Corporation, Inc.*, Case No. 02-48191 (Bankr. N.D. Ill. Dec. 11, 2002) (interim order authorizing payment of prepetition claims of certain outside maintenance providers, shippers, and construction contractors of approximately \$36 million); *In re US Airways Group, Inc.*, Case No. 02-83984 (Bankr. E.D. Va. Aug. 12, 2002) (order authorizing payment of prepetition claims of certain outside maintenance providers, shippers, and construction contractors of approximately \$13 million).

It is therefore in the best interests of the Debtor's estate, creditors and other parties in interest for the Debtor to be authorized by this Court to pay the prepetition claims of its outside maintenance providers, shippers, and contractors as described in the Maintenance Providers Motion in the ordinary course of the Debtor's business.

## 6. Fuel Suppliers Prepetition Claims

As previously stated, in *Adams Apple*, the Ninth Circuit stated that:

Cases have permitted unequal treatment of prepetition debts when necessary for rehabilitation, in such contexts as ... (iii) debts to providers of unique and irreplaceable supplies....

*Id.* at 1490.

The relief sought by the Debtor through the Fuel Providers Motion should be granted under the “doctrine of necessity.” The Debtor submits that its agreements with its fuel suppliers, its storage providers, the Fuel Consortia and its into-plane contractors, as fully described in the Fuel Suppliers Motion, are critical to its reorganization efforts, and that without these arrangements, the Debtor would have inadequate access to fuel and no infrastructure to distribute or receive its fuel. If the Debtor cannot distribute or receive its fuel, the Debtor’s domestic and international operations will be shut down, since without fuel, the Debtor cannot operate its planes.

Courts in this jurisdiction have authorized payment to vital suppliers under similar circumstances. *See, e.g., In re Liberty House, Inc.*, Case No. 98-01039 (Bankr. D. Haw. Mar. 20, 1998) (order authorizing payment of prepetition claims of certain service providers including shipping service providers under the “necessity of payment” doctrine); *In re Liberty House, Inc.*, Case No. 98-01039 (Bankr. D. Haw. Mar. 20, 1998) (order authorizing payment of prepetition claims of certain operators of leased and licensed departments under the “necessity of

payment” doctrine). Therefore, this Court should grant the Debtor’s request to pay such critical fuel suppliers.

7. Customers Prepetition Claims

The relief requested in the Customers Motion is also supported by the “necessity of payment” doctrine because the customer programs, as fully described in the Customers Motion, are necessary to maintain the continuity of the Debtor’s business. The Debtor submits that in order to maintain its ongoing business relationships with its customers, the Debtor must (a) honor all tickets that were purchased prepetition, (b) honor its obligations under its frequent flyer program and (c) honor all prepetition barter arrangements the Debtor entered into for the sponsorship of corporate and sporting events and other promotional services. Since the loyalty and continued patronage of the Debtor’s customers is critical to the Debtor’s financial health and reorganization efforts, the Debtor submits that all customers programs must be maintained and operated in the ordinary course of business.

The relief requested in the Customers Motion has been approved by courts in this District and other Districts. *See, e.g., In re Liberty House, Inc.*, Case No. 98-01039 (LK) (Bankr. Haw. Mar. 3, 1998); *In re Hawaiian Airlines, Inc.*, Case No. 93-01074 (LK) (Bankr. Haw. Sep. 21, 1993); *In re UAL Corporation, Inc.*,

Case No. 02-48191 (Bankr. N.D. Ill. Dec. 9, 2002); *In re US Airways Group, Inc.*, Case No. 02-83984 (SSM) (Bankr. E.D. Va. Aug. 11, 2002); *In re Kmart Corp.*, Case No. 02-02474 (SPS) (Bankr. N.D. Ill. Jan. 25, 2002); *In re Humpheys Inc.*, Case No. 01-13742 (REG) (Bankr. N.D. Ill. Apr. 18, 2001) (order authorizing debtor to honor certain prepetition obligations to customers and to otherwise continue in the ordinary course of business Customer Programs and practices); *In re Linc Capital, Inc.*, Case No. 01-03320 (JBS) (Bankr. N.D. Ill. Mar. 2, 2001).

Based on the foregoing, the Debtor respectfully requests that this Court grant the relief requested in the Customers Motion.

#### 8. Prepetition Tax Claims

The payment of taxes to all taxing authorities is necessary to the Debtor's successful reorganization. It is in the best interest of the Debtor's estate that all taxes, as fully described in the Taxes Motion, be paid on time so as to avoid administrative difficulties. The Debtor submits that a significant portion of the taxes that it owes to the taxing authorities are so-called "trust fund" taxes, which are required to be collected from third parties and held in trust for payment to such taxing authorities. Such "trust fund" taxes are not property of the Debtor's estate under section 541(d) of the Bankruptcy Code and the Debtor, therefore, has no equitable interest in such taxes. *See, e.g., Begier v. I.R.S.*, 496 U.S. 53 (1990) (taxes such as excise taxes, FICA taxes and withholding taxes are property held by

debtor in trust for another and, as such, do not constitute property of the estate); *In re Al Copeland Enters., Inc.*, 133 B.R. 837 (Bankr. W.D. Tex. 1991), *aff'd*, 991 F.2d 233 (5th Cir. 1993) (debtor obligated to pay state sales taxes plus interest because such taxes were “trust fund” taxes). Further, a precautionary withholding of the payment of the taxes likely would cause the taxing authorities to take precipitous action, including, but not limited to, a marked increase in state audits and a flurry of lien filings. Prompt and regular payment of the taxes will avoid this unnecessary governmental action. Moreover, the above-described taxes may be entitled to priority status under section 507(a)(8) of the Bankruptcy Code. The Debtor’s payment of all taxes will thus affect only the timing of the payments and not the amounts to be received by the taxing authorities.

Courts in this District and in other Districts have routinely granted the same or similar relief to chapter 11 debtors. *See, e.g., In re Air Transport International, LLC*, Case No. 98-30248 (GWZ) (Bankr. D. Nev. Feb. 10, 1998); *In re Einstein/Noah Barrel Corp.*, Case Nos. 00-0447-ECF-CGC and 00-0448-ECF-CGC (Bankr. D. Ariz. Apr. 28, 2000).

Accordingly, the Debtor submits that the payments described in the Taxes Motion should be allowed by this Court under the “doctrine of necessity.”

### **III. CONCLUSION**

Under the “necessity of payment” doctrine, the Debtor’s selective payment of the Prepetition Claims is warranted. As described briefly above and as demonstrated in detail in each of the respective Motions, authority to pay such claims is essential to the Debtor’s ongoing business operations and, ultimately, to the success of its reorganization efforts. Further, the “necessity of payment” doctrine is one of several legal grounds pursuant to which the relief requested in the Motions may be granted.

If the requested relief is not granted, however, there is a substantial risk that the Debtor’s business operations would be significantly - and perhaps irreparably - undermined. If the Motions are denied, the Debtor’s business may fail - to the benefit of no party - before the Debtor has the opportunity even to attempt reorganization. At the outset of these bankruptcy proceedings, it is especially important for the Debtor to maintain a “business as usual” atmosphere to ensure the smooth and uninterrupted operation of its business. The Debtor, therefore, respectfully requests that this Court authorize the Debtor to pay immediately the Prepetition Claims, since such payment is critical to the success of its reorganization efforts.

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Honolulu, Hawaii

Respectfully submitted,

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